

# AIRDRIE ACADEMY

## Higher Business Management



## Understanding Business Notes

curriculum for excellence



## Key areas for revision:

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## Factors of Production

In order to produce goods and services, businesses need to use resources.

These resources are the **inputs** for business activity, with the goods and services that they produce being the **outputs**.

**Land** – This is all the natural resources such as **oil, water** and the **land** itself. Anything that can be extracted from the land and sea. Also includes sunshine which is used with solar panels to create energy.

**Labour** – All organisations need **people** to work for them. It includes all their physical and mental effort.

**Capital** – These are the man-made resources. This is not money but **machines, lorries, tools** etc. They have all been created or produced from natural resources, and are needed to produce goods and services.

**Enterprise** – This could be described as the most important factor of production because, without it, production would not take place.

The entrepreneur is the person who brings together all the other resources and takes the risks to produce the goods or services.



## Wealth Creation

Entrepreneurs combine the **Factors of Production** to produce goods or services.

While all four factors must be present, the importance, or contribution, of each will depend upon what is being provided. At every stage of the production process, **value** is added and therefore more wealth is created. **Wealth Creation** occurs because the good or service is improved during each stage of production making that item more valuable.

## What is an Entrepreneur?

An entrepreneur is the person who brings together the factors of production. The person with the idea, the person who drives forward the business from dream to reality.

Richard Branson is a very good example of an entrepreneur. An entrepreneur is a person who has the ability to, among other things, identify a gap in the market for product or a service. Twenty years ago mobile phones did not exist. Can you imagine if you had been able to spot the gap in the market for a small personal communication device (i.e. a mobile phone)?

## **Role of the Entrepreneur**

In such circumstances it is not necessarily the entrepreneur who has the technical skills to develop the product. This is not really important. He/she will be able to hire the appropriate personnel with the right technical skills to develop the product. Indeed, entrepreneurs are not usually inventors. Henry Ford did not invent the automobile, but he mass produced his cars and took the industry to a new level of demand.

It is the entrepreneur who can assess the commercial viability of any new business idea. In essence is it worth doing? How much money will I make? Is it worth taking the risk? They are the ones who develop the business idea and by receiving financial backing or ploughing in their own money they can start the business. It is the entrepreneur who can organise the factors of production (e.g. land, labour and capital) in a productive and effective manner to make a product or service, which people want to buy.

## **Personal Qualities**

Entrepreneurs have certain personal attributes e.g. ability to sell themselves and their ideas, ability to organise resources, ability to read situations and make the right decisions. They are often noted for their drive, enthusiasm and creativity. Above all they are risk-takers, sometimes gambling with their life savings as well as their financial backers money!

Entrepreneurs have it all to gain, but at the same time they have it all to lose. True entrepreneurs are not afraid of failure. They only see their vision and their goal.

Successful entrepreneurs like Bill Gates (who created Windows Operating System used by almost every PC in the world!) can become billionaires. Failures like John DeLorean (of DMC) end up bankrupt and broken.

## Sectors of Industrial Activity



### Primary Sector

Businesses that are involved in exploiting or extracting the natural resources (e.g. farming, mining, fishing and oil exploration)

### Secondary Sector

Businesses that are involved in manufacturing and construction. They take the natural resources produced in the primary sector and change them into things we can use (eg car manufacture, building firms.)



### Tertiary (services) Sector

Businesses that are involved in providing services rather than goods, such as banking and tourism.



All economies start out in the primary sector, and as an economy grows it moves through each of the sectors. This process is called **de-industrialisation**, which the Scottish economy has gone through during the last 30 years.

### Quaternary Sector



Businesses are involved in providing information services, such as computing, ICT, consultancy and R&D (research, particularly in scientific fields).

The quaternary sector is sometimes included within the tertiary sector, as they are both service sectors.

All economies start out in the primary sector, and as an economy grows it moves through each of the sectors. This process is called **de-industrialisation**, which the Scottish economy has gone through during the last 30 years.

## Sole Traders



A sole trader describes any business that is owned and controlled by one person, although they may employ workers. This could be a newsagent's shop, for example. Individuals, who provide a specialist service like hairdressers, plumbers or photographers, are also sole traders. Sole traders do not have a separate legal existence. As a result, the owners are personally liable for the firm's debts, and may have to pay them out of their own pocket. This is called unlimited liability.

### Advantages

- The firms are usually small, and easy to set up.
- Generally, only a small amount of capital needs to be invested, which reduces the initial start-up cost.
- The wage bill will usually be low, because there are a few or no employees.
- It is easier to keep overall control, because the owner has a hands-on approach to running the business and can make decisions without consulting anyone else.

### Disadvantages

- The sole trader has no one to share the responsibility of running the business with. A good hairdresser, for example, may not be very good at handling the accounts.
- Sole traders often work long hours and find it difficult to take holidays, or time off if they are ill.
- Developing the business is also limited by the amount of capital personally available.
- There is also the risk of unlimited liability, where the sole trader can be forced to sell personal assets to cover any business debts.

## Partnerships



Partnerships are businesses owned by two or more people. A contract called a deed of partnership is normally drawn up. This states the type of partnership it is, how much capital each has contributed, and how profits and losses will be shared. Doctors, dentists and solicitors are typical examples of professionals who may go into partnership together. They can benefit from shared expertise, but like the sole trader, have unlimited liability.

### Advantages

- The main advantage of a partnership over a sole trader is shared responsibility. This allows for specialisation, where one partner's strengths can complement another's. For example, if a hairdresser were in partnership with someone with a business background one could concentrate on providing the salon service, and the other on handling the finances.
- More people are also contributing capital, which allows for more flexibility in running the business.
- There is less pressure of time on individual partners.
- There is someone to consult over business decisions

### Disadvantages

- The main disadvantage of a partnership comes from shared responsibility.
- Disputes can arise over decisions that have to be made, or about the effort one partner is putting into the firm compared with another.
- The distribution of profits can cause problems. The deed of partnership sets out who should get what, but if one partner feels another is not doing enough, there can be dissatisfaction.
- A partnership, like a sole trader, has unlimited liability.

## **Private Limited Company (Ltd)**

The capital of a company is divided into shares – each member or shareholder owns a number of these shares. The company must have a minimum of 2 shareholders. Limited companies are run by a Board of Directors who are appointed by the shareholders. Limited Companies must complete 2 documents – the *Memorandum of Association* and *Articles of Association* – these set out the aims of the business and how it will be run and financed. The company must register with the Registrar of Companies.

- A private limited company (Ltd) is not allowed to offer shares to the public through the stock exchange.
- Limited liability means investors (shareholders) do not risk personal bankruptcy. A company is treated as a separate legal entity from its owners. Thus a company can own assets, employ people and be sued. Just as one person cannot be held responsible for the debts of another, so owners of a company cannot be forced to pay the company's debts.
- A measure of privacy can still be retained – private companies are not obliged to publish their annual reports or issue a prospectus to members of the public if requested.

## **Public Limited Company (PLC)**

A PLC is generally a large company – it must have a minimum of £50,000 share capital. The shares of PLCs can be bought and sold on the stock exchange – large amounts of capital can be raised by selling shares to investors. PLCs must also complete a *Memorandum of Association* and *Articles of Association*. PLCs must also be registered with the Registrar of Companies.

- Shareholders are entitled to limited liability.
- Knowledge that shares in public limited companies can be resold on the Stock Exchange if required encourages people to invest.
- Huge sums of capital can be raised from individuals and institutional investors such as Pension Funds and Insurance Companies.
- All the above mean financial stability for the company which enable it to develop and expand.

### ***Disadvantages***

- Members of the public can examine financial information about companies which is lodged with the Registrar of Companies. PLCs have to make more information available to the public than private limited companies – for example, they must publish Annual Reports.
- PLCs may grow so large that they become inflexible and difficult to manage



effectively.

- In very large companies employees may feel out of touch ('alienated') from those at the top and it may be difficult to take a personal approach to customer service.
- The legal procedures necessary to set up companies, especially PLCs, can be very costly.

Examples of public limited companies include Legal & General plc, Marks and Spencer plc, Manchester United plc and the Boots Company plc.

## **Multi-national Corporations**

Many large PLCs operate as **multi-national corporations**. Multi-national corporations have branches (called *subsidiaries*) in more than one country. Many companies establish sales outlets for their products in various countries. However, the distinguishing feature of an MNC is that it sets up **production facilities** in more than one country. British multi-nationals include BP and ICI. MNCs are major employers in many countries.

Reasons for establishing MNCs:

- Increase market share.
- Secure cheaper premises and labour.
- Avoid or minimise the amount of tax which has to be paid.
- Take advantage of government grants available.
- Save on costs of transporting goods to the market place.
- Avoid trade barriers like the EU Common External Tariff.
- Enable their products to be sold globally without having to rely on other companies to sell them in some areas, under licence.

Disadvantages of MNCs for the host country:

- They can be very powerful – some of them earn more than some small countries in the course of a year – and can therefore exert quite a strong influence on the governments of host countries – for example, by threatening to close down their operations there.
- They can be accused of exploiting labour in low wage countries.
- They may use up non-renewable resources in the host country.
- Because they are so powerful and able to take advantage of economies of scale, they may force local firms out of business.
- Profits go back to the parent company – in which ever country it has its headquarters.
- All the major functions tend to remain at headquarters so that, in times of difficulty, it is relatively easy for the MNC to close down a subsidiary causing many job losses.

Examples of multinational include: Nike, Coca-Cola, Wal-Mart, AOL, Toshiba, Honda and BMW.

## **What is Globalization?**

Globalization is a term used to refer to the expansion of economies beyond national borders, in particular, the expansion of production by a firm to many countries around the world, i.e., globalization of production, or the "global assembly line." This has given transnational corporations power beyond nation-states, and has weakened any nation's ability to control corporate practices and flows of capital, set regulations, control balances of trade and exchange rates, or manage domestic economic policy. It has also weakened the ability of workers to fight for better wages and working conditions from fear that employers may relocate to other areas.

### **Pro-Globalization**

An old Chinese proverb has been used many times to indicate the good side of globalization; **"Give a man a fish and you feed him for a day, teach a man to fish and you feed him for a lifetime."**

### **Globalization:**

- Helps the world's poorest countries become globally integrated and positions them for greater growth in the 21st century.
- Is good for consumers as long as it causes global competition helping us gain fair prices.
- Should bring a better life for those people living in LEDC countries.
- Provides a greater share of wealth throughout the world.

### **Economically:**

- Increase in international trade at a much faster rate than the growth in the world economy.
- Increase in international flow of capital including foreign direct investment.
- Creation of international agreements leading to organizations like the WTO and economic cartels such as OPEC.
- Development of global financial systems.
- Increased role of international organisations such as WTO, WIPO, IMF that deal with international transactions.
- Increase of economic practices like outsourcing and offshoring by multinational corporations.

## **Anti-Globalization**

It indeed does optimize economic output under ideal conditions. However, there are important factors which make the situation less than ideal:

- Disruption of distribution or communications paths.
- Restrained flow of labour.
- The theory mostly addressed output (goods and services); ignoring job availability, stability, bubble risk, and other important factors.
- Past trends may not be indicative of future trends.
- Distribution of the benefits of free trade can be very uneven.
- Some countries are more interested in military advancement than in consumer prices, and subsidize certain specialties.

Some countries sacrifice benefits, retirement programs, safety, environmental safeguards, and human rights to achieve low labour rates. In other words they scorch both people and planet to "beat us".

