

Section 1: Understanding business activity

This section introduces you to the basic building blocks of business studies. You will learn about the nature and purpose of business activity and the importance of needs, wants, scarcity, opportunity cost, specialisation and adding value. You will find out how business activities are classified, for example in the private sector or public sector, and how this classification affects business objectives. You will also learn about the advantages and disadvantages of different forms of business and the role of entrepreneurs. The activities of all businesses affect several different groups of people. These groups, or stakeholders, will have their own objectives for the business and you will learn what these are and how they may influence or be influenced by the activity of the business.

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Objectives

In this chapter you will learn about:

- needs, wants, scarcity and opportunity cost
- the importance of specialisation to businesses and consumers
- the purpose of business activity
- what is meant by 'added value'
- how a business adds value.



KEY TERMS

Business activity: the process of producing goods and services to satisfy consumer demand.

Need: a good or service which is essential to living.

Want: a good or service which people would like, but is not essential for living.



TOP TIP

It is important to learn key terms. They are not only important when answering questions, but many in this chapter will help you to understand topics in later chapters.

Business activity

Introduction

The business world is all around us. From the minute we get up in the morning to when we go to bed at night, we are using things made by businesses around the world. Think about the food you eat, the clothes you wear, the bus or train you came to school on this morning, the music CDs you listen to, even this book – all these were made by businesses.

Businesses provide us – consumers – with all the goods and services that we need and would like to have. In this chapter you will learn about the purpose of business. You will look at how businesses turn resources into goods and services to meet all our needs and wants.

The purpose and nature of business activity

Needs and wants

The purpose of **business activity** is to provide consumers – that's you and me – with goods and services that meet our needs and wants. But what are **needs**? How are they different from **wants**?

A need is any good or service which people must have to be able to live. Water, food, shelter and clothing are essential needs for living.

Wants are different. They are any goods or services which people would like to have. They are not essential for living. Mobile phones, cars and holidays are good examples.



Customers in a shop

ACTIVITY 1.1

- 1 Make a list of your ten most important 'wants'.
- 2 Do you own any of these items? If not, why not?
- 3 If you are lucky enough to own all of these items, does this mean that you no longer have any wants?

You have probably identified things that you still want. The main reason you may have given for not having all of your wants is you may not have enough money to buy them. Even if you are able to buy these wants in the future, you may have other wants. This is because our wants are unlimited.

Throughout the world there are many people who are so poor that they cannot afford to buy the things they need for living, let alone afford their wants. So, some people cannot afford to buy their basic needs. Others, who can afford their basic needs, cannot afford to buy what they want. Surely, then, the cause of these problems is that consumers do not have enough money! Let's see if this is the case.

ACTIVITY 1.2

A very small island country has the following supplies of the four groups of goods and services identified as basic needs.

Basic need	Quantity available
Water	50,000 litres
Food	10,000 kilos
Clothing	8,000 units
Housing	400

The country has a population of 500 families. Each family unit must have the following quantities of each basic need for essential living.

Basic need	Quantity needed per family unit
Water	100 litres
Food	25 kilos
Clothing	20 units
Housing	1

In small groups:

- 1 Using the information in the tables, calculate whether there is enough supply of basic needs in this country to support the essential living of all the families.
- 2 If 100 people in the country had a much higher income than the rest of the population, what may happen?



KEY TERMS

Economic problem: unlimited wants cannot be met because there are limited factors of production. This creates scarcity.

Factors of production: the resources needed to produce goods and services – land, labour, capital and enterprise.



TOP TIP

The term ‘capital’ has several meanings in business. Make sure you understand its meaning as a factor of production.

Scarcity and opportunity cost

In Activity 1.2, you may have worked out that money alone cannot solve the problem. There are just not enough goods and services to meet the needs and unlimited wants of all consumers – this is known as the **economic problem**. If this is the case, then the answer is simple – produce more goods and services! Unfortunately, the answer is not so simple. To understand why not, first we need to look at **factors of production**.

The production of goods and services requires four factors of production:

- **Land** is all natural resources such as minerals, ores, fields, oil and forests.
- **Labour** is the number of people available to work.
- **Capital** is machinery, equipment and finance needed for production of goods and services.
- **Enterprise** is people prepared to take the risk of setting up businesses – they are known as entrepreneurs.