## **Co-Operative Businesses**

Co-operative businesses are owned and run by and for their members, whether they are customers, employees or residents. Co-operatives are not about making big profits for shareholders, but creating value for customers

### **Examples:**

The Co-Op  
John Lewis

John Lewis offers every permanent member of staff a share of profits and a say in how the organisation is run through staff committees and democratic debating forums.

## Franchise

Businesses run by one firm under the name of another. The franchiser gives the franchisee a licence permitting them to sell goods or services under the franchiser's brand name, usually in return for a share of the franchisee's profits. The franchisee's licence permits him/her to use the franchiser's name, publicity materials, decor, uniforms, etc.

Many individuals use franchising as a means of starting up their own business. There is less likelihood of failure as support and guidance is provided by the franchiser to the franchisee.

Businesses such as McDonald's operate some branches directly and others as franchises. Other examples of franchises: Kentucky Fried Chicken, the Body Shop and the British School of Motoring (BSM).

<b>Franchiser</b>	
<b><i>Advantages</i></b>	<b><i>Disadvantages</i></b>
It is a quick way to enter new geographical markets and the franchiser's name becomes better known as the business expands.	Franchisers are reliant on franchisees to maintain the image and 'good name' of the business.

<b>Franchisee</b>	
<b><i>Advantages</i></b>	<b><i>Disadvantages</i></b>
The new business can begin trading on the established reputation of the franchiser immediately.	A percentage of the profits has to be paid to the franchiser.
The franchisee has the advantage of a well-known brand name and back up service.	The franchiser may impose strict rules on the franchisees and restrict their ability to operate on their own initiative.
All franchisees can benefit from ideas generated by each of them. For example, when a McDonald's franchisee thought up the 'Egg McMuffin', the recipe was circulated to all the other franchisees and the product became very successful.	The franchisee's reputation and profitability depend in part on that of the franchiser and the performance of the other franchisees.

## Getting Started

Franchises can cost anything from a few thousand pounds for a mobile cleaning business to hundreds of thousands of pounds for a fast food franchise. Before you buy a franchise do your homework, write a business plan and carry out your own market research on your potential customers.

Speak to your bank. They will probably have a person who specialises in advising would-be franchisees.

You should look into the background of the franchisor. Find out how long the business been running, and how many franchises it has. Also check how successful its franchisees have been - have many failed?

You should also check into the support and training that you will receive. And look closely at the financial projections for your franchise. Make sure you are aware of the terms of your agreement, specifically how long you will have the franchise for, whether you'll have an option to renew it and what happens if you need to sell the business.

Never sign up without getting the agreement vetted by a lawyer. Make sure you speak to other franchisees - those suggested by the company, and others that you find by yourself. Ideally try to speak to a franchisee whose business failed.

### **Other Types of Franchise**

There are several different types of franchise. As well as complete packages, there are franchises like car dealerships where you might have a contract to sell a product without trading under the franchise name.

There are also franchises where self-employed distributors sell goods on behalf of manufacturers. They make commission on the number of items they sell, and employ other distributors to work for them.

### **People to Speak to**

The British Franchise Association publishes an information pack and a full list of its members. If your franchisor isn't a member, find out why not.

The BFA can also advise you on franchise exhibitions, which are a good place to see a variety of franchises.

McDonald's

McDonald's Franchisees go to Hamburger University to learn every aspect of the business. They sign an agreement for 20 years using the McDonald's franchise but they cannot have any other business interests.

## **Public-Sector Organisations**

The overriding aim of public-sector activity is to provide services thought necessary for the general public. It is often the case that public-sector organisations have to operate within an allocated budget.

### **Central Government**

Central Government control and provide people with essential services such as health (NHS) and defence (Army).

The Scottish Government is an example of central government. People are elected, voted in, to become Members of Scottish Parliament (MSPs) or politicians.

### **Local Government (Local Authorities)**

Scotland is made up of 32 local councils each responsible for providing services in their area. (The council we are in is Glasgow City) Local government is responsible for as housing, street lighting, refuse collection, education, leisure and recreation, and environmental health in the local area. Most of these activities are financed from receipts from council tax and grants from central government. Some local authority facilities such as local swimming pools are financed by charging users a fee.

In recent times there has been a trend to 'contract out' some local authority services, such as refuse collection and school meals. This means that private firms are invited to submit bids to the local authority for the right to run a particular service (called *competitive tendering*). It is argued that this will result in a more cost-effective service for the community because, unlike government-run enterprises, private firms have an incentive to keep costs low and efficiency high in order to survive and to maximise profits.

### **Public Corporation**

These are business organisations that provide goods and services to the public and are owned by everyone in the country. They are also known as National Industries. Their chairman and board of directors are chosen by the government and are accountable to a government minister who in turn is responsible to Parliament.

An example is the British Broadcasting Corporation (BBC).

## Public Goods

Public goods are services which must be provided collectively for two main reasons:

- **Non-excludability** - the goods cannot be confined to those who have paid for it.
- **Non-rivalry in consumption** - the consumption of one individual does not reduce the availability of goods to others.

Examples of pure public goods include flood control systems, street lighting and national defence. A flood control system, such as the Thames Barrier, cannot be confined to those who have paid for the service. Also, the consumption of the service by one household will not reduce its availability to others. If left to the free market mechanism, no public goods would be provided and, as a result, there would be a clear market failure. No individual consumer would pay for a product that could be consumed for free if another household decided to purchase it.

## Voluntary Organisations

These organisations have **different aims** from those of other private sector enterprises. They are 'not for profit' organisations and very often their reason for existing is to help a charitable cause in some way. Any proceeds they do make – is simply ploughed back into the charity. Thus profitability is not their main aim, but raising funds is a way of achieving their objective of helping certain causes or groups of people.

To be recognised officially as a charity, the organisation must have one or more of four main objectives:

- to relieve poverty.
- to advance education.
- to advance religion.
- to carry out activities beneficial to the community.

The Charity Commissioners are appointed by the government to regulate the activities of charities. They keep a Register of Charities. Recognised charities are given 'charitable status' which means that they are exempt from paying certain taxes, such as VAT.

Examples: Help the Aged, Save the Children, Barnardos, Oxfam.

## Objectives

An objective is a goal that needs to be achieved.

Objective	Description
<b><i>Maximising profit</i></b>	To the economist, the main aim of a business is to make as big a profit as possible. Certainly, in the long run, a business has to make some kind of profit in order to remain viable.
<b><i>Survival</i></b>	For some firms this is the over-riding goal. Small family firms may be more concerned about keeping the business safe from take-over by large enterprises than making enormous profits.
<b><i>Growth</i></b>	A business may have the objective of growth. Becoming larger may enable a business to take advantage of economies of scale and become more efficient through having lower costs.
<b><i>Maximising sales</i></b>	In many large companies, where ownership and control are separated so that the managers are not necessarily shareholders, the size of a manager's salary is linked to the annual turnover of the business. Thus a major aim of the management team in such businesses may be to generate as much sales revenue as possible.
<b><i>Managerial objectives</i></b>	Where ownership and control are separated (e.g. in a PLC), managers within a business may choose to pursue their own individual aims. These will vary depending on what individual managers wish to achieve. Among the aims which have been suggested are that managers will aim to have a lot of staff reporting to them; they will aim to have money to spend on perks (e.g. company cars); they will aim to get budgets to spend on projects which they believe will bring them prestige and status, e.g. expansion to new markets.
<b><i>Satisficing</i></b>	Instead of having an objective to make the maximum level of profits, a business may aim only to make a level of profit which is sufficient to keep all its stakeholders satisfied, e.g. enough to pay acceptable dividends to shareholders. Another way to describe this is to say that a business has the objective of making a satisfactory level of profit. This has been described as 'satisficing'. (This is particularly relevant to public sector organisations which have to operate within specific budget guidelines.)



<p><b><i>Creating a good reputation (corporate or social responsibility)</i></b></p>	<p>A firm may wish to improve its public image and hence its chances of survival and market growth by demonstrating <i>corporate responsibility</i> through measures such as sponsorship of worthy causes or a commitment to ecologically sound practices. Spending money on such public relations initiatives will diminish short-term profitability, but can help to boost the chances of survival in the long term. Activities by pressure groups such as Greenpeace (which, for example, generated some adverse publicity for Shell UK by protesting against their dumping of obsolete oil rigs) have increased the emphasis on <i>social responsibility</i> in businesses in recent years.</p>
<p><b><i>Provision of a service</i></b></p>	<p>Business organisations, especially in the public sector, may have the provision of a service as their main objective. This means that they aim to provide the service in the best way possible to meet the needs of their customers or users. A hospital or a school, for example, may have this as their main objective.</p>

## **Mission Statements**

Under both UK and EU law, a company must state what it is in business to do - this is known as its overall aim and it can be embodied in a mission statement. This is often a simple and memorable sentence which explains what the organisation is in business to do and what it wants to achieve. A mission statement can often be found in the front of a company's annual report and it is, effectively, a summary of its day-to-day activities and long-term objectives, showing a sense of underlying purpose and direction.

A good mission statement should be clearly defined, realistic and achievable, and at the same time it should ensure that the employees' attention is focussed towards the overall company aim.

Mission statements normally express the organisation's objectives in qualitative terms, (as opposed to quantitative, that is, facts and figures) and many businesses include the following variables in their mission statement: their number one priority, their product definitions, their non-financial objectives and their overall values and beliefs.

Although many people view mission statements as a focus for employees and for other stakeholders, they are still viewed by their critics as nothing more than a publicity seeking exercise.

## **Business Objectives**

It is important to understand how business objectives 'fit in' with business aims and strategies.

- An aim states what you want.
- An objectives set out what you need to have achieved to get what you want.
- Strategies are courses of action which enable you to meet your objectives.

### **In order for objectives to be effective, they must:**

- Provide detail about what specifically needs to be achieved. (often in a quantitative form)
- Have a time limit by when they need to have been achieved.
- Need to state the necessary resources that they require in order to be met.

Setting clearly defined and realistic objectives will enable many employees to understand exactly what their job entails and achieving clearly stated objectives might be linked to bonus payments - this can easily act as an incentive and motivator to employees.

### **Primary and Secondary Objectives**

A primary objective is an ultimate long-term goal of the business (e.g. survival, profit maximisation, diversification and growth). They are often referred to as strategic objectives.

A secondary objective is a day-to-day objective, and it makes a direct contribution to meeting the primary objectives (e.g. increase sales by 5% each year, keep labour turnover at less than 4%). They are often referred to as tactical objectives.

### **Private and Public Sector Objectives**

#### **Private Sector**

Private sector objectives will often differ considerably from objectives set in the public sector. Profit maximisation is often quoted as the over-riding objective for businesses in the private sector. This will involve trying to produce at the point where there is the maximum difference between the firm's total revenue and its total cost - resulting in large dividend payments for the shareholders. However, it is far more likely that businesses will aim to profit satisfy rather than profit maximise (that is, they will aim to earn a satisfactory level of profits to keep shareholders content, and then use the remaining resources to pursue other objectives such as diversification and growth).

Another objective in the private sector, for a rapidly growing business, may well be to maximise sales (or sales revenue) and so increase their market share in order to gain a competitive advantage.

Many businesses set objectives to improve their image and to appear more socially responsible and environmentally friendly – this is often achieved through strategies of recycling materials, sponsoring local events and strictly adhering to all employee legislation (e.g. pay levels, Health & Safety, discrimination, etc.).