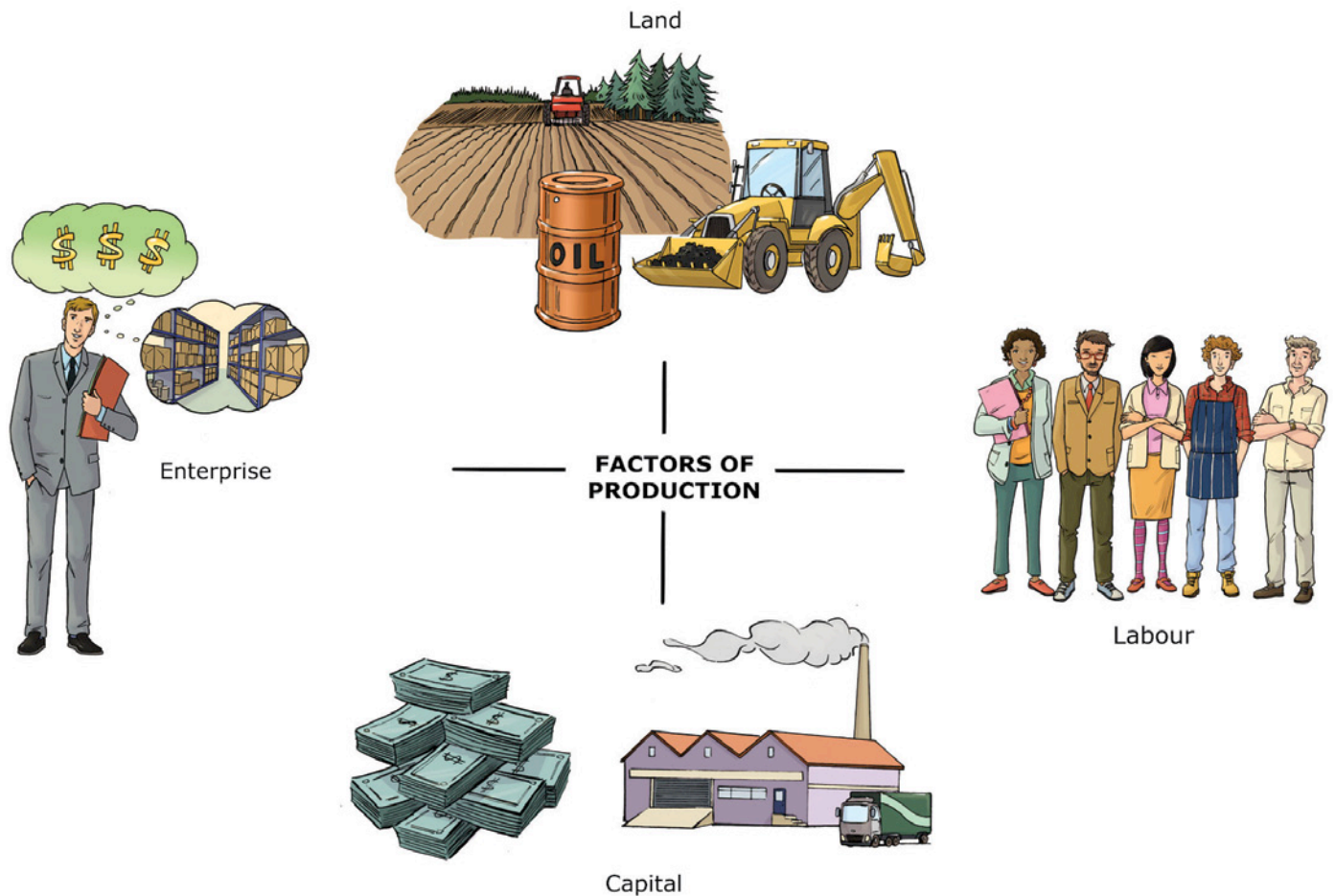
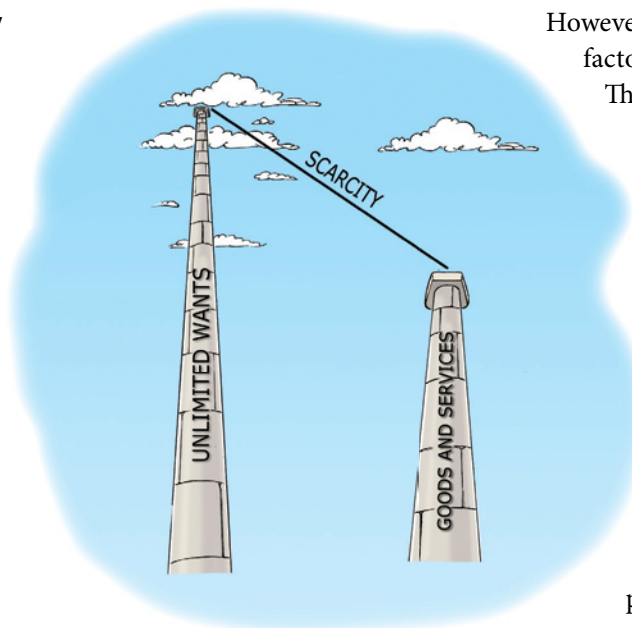