### **Public Sector**

Public sector objectives have, traditionally, been centred around providing a public service, rather than make a profit (e.g. when British Gas was a public corporation it had to provide gas supplies to all areas of the UK, many of which were isolated and very unprofitable for the organisation). This regularly led to loss-making organisations being subsidised by the government, and complacency crept in with regards to customer service, quality levels and response times. However, in the UK in the 1980s and 1990s, a massive privatisation programme by the government was implemented and many large utilities such as British Gas, British Telecom and the Electricity Boards were sold to the private sector.

The remaining public sector organisations were told to run in a more cost-efficient manner and to improve the quality of their services to consumers. Performance targets were set for many Local Health Authorities, Local Education Authorities and council services in an attempt to make them more accountable, to reduce their costs and to improve the quality of their output.

### **Short-Term and Long-Term Objectives**

Short-term objectives will often differ from long-term objectives, especially if the business is experiencing poor financial performance at present. A short-term objective may be to consolidate, or even simply to survive the difficult trading conditions that it is experiencing. Once this has been achieved and the business has stabilised its performance, then it may well look to achieve its long-term objective of diversification into new products and new markets, or growth through amalgamation.

## Methods of Growth

If a business is successful it will tend to become bigger each year. The bigger the business the more able it is to survive. However, for many firms this process of organic growth is not fast enough and they may consider joining forces with another firm in order to achieve a more rapid rate of growth.

*Integration* refers to firms combining in order to become larger and more powerful. If the integration is on equal terms it is described as a *merger*, whereas if it results from one firm taking control of another so that the latter loses its identity completely it is called a *take-over*. Such take-overs may be friendly, where both firms realise that this is the best way to survive, or hostile when a predatory firm swallows up another one in order to gain market share by destroying the opposition and/or swelling its own profits by *asset stripping* (selling off at a profit the assets of the firm which has been taken over).

### Horizontal Integration

This is the combining of two firms operating at the same stage of production, for example, two supermarkets. One firm might merge with another in this way in order to:

- eliminate competition and increase market share.
- achieve greater economies of scale, such as greater discounts as a result of now being able to buy inputs in larger quantities.
- acquire the assets of other firms.
- become stronger and therefore more secure from hostile take-over bids.

### Vertical Integration

This is the joining together of firms operating at different stages of production.

***Backward vertical integration*** is when a firm takes over another at an earlier stage of production – for example, a jam manufacturer taking over a fruit farm. This enables the take-over firm to be sure of the availability and quality of its input.

***Forward vertical integration*** is when a firm takes over another at a later stage – for example, a pie manufacturer taking over a chain of delicatessens. The main reason for this is to control the distribution outlets for the product.

#### **Advantages are that this:**

- eliminates the middleman and his profit.
- gives the firm greater economies of scale.

- allows the firm to link processes more easily.

### **Conglomerate Integration (diversification)**

This refers to the combining of firms which operate in completely different markets – for example, an airline company taking over a chain of record shops.

#### **Reasons for Diversification:**

- It allows the firm to spread risk – failure in one area can be compensated for by success in another.
- It enables a firm to overcome seasonal fluctuations in its markets.
- It makes the firm larger and more financially secure.
- The firm acquires the assets of other companies.

### **De-merger**

This involves splitting up the conglomerate so that its subsidiaries become new companies in their own right. Shareholders are given shares in the new company according to how many they have in the original one.

### **Divestment**

This involves the selling off of one or more subsidiary companies – for example, when British Aerospace owned Rover cars they sold it to BMW.

### **Contracting out/Outsourcing**

This is when, instead of the firm undertaking certain activities itself, it pays other firms to do them. Many businesses nowadays contract out services like transport and catering.

### **Management Buy-Out/Management Buy-In**

This involves a team of managers getting together and buying an existing company from its owners. The management team have to raise the necessary finance to buy and run the organisation – this may involve large bank loans. A *buy-out* is when the team of managers come from within the firm, whereas a *buy-in* is when the team comes from outside.

## Grouping of Activities

'An organisation is the rational co-ordination of the activities of a number of people for the achievement of some common explicit purpose or goal, through the division of labour and a hierarchy of authority.'

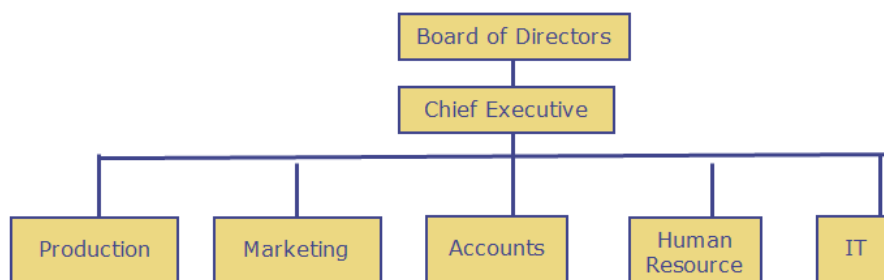
*Edgar Schein*

Whilst Schein gives us a general definition of an organisation, he does not tell us how that organisation is structured – what activities are grouped together and why. In fact there are many different types of business organisation and many different ways that organisations can be structured.

### Functional Grouping

This was a very common organisational structure, widely used by British companies up to the 1960s. In recent years it has largely been replaced by divisional grouping based on product or service (as described below). This is where the activities in an organisation are grouped into departments based on similar skills, expertise and resource used. The functional departments most commonly found in modern organisations include:

- Marketing
- Human Resource Management
- Finance
- Operations
- Research and Development
- Administration.



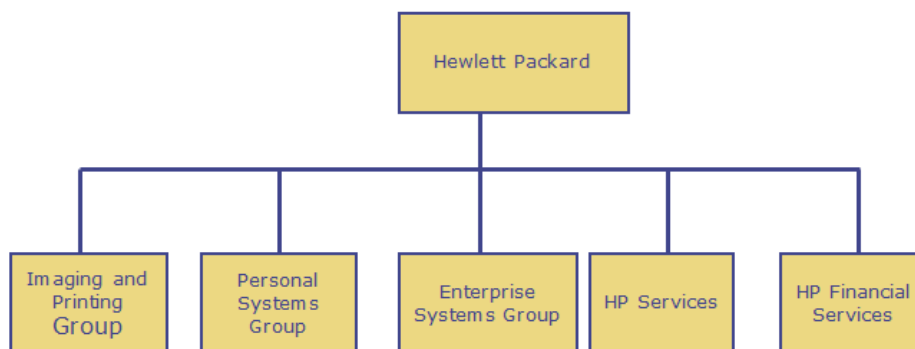
Such organisations usually have a centralised decision-making structure that provides a unified direction for the organisation originating from the top. Each functional department may be large with a great many employees.

### Product/Service Grouping

Here the grouping of activities is based around a particular product or service and is usually described as a **division**. Each division is a self-contained unit. The functional activities – marketing, finance, operations, administration, research and development, and human resources – needed to produce the

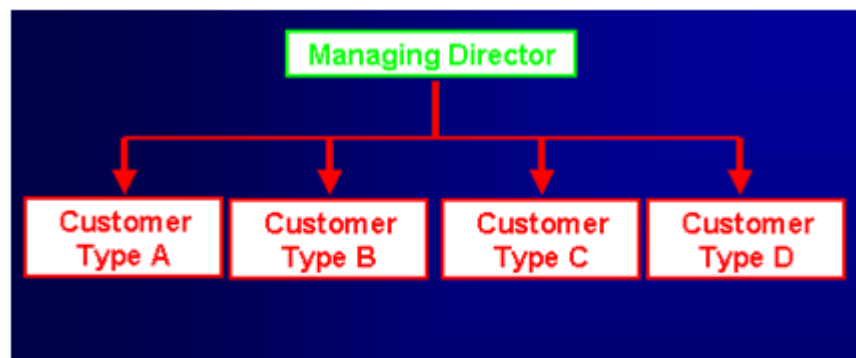
single product or service will be grouped together and assigned to that product. They are likely to be smaller in size than in a functionally based structure.

In most cases, organisations using this type of structure are very large, producing a variety of products for different markets. They are also often highly decentralised. Time Warner Inc. has divisions that include *Time* magazine, Warner Brothers record company, HBO (Home Box Office, a leading pay cable television channel), and a book publisher called Little, Brown.



### Customer Grouping

Organisations structured around customers or groups of clients are more likely to be found in the service sector. They may exist in a private medical practice for



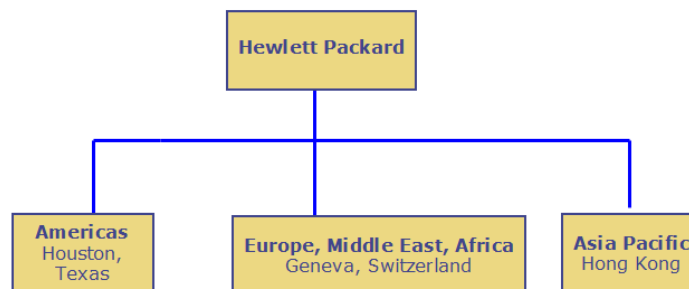
example, but may also be used as the structural basis for sales teams where each representative has his/her own customer group. Organisations like this offer a high degree of personalised service to their customers. They are highly responsive to immediate customer needs and to the anticipation and provision of future customer wants due to the close links they have with their customers.

### Location/Geographical Grouping

An alternative structure can be designed around a geographical or territorial base. The grouping of activities is organised by geographical region. For example, an organisation might have both a North-East Scotland group and a Midlands group. Many organisations selling to a broad customer base spread over a large area are structured in this way. Multinational organisations, such as Shell Exploration and Production, have a geographical base.

Organisations structured along these lines can meet the needs of customer groups in different countries who may have language and cultural differences. This allows specialist knowledge and specific marketing techniques to be applied. In Britain we had the 'Marathon' bar, whilst everywhere else had the

'Snickers' bar. This was because the bar was launched in the UK around the time that running became the nation's favourite sport. Everyone wanted to complete a marathon, and the bar was named to associate an image of fitness and fun with a type of chocolate bar.



There may be significant cost advantages in hiring a local workforce, especially for unskilled and semi-skilled work. This can be seen in the oil industry, for example, where Shell recruit large numbers of local workers in Nigeria and the Middle East.

### **Technology Grouping**

Organisations may group their activities along technological lines. This is often because they produce diverse products that require different technological processes. It is really only appropriate when there are obvious stages of production, and where these stages flow naturally on from one to the next. There are many manufacturing firms set up along these lines, but, although it is possible, such a structure is seldom seen in the service industries.

Organisations can achieve many benefits from grouping activities in this way. There is scope for increased specialisation within the workforce because training is simplified and concentrated on only one technological system. When problems in the production process occur it is easy to pinpoint where they have arisen.

### **Line/Staff Grouping**

**Line departments** perform tasks that reflect the organisation's goals or objectives. They undertake the core operations (those that directly return revenue to the organisation). **Line authority** describes the relationship between superior and subordinate in the organisation. At the top of the line in the typical large organisation there will be the Board of Directors.

Below them will come the management team in charge of the day-to-day running of the organisation. Below them there will be various functional departments, such as marketing, finance, production and human resources. There is also likely to be a line structure within each of these departments. Starting with the department manager the line will progress down to the most junior worker.



## Functional Activities of Organisations

Functional relationships within organisations exist when people, who perform similar tasks, and use similar skills or resources, are grouped into sections or departments. These functional activities are all essential to the organisation, each section or department contributing to the overall performance of the organisation. Each may have its own manager or section head. Departments can be large or small, with few or many employees. For example, in a retail organisation such as Tesco there will be far more sales staff than administration staff in each store, yet both are essential to the efficient running of the store.

Grouping employees together in departments based on skills or use of similar resources, or similarity of work has a number of advantages for the organisation.

- There is efficient use of resources.
- Individuals develop in-depth skills in one area of work.
- Individuals have specific expertise or training in one area of work.
- Career progress is often based on functional expertise – therefore employees are motivated to develop their skills in one particular field (think of teachers who most often get promotion firstly to assistant principal teacher then to head of department in their own subject).
- This structure provides a way of centralising decision-making because there are only a few managers who between them may be responsible for a large number of employees.
- Communication and co-ordination between members of a department are excellent.
- The idea of working as a member of a team often motivates individuals to work harder.
- Individuals will be working with others who are also 'experts' in one particular area of work – problem sharing and problem solving is greatly improved.

However, having a number of functional departments within an organisation can also lead to problems.

- There are often barriers and rivalries between departments.
- Communication between departments can be slow, resulting in poor coordination of the organisation's activities.

- This can also lead to a slow response time to external factors, such as changes in customer demand.
- Decision-making can be a long and slow process as each department is consulted and responds with information or suggestions which then have to be passed onto other departments for consideration.
- Work in individual departments can be so specialised that it becomes routine and meaningless. Being such a small part of the whole operation, employees may only see departmental goals and lose sight of the organisation's goals.
- It may be difficult to pinpoint responsibility for problems within departments.

In modern organisations it is likely that some or all of the following functional departments will be found:

- Marketing
- Human Resource Management
- Finance
- Operations
- Research and Development.

## Forms of Organisational Structure

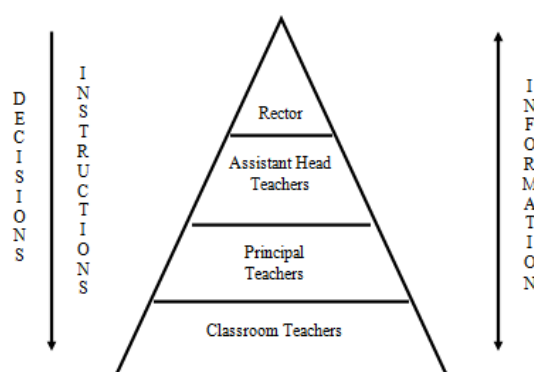
### Hierarchical Structure

This is the traditional structure for many medium and large organisations. It is also sometimes called a **pyramid structure** because of its shape – like a pyramid.

Decisions and instructions are passed down from the senior staff of the organisation to the workforce, and information passes back up the pyramid. Position in the pyramid indicates the level of responsibility the individual has – the higher up the pyramid the greater the responsibility. Members of the organisation have clearly defined roles and procedures – often laid down to define their behaviour at work. Specialisation of tasks is very common, and this is often combined with a breaking up of the organisation into functional departments. This specialisation allows the organisation to benefit from economies of scale in its operations.

In recent years this type of organisation has been criticised for its inability to respond quickly to changes in market and consumer demands. It is also often felt that such structures suffer from time delays, both in communications passing up and down the structure and in the decision-making process, when many individuals on different levels are required to provide input. Some large organisations – the Civil Service, the Armed Services, the Police, and the National Health Service – may have a very large number of layers in the pyramid – 20 to 30 layers is not uncommon.

#### **Example: A school's hierarchical structure (Christon Academy)**



It is important to remember that many individual schools belong to a much larger organisation. They are part of a local authority and the local authority itself is part of a larger organisation. All local authorities in Scotland come under the control of the Scottish Parliament.

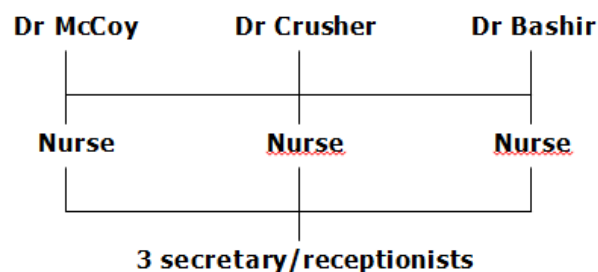
Communications and **operational** decisions within the school are made relatively quickly. These might include telephoning a teacher on the supply list to come in and provide cover for an absent colleague, closing the school because of bad weather, or deciding the date for Sports Day. The individual school would make these decisions itself. **Tactical** decisions, including the

setting of local holidays, or the start date of the new academic year, or the total number of teachers each school is entitled to, will be made by the local authority. The Scottish Parliament will make **strategic** decisions, such as the content of the curriculum and the form examinations will take.

## Flat Structure

The flat structure is just what it says – flat. There are very few levels in the hierarchy. This has a number of significant benefits for the organisation. The main one is that communications are passed quickly from one level to another. This speeds up the processing of information and any decision-making. Many small organisations, such as professional partnerships of doctors, dentists or lawyers, use this type of structure.

### ***Example: A doctor's practice***



Increasingly, large organisations are moving towards a flatter structure, largely in an attempt to overcome the problems of a hierarchical structure. This often involves cutting out some of the layers of the hierarchy (see later notes on 'delayering').

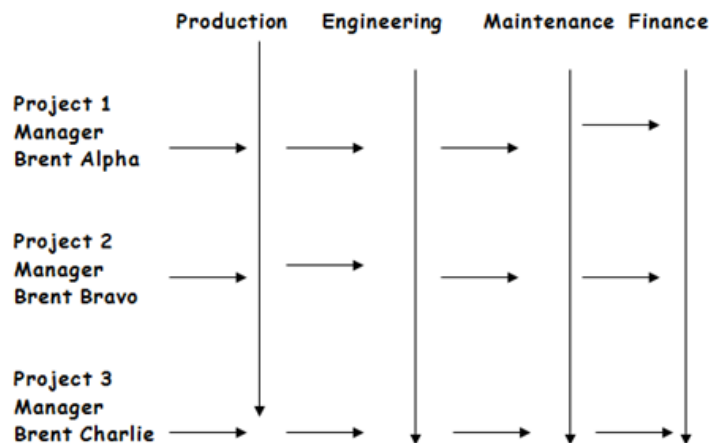
## Matrix Structure

This structure emphasises getting people together who have particular specialist skills and placing them in project teams to complete specific tasks. Individuals have their own areas of functional responsibility within the overall remit of the project. Many people argue that this is the best way to organise individuals, as it is based on the expertise and skills of the people involved.

In its favour, the matrix structure gives scope for ALL individuals to use their talents effectively. There is no hierarchy – everyone in the project team has the same level of responsibility and authority. It is also likely that all individuals will get the opportunity to work in a variety of project teams over a period of time. This variety of work promotes personal staff development, and increases job satisfaction and motivation.

Against its use lie the arguments that it is costly in terms of support staff (for example, secretaries and administration staff) as each project team may need its own dedicated back-up. There are also problems with coordinating a team made up of individuals from different functional departments.

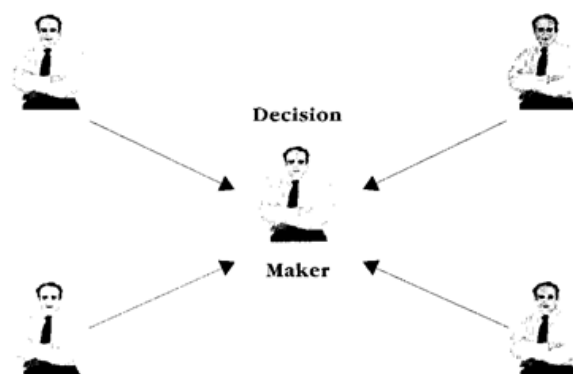
## Example: Shell UK Exploration and Construction



## Entrepreneurial Structure

This is a common structure in many small businesses and in those organisations where decisions have to be made quickly, such as in the production of daily newspapers. Decisions are made centrally with very little input from staff, and are based on the expertise of only one or two individuals. There is a great reliance on a few key workers.

There can be problems with this structure as the organisation grows. Too heavy a workload is placed on too few individuals who have responsibility for decision-making. This can lead to inefficiency.



## Centralised Structures

Here all of the control and decision-making lies with the most senior directors or managers or the owners of the organisation. Subordinates have little or no authority at all. This type of structure is often associated with a hierarchical structure and has several key advantages:

- Organisations may benefit from strong leadership from the top.
- Senior management have control of all aspects of finance and budgeting.
- Procedures, such as ordering, purchasing and storage can be standardised – this can lead to the organisation benefiting from economies of scale.

- Decisions are made from the point of view of the business as a whole, not for the particular benefit of one department or another.
- Managers are likely to be more experienced and skilled in the role of management and the decisions they make will be of better quality.
- It is easier to promote a corporate image if the organisation adopts a centralised approach, as all external communications can be done in a standardised format.

## Decentralised Structures

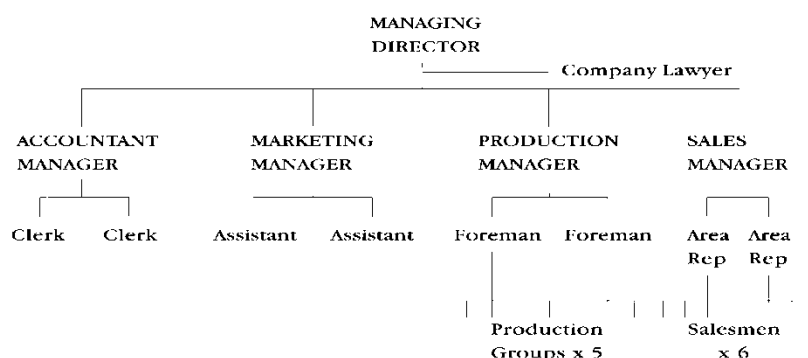
In these organisations decision-making and control are delegated to and carried out by subordinates. This relieves senior management of having to make many of the routine operational decisions required by the organisation. This structure is often associated with a flat structure and also has several key advantages:

- The delegation of authority is felt by many to be a key motivator for subordinates and allows them to be groomed for senior positions when they become available.
- Subordinates often have better first-hand knowledge of the requirements of their departments or customers, and can therefore make better quality decisions based on this knowledge.
- Delegation allows a more proactive approach and much greater flexibility of roles.
- Decision-making is quicker and more responsive to external changes.

There is no 'right' form of organisational structure. For each organisation the structure it adopts must reflect its aims and objectives and be the best – at that moment in time – to fulfil these. It may well be the case that an organisation will change its structure as it grows and responds to changes in its external environment.

## Organisational Charts

These show the structure of the organisation in diagrammatic form. Individuals are identified in specific positions within the organisation, clearly showing their links to others along lines of authority and responsibility.



## Advantages of Organisational Charts:

- Each individual can be named in the position he or she holds, providing clear identification;
- They identify appropriate lines of communication or where bottlenecks occur;
- They identify the ***span of control*** or number of subordinates each individual has.
- New members of staff can learn who they are responsible to and for.
- They may identify areas where it would be appropriate to call in a specialist staff member, for example a design engineer in the production department.
- The links between individual departments can be identified.
- Functional levels in the organisation can be easily identified.

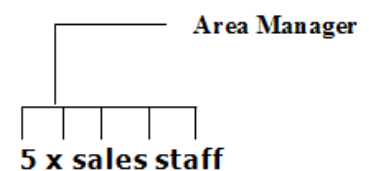
## Disadvantages of Organisation Charts:

- They do not show how much authority each position in the chart carries.
- They do not identify any informal relationships that occur.

## The Span of Control

This refers to the number of workers or subordinates under a supervisor or manager. There is no perfect size for a span of control. Henri Fayol, a writer on management, suggested that the optimum size should be between 3 and 6 subordinates because this gives the manager a lot of control over his subordinates. He also argued that 3–6 subordinates was all that a manager could cope with.

In this diagram the Area Manager has a span of control of 5 sales staff.



There are, however, four important factors that should be considered when deciding on the span of control of any manager or supervisor:

- The calibre and ability of the manager or supervisor must be considered. Some people are better at managing and leading than others and can therefore cope with a larger number of subordinates.
- The calibre and ability of the subordinates must be considered. Intelligent, motivated and able subordinates will need little in the way of control, and therefore a superior can manage a relatively large number of people. The same will not be true if subordinates are lazy, demotivated or less able.
- The third factor that should be considered is the actual task itself. A task of great importance to the organisation, or of a difficult nature, will be more

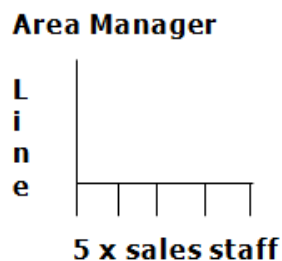
likely to be closely controlled by the manager, and therefore a small number of subordinates would be more appropriate.

- Fourthly, the practices and customs of the organisation must be taken into account. In some organisations there may be clear indicators and guidelines as to the number of subordinates in each span of control. If this is stuck to rigidly, some managers may struggle to cope with the number of subordinates they have, whilst others may find that they are not given enough to do.

## Line Relationships

This describes the relationship between superior and subordinate and can be clearly identified on an organisation chart as a **vertical line** between individuals.

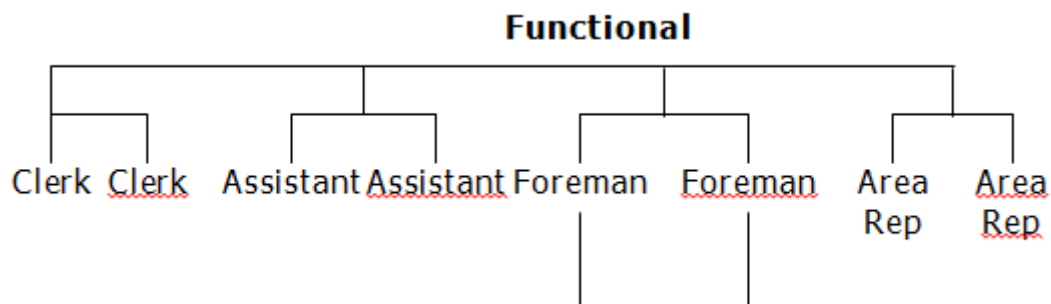
In the diagram below the **line relationship** is between the Area Manager and the five sales staff.



## Functional Relationships

These exist between individuals at the same level in the hierarchy. These individuals have the same level of authority and responsibility, although they may be in different departments, or even in different locations. This relationship can be clearly identified on an organisation chart as a **horizontal line** between individuals.

In the diagram below, each person on this level of the organisational chart has a **functional relationship** with everyone else at this level.

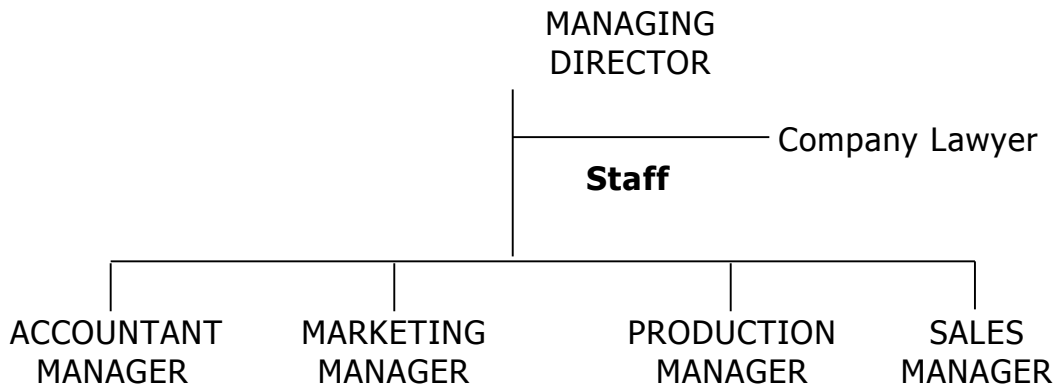




## Staff Relationships

This is a relationship between the organisation and someone in it who acts in an advisory capacity **for the benefit of the organisation as a whole**, not just for one department. People who might be in a staff relationship include company lawyers, taxation specialists, company secretary or company receptionist.

The **staff relationship** seen in this organisation chart is the company lawyer.



## Formal and Informal Structures

The formal structures within an organisation have been described above and consist of the relationships between individuals within an organisation in terms of the superior, the subordinate, level of authority and degree of responsibility. However, there may also exist very important informal relationships – an internal network or grapevine – that consists of communication passed between individuals in ways that are not set down in the formal structures.

Many people obtain a sense of security and belonging, as well as achieving social status, by contributing to the grapevine. Information passed on in this way is often of a confidential nature and is not usually available to members of the group – unless they hear it 'on-the-grapevine'.

The need for such structures may arise because the organisation's formal communication processes are inefficient or at least are felt to be inefficient by some of the staff. Whilst information passed along the grapevine is likely to be news to members of the informal group, it is not necessarily always accurate. Because of this, managers must be aware of the informal structures within their organisation and may even purposely feed the grapevine with information they DO want communicated quickly to the staff.

Informal structures can be destructive to the smooth running of the organisation. Information that is passed on incorrectly can, in some instances, result in bad feeling, resentment or even hostility among the staff. Members of staff may be excluded from the grapevine and may feel isolated, or confused and unsure of their position. In extreme cases, the informal structure may be opposed to the decisions taken by the formal structure (the management team) and can sabotage management aims and objectives.

## External and Internal Factors

There are many variables that operate within an organisations environment that have a direct or indirect influence on their strategy. A successful organisation is one, which understands and can anticipate and take advantage off changes within their environment.

An organisations operating environment can be analysed by looking at:

- External forces (*those factors that an organisation has no control over*),
- Internal forces (*factors that an organisation has direct control over*)

## External Factors

The external environment of an organisation can be analysed by conducting a **P.E.S.T.E.C** analysis. This is a simple analysis of an organisations *Political, Economic, Social, Technological, Environmental and Competitive* surroundings.

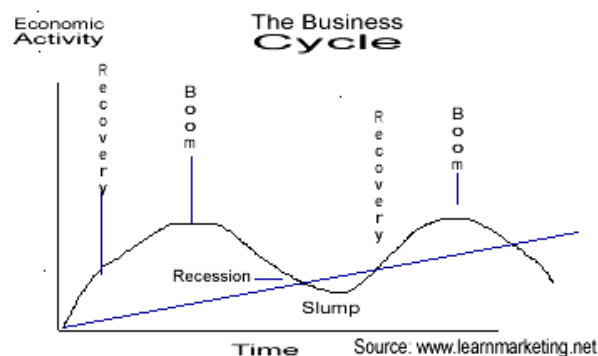
### Political

Political factors can have a direct impact on the way business operates. Decisions made by government affect our every day lives and can come in the form of policy or legislation. The government's introduction of a statutory minimum wage affects all businesses, as do consumer and health and safety laws and so on. The current increase in global petrol prices is having a profound impact on major economies, it is estimated that £200bn has been added to the global fuel bill since the price increases started (BBC news 19/9/00).

The political decision as to whether the UK signs up to the Single European Currency is again having an impact on UK businesses. Firms like Nissan who have recently invested in the UK have signalled that they will withdraw their business from the UK if the government fails to sign up.

### Economic

All businesses are affected by economic factors nationally and globally. Interest rate policy and fiscal policy will have to be set accordingly. Within the UK the climate of the economy dictates how consumer may behave within society. Whether an economy is in a boom, recession or recovery will also affect consumer confidence and behaviour.



An economy, which is booming, is characterised by certain variables. Unemployment is low, job confidence is high, and because of this confidence spending by consumers is also high. This has an impact on most businesses. Organisations have to be able to keep up with the increased demand if they are to increase turnover. An economy, which is in a recession, is characterised by high unemployment, and low confidence. Because of high unemployment spending is low, confidence about job security is also low. Businesses face a tough time, consumers will not spend because of low disposable income. Many businesses start cutting back on costs i.e. Labour, introduce shorter weeks and cut back on advertising to save money.

***Case: In the early 1990's when the UK economy was in a slump, and businesses were folding repeatedly, a security company called 'Dreadlocks security' to combat falling sales embarked on strategy of cutting back on labour costs, and doubling advertising expenditure. The companies' theory was that not their entire target segment was affected by the recession and he had to fight for the customers that still had the income to spend on security products.***

Economies globally also have an impact on UK businesses, cheaper labour abroad affects the competitiveness of UK products nationally and globally. An increase in interest rates in the USA will affect the share price of UK stocks or adverse weather conditions in India may affect the price of tea.

A truly global player has to be aware of economic conditions across all borders and ensure they employ strategies and tactics that their protects their business.

## **Social**

Within society forces such as family, friends, and media affect our attitude, interest and opinions. These forces shape who we are as people and the way we behave and what we ultimately purchase. For example within the UK people's attitudes are changing towards their diet and health. As a result the UK is seeing an increase in the number of people joining fitness clubs and a massive growth for the demand of organic food. On the other end of the spectrum the UK is worried about the lack of exercise its youngster are obtaining. These 'fast food games console' children are more likely to experience health problems in their future because of the lifestyle they are living now.

Population changes also have a direct impact on all organisations. Changes in the structure of a population will affect the supply and demand of goods and services within an economy.

In Japan the fall in the birth rate has had a major impact on the sales of toys, as demand falls competition for the remaining market becomes very intense. If this trend continues it will have an impact on other sectors within the future affecting teen products, 20's products and so on.

As society changes, as behaviours change organisations must be able to offer products and services that aim to complement and benefit peoples lifestyle and behaviour.

## **Technological**

Changes in technology are changing the way business operates. The Internet is having a profound impact on the marketing mix strategy of organisations. Consumers can now shop 24 hours a day comfortably from their homes. The challenge these organisation faces is to ensure that they can deliver on their promise. Those businesses, which are slow to react, will fall at the first few hurdles. This technological revolution means a faster exchange of information beneficial for businesses as they can react quickly to changes within their operating environment.

There is renewed interest by many governments to encourage investment in research and development and develop technology that will give their country the competitive edge. The pace of technological change is so fast that in the computer industry the average life of a computer chip is approximately 6 months. In the name of progression technology will continue to evolve organisations that continue to ignore this will face extinction.

## **Environmental**

These have become much more significant in recent years. Pressure groups which promote environmental awareness such as Greenpeace and Friends of the Earth have become much more high profile. As a result they are able to affect the behaviour of businesses. In 1995, for example, Shell Oil wished to dispose of the disused oil platform, Brent Spar, by dumping it at sea. Action by Greenpeace in many countries, including encouraging customers not to buy Shell petrol, forced Shell to abandon their plans and consider other ways of disposing of the platform. Shell and many other businesses now stress that they have an aim of corporate or social responsibility.

Environmental concerns have also led to changes in legislation, e.g. in Germany businesses must recycle packaging material, while in Holland every government department must set an environmental quality target.

It is important to realise that changes such as those detailed above will have many far-reaching effects on business activity – for example, the existence of out-of-town hypermarkets and one-stop shopping was made possible by the spread of car ownership and would be threatened if the use of cars was to be limited because of the pollution they cause. This gives an impetus to oil firms to try to find an environmentally friendly fuel, and to governments to finance alternative methods of transportation rather than build more motorways which destroy the environment.

## **Competitive**

Rivals affect firms also. Competitors can make imitations of products that steal market share. The existence and/or actions of competitors will influence the operation of a business – action will have to be taken to protect sales, market share, profits, etc.

Price wars can take place which benefit the customers and consumers but hit hard the profits of the companies involved.

## **Internal Factors**

### **Finance**

Money affects the business. If there is no money to expand or buy new resources it will limit the success of the business.

A lack of funds might mean a business:

- Is unable to produce more to increase its market share.
- May not be able to employ the experienced staff it needs to design and produce the products or to deal with customers.
- Has to buy cheaper materials which reduce the quality of product on offer to customers.

### **Employees**

The skill, ability and number of staff that a business has may restrict what it wants to achieve:

- Skilled workers may be in short supply.
- Employees may not be motivated.
- Their work could be poor.
- More likely to take time off and take less care in the job they are doing.

### **Corporate Culture**

This is the values, beliefs and norms relating to the company or organisation that are shared by its entire staff. It can also be described as the atmosphere or feeling within an organisation as shown by its employees.

Any successful business has a positive culture; this is shown by the positivity of the staff and their commitment to achieve the organisations goals and objectives. Creating such a positive environment can be a challenge for many managers. Getting a balance of enthusiastic staff who work well as a team and all contribute well to the success of an organisation is difficult to gain.

Culture is visible in many organisations where staff wear similar clothes i.e. a uniform is worn, a suit or casual wear. Through the way colleagues dress shows corporate culture as they are all demonstrating common values and standards.

## Types of decision

In order to achieve the organisation's aims and objectives managers must make **decisions** about issues such as:

- what to produce.
- where to locate premises.
- what method of production to use.
- how many people to employ.
- what price to charge for the product and many others.

There are three main types of business decision: strategic, tactical and operational.

### Strategic Decisions

Strategic decisions are made to set out the AIMS of an organisation. These decisions affect the long-term position of the organisation and what it hopes to achieve at some future point.

These decisions are made by the Chief Executive and the Board of Directors – the Senior Management Team – and reflect the overall view of the organisation's owners. Of course, in the case of a Sole Trader this is the owner him/herself. In a government organisation these strategies would be part of government policy.

Alfred D Chandler (1962) defined a strategy as follows:  
'...[strategy is] the determination of the basic long-term goals and objectives of an enterprise, and the adoption of courses of action and the allocation of resources necessary for carrying out these goals'.

The planning of the long-term strategy of the organisation must ask questions such as:

1. 'What, if anything, do we have to change?' This requires a review of the present position of the organisation and an assessment of how well that position continues to fulfil the goals of its owners.
2. 'Where do we want to be in five, ten, fifteen or twenty years' time?' This involves setting targets to improve/alter the present position of the organisation to meet the revised or new goals of the owners.
3. 'What resources are we likely to require?' In general terms the organisation looks at whether or not there will be a change in the quantities or sources of resources used over the next time period.

4. 'What changes are likely to take place in our operating environment?' Questions must be asked to identify any external factors that might affect the organisation, such as changes in government policy or consumer trends. Do these factors pose a threat, do they offer an opportunity, or are they unlikely to be of any consequence?
5. 'How can we gain/maintain a competitive edge over others?' Operating in even a small local market there is likely to be competition. Companies operating in national or international markets must take account of, and be competitive with, others.

### **Tactical Decisions**

Tactical decisions are made to set out the OBJECTIVES of an organisation. These decisions affect the short-term position of the organisation and set out how the strategic decisions are going to be achieved. They describe, in detail, how resources are going to be brought together and used.

Tactical decisions are likely to specify departmental targets or responsibilities and are generally measurable. For example, the strategic aim may be to increase market share by 12% over the next five years. The **tactical decision** might be to give the sales department a target of an increase in new orders to the value of £100,000 during the next twelve months.

However, tactical decisions are likely to be constantly under review and objectives may be changed as a result of changes that may influence the effectiveness, or otherwise, of the decisions made. Sainsbury and Tesco are the two largest supermarket chains in Britain. When Tesco opened several of its stores on a 24-hour basis, Sainsbury were quick to react to their competitor's decision and made the tactical decision to follow suit in a number of their stores.

### **Operational Decisions**

These are the day-to-day decisions made within various departments of the organisation as they work to achieve the objectives of the organisation. They are often made in response to changes in circumstances, for example, if a secretary has telephoned to say she is ill and cannot come in to work. If the task that she was currently doing is of great importance, the **operational decision** might be to transfer another member of the administrative staff to cover her duties until her return.

### **Review/Evaluation/Alteration**

As well as the actual process of making decisions, managers have to look at the outcomes of these decisions. What actually was achieved? Was this what we expected? If not, do we have to make any alterations to the work we are doing?

Management undertake a continuous process of review, evaluation and alteration of their decisions – strategic, tactical and operational. No decisions, however large or small, can stand in isolation and fail to affect something else in the organisation. The more flexible the organisation is, the more easily it can respond and adapt to change as circumstances require, and the more successful it will be.

Short-term objectives have to be reviewed in order to assess their performance in meeting the long-term targets set by management. Long-term aims also have to be re-assessed, and perhaps altered, in view of the achievements made in the short-term.

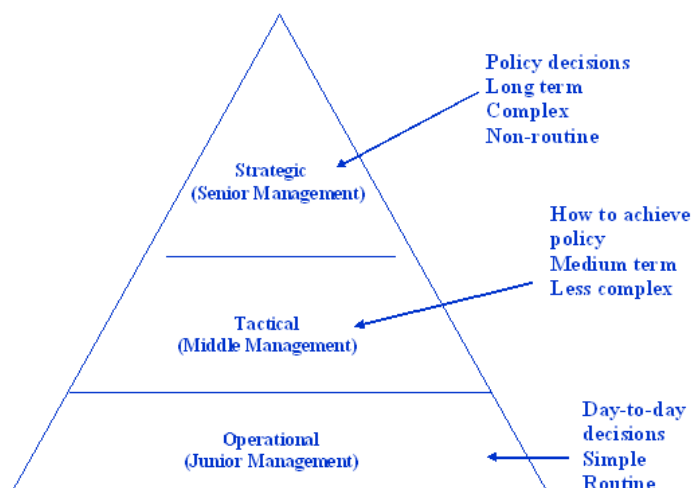
### **Who Makes the Decisions in an Organisation?**

The more important a decision, in terms of its effect on the organisation, the more senior will be the person responsible for making the decision.

### **Strategic Decisions**

The most senior people in any organisation make these decisions. They are the decisions that are made to achieve the goals of the owners, and are most likely to be made by the owners of the organisation or their representatives. In other words:

- The sole trader will make these decisions.
- The partners in a firm will make these decisions.
- The directors of a private limited or public limited company will make these decisions, although shareholders may vote on proposals at the Annual General Meeting.
- The government ministers responsible will make these decisions.
- The office bearers of the charity or club will make these decisions.





## Tactical Decisions

The most senior people in the organisation may also make these decisions. However, with very large organisations, such as multi-national companies or government bodies, there may be divisional directors or senior managers in charge of sections or geographical areas who would be likely to be involved in the tactical decision-making for their specific area of responsibility.

## Operational Decisions

These decisions are most likely to be made by the manager, section head, team leader or even the individual worker responsible for the completion of the task on a day-to-day basis.

### EXAMPLES OF DECISION MAKING

Strategic Decisions	Tactical Decisions	Operational Decisions
<ul style="list-style-type: none"> <li>➤ Increase market share</li> <li>➤ To maximise profits</li> <li>➤ To provide a service</li> <li>➤ To grow</li> <li>➤ To survive</li> <li>➤ What products will the business produce?</li> <li>➤ Who will be our customers?</li> </ul>	<ul style="list-style-type: none"> <li>➤ Recruiting staff</li> <li>➤ Who to give subcontracts to</li> <li>➤ What kind of marketing to have? (Promotional decisions)</li> <li>➤ Open new branches</li> <li>➤ Raise/lower prices</li> <li>➤ Make cutbacks on expenditure</li> <li>➤ Mergers or Takeovers</li> <li>➤</li> </ul>	<ul style="list-style-type: none"> <li>➤ arranging work rotas</li> <li>➤ Purchasing materials</li> <li>➤ Which firm will we use to make deliveries?</li> <li>➤ Dealing with customer complaints</li> </ul>
Example: St Andrew RC Secondary School		
STRATEGIC	TACTICAL	OPERATIONAL
<ul style="list-style-type: none"> <li>➤ Aims to be the best performing school in GCC</li> </ul>	<ul style="list-style-type: none"> <li>➤ Hire experienced staff</li> <li>➤ Offer courses pupils like</li> <li>➤ Train staff in Active Learning methods</li> <li>➤ Train pupils better study skills</li> <li>➤ Buy quality resources (ICT, Books etc)</li> <li>➤ Build 21<sup>st</sup> Century classrooms</li> </ul>	<ul style="list-style-type: none"> <li>➤ Arrange staff cover</li> <li>➤ Computerised attendance</li> <li>➤ Timetable arrangements</li> <li>➤ Fire Evacuation procedures</li> <li>➤ Schemes of work</li> </ul>

## Management

Businesses are only as good as their managers/owners. Therefore if they are not making good decisions the organisation could fail:

- Managers may not have the ability to make good decisions.
- Owners and managers may be unwilling to take risk.

## Technology

If the technology in the business cannot do what people need it to, then this will restrict the ability to achieve objectives.

- The technology may not be available to improve production.
- It may be unable to provide the e-commerce it needs to sell online.
- Customers' expectations of technology may not be met.

## The role of Managers

There are many definitions of 'manager' or 'management', all of which have roughly the same meaning and all of which are probably equally correct.

We could say that a manager:

- gets things done through other people.
- gets things done by using an organisation's resources.
- controls and supervises activities in an organization.
- makes decisions about the running of an organization.
- is in charge of a number of subordinates.
- is in charge of a department.
- is accountable to, and carries out the wishes of, the owner(s) of the organisation.

With all of these statements about a manager we are, in a way, identifying his/her role within an organisation.

Henri Fayol, (*right*) writing in 1916, specified five functions of management.



### Plans

looks ahead and sets aims and strategies;

### Organises

makes arrangements for all the resources of the organisation to be in the right place at the right time and in the right quantities;

### Commands

tells subordinates what their duties are;

**Co-ordinates** makes sure everyone is working towards the same aims and that the activities of individual workers fit in with the work of other parts of the organisation;

**Controls** measures, evaluates and compares results against plans, and supervises and checks work done.

More recently these functions have been added to and could now be said also to include:

**Delegates** makes subordinates responsible for tasks and gives them the authority to carry them out;

**Motivates** encourages others to carry out their tasks effectively often by introducing team-work, empowerment, worker participation in decision-making and other non-financial methods.

Derek Torrington and others, in their book *Effective Management* (Prentice Hall, 1989) put forward a mnemonic (**GROUP**) to describe the art of management. This stands for:

- management have conflicting **G**oals.
- managers are held responsible for **R**esults.
- managers work in **O**rganisations.
- managers must cope with **U**ncertainty.
- managers work with and through **P**eople.



Management decisions are made in order to achieve the long-term aims of the owners of the organisation. If an organisation does not have a set of clearly defined aims, it will be at a considerable disadvantage when compared with its competitors, as it will have no focus for its operations.

Managers must make decisions in order to carry out their roles and functions within the organisation. There will always be a need to make decisions about different combinations of resources, methods of production, markets to target and products to develop, as well as decisions about which staff to employ and what their duties should be.

If the organisation does not have a framework of long-term aims, short-term objectives and targets to be achieved to fulfil these, managers will be unable to give clear instructions to the people employed within the organisation. The employees will then have little or no direction or purpose for their work. This will reduce employee motivation and productivity and, as a result, the profits of the organisation.

Managers also make comparisons between the actual performance over a period of time and the aims and objectives the organisation has set. This provides them with a method of judging the success or failure of the decisions they have previously made. It also guides them in making decisions for the next time period, or in making modifications to existing decisions to take account of changes which have occurred.

### **Managers, Strategy and Objectives**

An organisation begins with a strategic plan then progresses to a structure to put that plan into action, which is then carried forward by controlled activity between managers and workforce. The different departments are harmonised by coordinated management and then is checked for efficiency and effectiveness.

1. How would you define a manager?

In an NHS Hospital some managerial activities could be as follows:

<i>Managerial Activity</i>	<i>Description</i>	<i>Example</i>
Planning	Setting tasks/goals	❖ Reduce patient waiting times
Organise	Allocating resources	❖ Set up nurses work rotas ❖ Schedule for patients' beds ❖ Different theatre days
Command	Keep employees under supervision	❖ Appoint Matrons ❖ Instigate Doctors' rounds
Co-ordinate	Activities run seamlessly	❖ Ward meetings ❖ Use of porters and other support staff
Control	Checking on overall progress	❖ Patient waiting lists ❖ Staff appraisal

Motivate	Giving employees incentive to work	<ul style="list-style-type: none"> <li>❖ Increase nurses pay</li> <li>❖ Pay overtime</li> </ul>
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### **The Role and Responsibilities of Management**

Overall, the role of management is to ensure that they choose a structure for the organisation which enables it to meet its purposes in the most effective and efficient way. They have the responsibility to ensure that all members of the organisation are aware of the structure and how it should operate. In choosing a structure and making it work, management need to recognise the existence of an informal structure and of organisational culture. If at all possible, they should try to ensure that the formal structure is consistent with these.

Management also need to be prepared to change a structure where it has ceased to be effective. However, this may not be easy to do, especially if the structure has been in existence for some time as some staff may be reluctant to move to a new and unfamiliar system. Also, constant tinkering with the structure of an organisation may lead to confusion and resentment among the workforce and may be counter-productive.

## A Structured Decision-Making Model

This simple nine-step process can be applied to any decision that has to be made. It doesn't matter what that decision is, or who is making it.

1. **IDENTIFY THE PROBLEM** Consider the issues that must be tackled by the organisation in the future, about which it must make decisions now – looking to set the future aims of the organisation.
2. **IDENTIFY THE OBJECTIVES** Consider the objectives that must be implemented in order to meet the aims identified above.
3. **GATHER INFORMATION** Gather all relevant information, internal and external.
4. **ANALYSE INFORMATION** Analyse all information. What are the physical, financial and human constraints?
5. **DEVISE ALTERNATIVE SOLUTIONS** Devise a number of possible alternative solutions to the problem all of which might succeed in fulfilling the objectives.
6. **SELECT FROM ALTERNATIVE SOLUTIONS** Select the solution most likely to achieve the objectives successfully.
7. **COMMUNICATE THE DECISION** Communicate the decision to those involved in implementing it.
8. **IMPLEMENT THE DECISION** Put the solution into effect, consulting everyone involved at all levels.
9. **EVALUATE** Appraise the effectiveness of the solution and undertake remedial action if required

MNEMONIC- **POGADSCIE**

## S.W.O.T. Analysis

This is another method of helping management to reduce the risk involved in making decisions in a dynamic industry. It involves analysing the current position of a product, a department or even the whole organisation, and trying to identify its possible future courses of action, by looking at its Strengths, Weaknesses, Opportunities and Threats.

A **strength** is a factor which a business currently possesses and which it performs effectively, such as having a strong management team, a profitable portfolio of products, or a loyal customer base.

A **weakness** is an area in which the business currently performs poorly, such as having a high level of industrial disputes, falling profitability, or falling productivity levels.

An **opportunity** is a potentially successful or profitable activity that the business could take advantage of in the future, such as the take-over of a competitor, the development of new products, or breaking into new markets.

A **threat** represents a potential future problem which the business may face in the future, such as new competitors entering the industry, new legislation restricting the use of certain raw materials, or the possibility of being taken-over by another company.

Remember, the strengths and weaknesses are internal factors which the company currently faces. The opportunities and threats are external factors which the company may face in the future.

The S.W.O.T. analysis is represented in a simple four-box diagram, as illustrated below:

S.W.O.T analysis for a Chocolate manufacturer.

<b>Strengths:</b> Plenty of R&D, leading to new product ideas. Achieving economies of scale in production. High level of customer loyalty and repeat purchasing. Effective promotion.	<b>Weaknesses:</b> Several of our products are reaching the end of their product-life-cycle. Too many marketing personnel are leaving the business. Restricted product range.
<b>Opportunities:</b> New markets in Far East. A joint venture with a foreign chocolate firm. Product extensions, such as different sizes of bars.	<b>Threats:</b> Take-over by domestic rival. New legislation may affect the source of our ingredients. Competitors are threatening a price war.

This diagram is simple and easy to follow, and it can provide the basis for discussion of business strategy at meetings. The results of a S.W.O.T. analysis may often identify possible courses of action that had not been considered, as well as categorising and prioritising the problems that the business faces. In most large businesses, the marketing department will carry out a S.W.O.T. analysis as part of its annual marketing audit – this highlights the products which are performing effectively, those which are reaching the end of their lifecycle, potential new markets to break into and the overall effectiveness of its personnel.

## **The Problems of Using Structured Models**

### **1. The Time-Scale Required**

Using a structured process looks as though it will take time to complete, and this is possibly true. The more important or complicated the decision the longer it will take to make.

### **2. The Ability to Collect all Information**

Before making any decision it is important to have all the information you require. Gathering information can, in itself, be time consuming, but there is also the problem of the accuracy, relevance and amount of information you collect.

There is also an increasing problem in the quantity of information facing decision-makers today. Vast amounts of data are available, from a huge variety of sources. How do you find exactly what you are looking for when there is so much information accessible?

### **3. The Problems of Generating Alternative Solutions**

It is always better to consider **all** of the possible alternative solutions that might achieve the aims and objectives we hope to fulfil. However, the actual **thinking** of alternative solutions can, in itself, be a problem. Many people find it difficult or are uncomfortable with having to make choices from many different, perhaps complex, alternatives – they prefer to be given a very limited choice between straightforward alternatives.

In reality there may also be a number of constraints, both internal and external, which will affect the ability to construct a number of viable alternatives from which we will then have to choose.

#### ***Internal Constraints***

- (a) The availability of finance.
- (b) Existing company policy.
- (c) People's behaviour – both in their ability and in their attitude.



## ***External Constraints***

- (a) Government and EU legislation.
- (b) Competitors' behavior.
- (c) Lack of technology.
- (d) The economic environment.

When looking at alternative solutions there is also the risk that the consequences of the implementation of various alternatives are not fully considered. What appears to be the best solution may, in the long term, have far-reaching effects on the organisation.

### **4. Lack of Creativity**

By having to follow a structured process for making decisions it may be that the individual is less inclined to follow that 'gut feeling', the instinctive response that can lead to the best decision in a given situation. Structured processes that involve the collection and analysis of information may mean that the decision-maker is less inclined to take risky decisions – because of the cost, time and effort put into the process. It may also be that the length of time taken to make structured decisions following a detailed process means that the organisation is not very responsive to changes in the market, and therefore loses actual or potential sales to rival organisations.

## **The Benefits of using a Structured Process of Decision-Making**

### **1. No Hasty Decisions will be Made**

There will have been time taken both to collect information and to assess and analyse it. No snap judgments will be made, and everyone will have time to assess what needs to be done and how best to do it.

### **2. The Quality/Quantity of the Information you have**

Decision-makers will be confident that their decisions are based on a full knowledge of all relevant facts and information.

### **3. The Availability of Alternative Solutions**

There will be time and an opportunity to propose and assess alternative solutions and their viability, and the consequences of their implementation.

### **4. Enhances Innovation and Responsiveness**

By following a logical process of decision-making, innovation will be enhanced, as all of the alternatives will have been considered. Responding to a situation by making quick decisions is not helpful to the organisation if the quality and long-term effectiveness of the decision made is less than it could have been if time had been taken to follow a structured process.

## Changes in Structure

Reference has already been made to the fact that organisations can change their structure. Ideally, the structure should reflect the purpose of the organisation. Over the last decade or so, many UK-based organisations have undergone structural change in an attempt to ensure that they can cope with changing circumstances. These changes have affected all types of organisations in all industries but have had a particular influence in manufacturing organisations.

For more than twenty years the UK's manufacturing industries have been in decline. Much of this has been seen as a natural development for a mature economy as it goes through the process of de-industrialisation.

UK industries have been subjected to fierce competition from emerging economies such as the 'Tiger Economies' of South East Asia. This has led to many of our products being too costly and of inferior quality, to compete in international markets.

The accepted explanation has been that the cost of labour in developing countries has been much lower than in the UK, and if we are to compete then our wage rates need to be forced down. To an extent this has happened. In May 1996 a CBI report stated that the average manufacturing wage in the UK was lower than that of an equivalent worker in Korea. Yet the trend of decline in our manufacturing industries has continued.

Large, successful multinational companies who are based in these tiger economies have now opened manufacturing facilities in the UK, leaving our home-grown firms even further behind. In addition, we have been through a recession which has forced many changes on almost every organisation in the UK.

Recognising the problems, particularly within the traditional approaches to management in the UK, was perhaps the hardest task facing our industries.

The traditional approach involved:

- direct lines of responsibility.
- employees doing what they are told.
- paying people for the position they hold.
- management alone making decisions.
- management having the *right* to manage.
- different levels of management having different levels of decision making power.

This approach is not necessarily wrong in itself. However, the development of the economies of the East is a genuine threat to the structure and methods of management and production processes in most Western economies.

The challenge that faces modern management is that they must change in order to survive and compete in the next century. Our production needs to be revolutionised; just becoming more efficient will not be enough. To gain a truly competitive advantage we must be innovative and imaginative in our approach to management.

### **De-layering**

This involves the cutting out of levels of management within the organisation in order to 'flatten out' the structure and is one of the strategies used by companies in recent years to overcome the effects of aggressive competition in the market place.

One of the steps that businesses have been forced to take in order to become more competitive and to survive the worst of a recession is to look at the organisational structure and see where savings could be made.

Organisations found that some of the levels of management were not only unnecessary, but were also hampering the lines of communication. This, in turn delayed the process of change as information passed through too many layers of authority, created unnecessary work and slowed down the decision-making process.

All levels of management are dependent upon those below them to supply the information that is required and often consult them before decisions are made.

It became obvious that the best people to make decisions were the staff who were directly involved, and so levels of management, especially middle management, were removed. Staff were empowered to make their own decisions.

Where successful, organisations became much flatter, with far fewer layers in the hierarchy, communications improved and decisions were made more quickly. Organisations became more responsive to changes in the market and could adapt more quickly. One such organisation was General Accident, the insurance giant, which carried out a process of de-layering in the late 1980s.

However, in some instances, too many layers were removed and the remaining staff, managers and subordinates alike, found that the extra work that they had to take on was too much. A number of companies, such as Vetco Grey, an engineering and fabrication production organisation, have now begun to re-employ staff at middle management levels.

## Down-sizing

This involves the removal of certain areas of the organisation's activities that are not directly linked to the **core** activities, thereby reducing the scale of production to meet the actual demand for the firm's products.

The term is used by organisations when they attempt to reduce costs by:

- reducing the scale of their operations to meet actual market demand.
- stripping out excess capacity within the organisation (at all levels and within all functions).
- consolidating complementary operations under one function.
- reducing the resources of the organisation following increases in productivity.

Recessions in Western economies force companies to look very closely at ways of reducing costs in order to survive. Many find that their productive capacity exceeds the actual or predicted demand for their product. Even after a recession, the demand for their products may continue to be less than it had been before.

For some organisations down-sizing meant the closure of factories or production units. For others it meant the merging of two or more separate operations under separate management functions, and bringing them together under one management umbrella. And for some it meant the scaling down of their production capacity.

Duplication occurs not only in production and management, but also in areas such as sales, research and development and administration. For example, having two separate sales forces for different product ranges is an expensive luxury. This may be sustainable, and even necessary, during an economic boom, such as in the mid 1980s. However, with ever increasing competition and the lingering effects of a recession, many organisations find that the additional cost of supporting such duplication make them uncompetitive.

A recent example of down-sizing has been seen in one of the world's giant oil corporations, Shell Exploration and Production. At a time when the dollar price of oil was very low, the organisation found it had to justify and sustain the position of four administration staff for every off-shore production worker. Cost cutting had to take place. Shell decided to close their large prestigious offices in London and base their European Operations headquarters in Aberdeen. This move meant considerable numbers of job losses but resulted in significant savings for Shell.

## **Stakeholders**

There are many groups of people who have an interest, financial or otherwise, in the performance of a business – these different groups are known as stakeholders. The main stakeholders are considered to be:

### ***Owners/Shareholders***

These people have a clear financial interest in the performance of the business. They have invested money into the company through purchasing shares and they expect the company to grow and prosper so that they receive a healthy return on their investment. The return that they receive can come in two forms. Firstly, by a rise in the share price, so that they can sell their shares at a higher price than the purchase price (this is known as making a capital gain). Secondly, based on the level of profits for the year, the company issues a portion of this to each shareholder for every share that they hold (this is known as a dividend). The shareholders are also entitled to vote each year at the A.G.M. to elect the Board of Directors, who will run the company on their behalf.

### ***Employees***

This group also has an obvious financial interest in the company, since their pay levels and their job security will depend on the performance and the profitability of the business. It is employees who perform the basic functions and tasks of the business (producing output, meeting deadlines and delivery dates, etc.) and over recent years their traditional role has started to change. They are often now encouraged to become involved in multi-skilled teamworking, problem solving and decision making – thus having a significant input to the workings of the business

### ***Customers***

Customers are vital to the survival of any business, since they purchase the goods and services which provides the business with the majority of its revenue. It is therefore vital for a business to find out exactly what the needs of the consumers are, and to produce their output to directly satisfy these needs - this is done through market research. The goods and services must then be promoted in such a way as to appeal to the target market and to inform them of the availability, price, etc. Once the goods and services have been purchased by the customer, it is essential that after-sales service is offered and that the customer is happy with his/her purchase. The business must try to keep the customer loyal so that they return in the future and become a repeat-purchaser.

### ***Suppliers***

Without flexible and reliable suppliers, the business could not guarantee that it will always have sufficient high quality raw materials which they require to produce their output. It is important for a business to maintain good relationships with their suppliers, so that raw materials and components can be ordered and delivered at short notice, and also so that the business can negotiate good credit terms from the suppliers (i.e. buy now, pay at a later date).

## ***The Government***

The government affects the workings of businesses in many ways:

1. Businesses have to pay a variety of taxes to central and local government, including Corporation tax on their profits, Value-Added Tax (V.A.T) on their sales, and Business Rates to the local council for the provision of local services.
2. Businesses also have to adhere to a wide-ranging amount of legislation, which is aimed at protecting the consumers, the employees and the local environment from business activity.
3. Businesses will be affected by different economic policies, (for example, if interest rates are increased, then this will discourage businesses from borrowing money since the repayments will now be significantly higher). However, businesses can also benefit from government incentives and initiatives, such as new infrastructure, job creation schemes and business relocation packages, offering cheap rent, rates and low-interest loans.

## ***The Local Community***

Businesses are likely to provide significant amounts of employment for the local community and often will produce and sell much of their output to the local residents. The sponsorship of local events and good causes (such as local charity work) can also help the business to establish itself in the community as a caring, socially responsible organisation. Many businesses develop links with local schools and colleges, offering sponsorships and resources to these under-funded institutions. However, businesses can also cause many problems in local communities, such as congestion, pollution and noise, and these negative externalities may often outweigh the benefits that the businesses bring to the community.

## **Disagreements between Stakeholders**

As stakeholders do not all have the same interest in an organisation, conflict can arise between them. For example, a business may want to maximize profits, whereas its customers will want to buy goods at the lower price. A business may want to build a new factory, but the local community may object as it could harm their local environment. The owners of a business may want to close a factory to cut costs but employees will not want to lose their jobs.

Due to the demands placed on businesses by so many different stakeholders, it is no surprise that there are often disagreements and conflict between the different groups. Some of the more common areas of conflict are:

## ***Shareholders and Management***

Profit maximisation is often the over-riding objective of shareholders – resulting in large dividend payments for them. However, it is far more likely that the managers of the business will aim to profit satisfy rather than profit maximise (that is, they will aim to earn a satisfactory level of profits, and then use the remaining resources to pursue other objectives

such as diversification and growth). This conflict between these two groups is often referred to as divorce of ownership (the shareholders) and control (the management).

### ***Customers and the Business***

Customers are unlikely to remain loyal and repeat purchase from the business if the product that they have purchased is of poor quality and/or is poor value for money. More customers are prepared to complain about the quality of products and after-sales service than ever before, and the business must ensure that it has in place a number of strategies designed to satisfy the disgruntled customer, reimburse any financial loss that they may have incurred and persuade them to remain loyal to the business.

### ***Suppliers and the Business***

Suppliers are often quoted as complaining about the lack of prompt payments from businesses for deliveries of raw materials, and if this became a regular problem then the suppliers may well refuse credit to the businesses or may even cease all dealings with them. On the other hand, many businesses have been known to complain about the late deliveries of raw materials and components from suppliers, and the dubious quality of the parts once they have been inspected.

### ***The Community and the Business***

As outlined previously, the local community can often suffer at the hands of a large company through the negative externalities of pollution, noise, congestion and the building of new factories in areas of outstanding beauty. However, if the business faces strong protests from residents and from pressure groups concerned about its actions, then it may decide to relocate to another area, causing much unemployment and a fall in investment in the community it leaves behind.

Examples include:

- Employees and owners – working conditions, training, wages.
- Customer and owner – quality, provision of after-sales service, price of product/service.
- Supplier and owner – price of products, quality, delivery.
- Government and owner – taxation, meeting legislation.
- Local Government and owner – pollution.

Stakeholders can exert influence on organisations in a variety of ways:

- Ordinary shareholders have voting rights at the Annual General Meeting of limited companies.
- Managers have day-to-day decision-making powers.
- Employees may take industrial action, such as strikes or working to rule, to persuade the organisation to do what they want.

- Suppliers can vary the period of credit and/or the level of discount offered to firms.
- Customers influence firms by buying, or refusing to buy, their output. For example in the 1980s some customers stopped buying Nestlé products in an attempt to deter the firm from supplying powdered baby milk to third world countries.
- Banks have the power to grant or withhold loans to firms and to set the rate of interest charged.
- The government can introduce laws to make firms carry out its wishes – for example, the Sex Discrimination Act has made it illegal for firms to refuse to employ a man or a woman simply because of their gender.
- The community as a whole can persuade firms to do as it wants through pressure groups such as Greenpeace, etc.
- Donors can influence what charities do by altering the amount of money that they donate. If a charity does something with which many donors do not agree, it may receive less money from them.
- The local community can influence how businesses in their area behave through the local newspapers (e.g. by writing letters for or against things the business has done); or through protesting against a business's decisions such as the closure of a factory.
- Local government can influence business organisations through planning and other legislation for which local government are responsible. They can also provide help through the creation of suitable sites for businesses such as business parks.

### Stakeholders – Interest and Influence

Internal Stakeholder	Interest	Influence
Shareholder	They want the firm to be profitable to provide them with good dividends and improved share value.	They can exert influence on the firm by voting for particular directors and approving dividend payments at the AGM.
Manager	They receive salaries and perhaps bonuses so they will want the organisation to be successful. They also want responsibility and status.	They make important decisions regarding hiring staff, product portfolio, etc. This may or may not be successful.
Employees	They want good salaries, job satisfaction and job security.	They can exert influence by the standard of their work and industrial relations (e.g. strikes).



External Stakeholder	Interest	Influence
Customers	They want best quality products from organisations at the lowest prices.	Customers can choose to buy or not to buy an organisation's products or services. This influences the products and services an organization makes/gives. Customers may recommend the organization to family/friends.
Banks/other lenders	They will want to ensure that a business applying for a loan or with an existing loan has sufficient funds to make agreed repayments.	They can exert influence by granting or withholding loans, setting loan interest rates, or requesting repayments of loans if an organisation's ability to make repayments is in doubt.
Suppliers	A supplier will want a business to be a success to ensure repeat custom as they depend on their custom for survival.	They can exert influence by changing prices, credit periods and discounts offered.
Local Community	Companies produce employment therefore generating wealth for a area, communities also have an interest that their environment is not harmed by noise or pollution.	They can exert influence by petitioning companies or making complaints to their local authority.
Central Government	They want the business to be successful as they provide jobs, generate wealth and provide government with finance through taxes.	They can exert influence by producing legislation which businesses must comply with, e.g. health and safety, environmental laws, etc. Economic policies affect businesses, e.g. interest rates, inflation, etc. If interest rates are increased the cost of businesses borrowing finance increases.

Local Government	They want businesses to be successful as they provide jobs and make payments of business rates. A council can receive a good image if it can attract and retain successful organisations. Local government also want the service it provides, e.g. schools, to be successful, to meet central government targets, provide them with a good image and be able to justify budget spending.	They can exert influence on businesses by granting or not granting licenses for hotels and pubs, providing subsidized premises, or granting planning permission. They also influence the services they provide, e.g. schools, by allocating funding from council budget and setting operational policies for services.
Charity donors	Corporate donors will want the charity that they donate to; to be successful as it may provide them with good public relations.	They can exert their influence on a charity by giving or not giving donations. Donors of large amounts of money may specify the use to which their donation is put.
Taxpayers	They have an interest in publicly funded organisations to ensure that the taxes that they paid are used effectively.	They exert influence by voting for political parties at national and local government elections.