Figure 1.1 Factors of production

Figure 1.2 Scarcity



However, there are not enough of these factors of production in the world.

This means that it is not possible to make all the goods and services needed or wanted by the world's population. In other words, the unlimited wants of consumers cannot be satisfied because of limited factors of production required to produce the goods and services to meet those wants. This is the problem of **scarcity**.

We have seen that there are not enough resources to produce all the goods and services needed to meet consumers' wants. So, choices have to be made.

We all make choices in our everyday lives. Do you choose to go to the cinema with friends or spend the money on a new computer game? Perhaps you have enough money to buy the latest CD release from your favourite pop star, or you can use the money to buy a Business Studies revision textbook. Whichever decision you make will mean that you will have to give up the chance of having the other. When making the choice you need to make sure that the product or service you choose is worth more to you than the one you give up. The next best alternative you give up is known as the **opportunity cost** of your decision.



KEY TERMS

Scarcity: there are not enough goods and services to meet the wants of the population.

Opportunity cost: the benefit that could have been gained from an alternative use of the same resource.

ACTIVITY 1.3

Fatima works in a bakery and earns \$120 per week. Fatima's grandfather has given her \$5,000. Fatima is going to use this money to start her own business. She is going to make cakes for special occasions such as birthdays, weddings and religious festivals.

- 1 Give an example for each of the four factors of production Fatima will use in her new business.
- 2 What is the 'opportunity cost' to Fatima of her decision to start her own business?
- 3 Is Fatima's business meeting consumer 'needs' or consumer 'wants'? Justify your answer.



EXPLORE!

Use newspapers, library resources or the internet to research the things that your government spends money on.

Have a class discussion about the opportunity cost of these spending decisions. If you were a member of the government would you spend the money differently?

It is not only consumers like you who have to make choices about how to use scarce resources. Businesses and governments also have limited resources and must choose between alternative uses of those resources. For example, a business might have to choose between using resources on an advertising campaign, or on a training programme for its workers. A government might have to choose between building a new school or a new hospital.

Importance of specialisation

We have seen how consumers, businesses and governments must make choices. They must do this because of the scarcity of goods and services which results from limited factors of production. For this reason, it is very important that the



Figure 1.3 A single worker and the production process

factors of production are not wasted on the production of goods and services that consumers do not need or want.

Most goods and services are produced by more than one person. The production process often uses machinery and equipment which has been specially designed to produce a specific good. This is very different from the production that would have taken place hundreds of years ago. Then a product would have been produced by just one person using machinery and equipment which was far less specialised.

The increasing **specialisation** of factors of production has meant that businesses are far more efficient than they once were. Specialisation reduces the costs of production. This benefits consumers by providing more goods and services at lower prices than before specialisation took place. A good example of specialisation in business is Microsoft, which develops and produces computer software.



KEY TERM

Specialisation: people and businesses concentrate on what they are best at.

CASE STUDY

Making footballs

Global Sports manufactures sports equipment. Their most popular product is footballs.

To make one football requires five workers. Each worker completes a separate task, usually with the aid of specialised machinery.

The five stages in making a football are:

- 1 Panels are cut out of sheets of leather.
- 2 A design and logo is stamped on panels.
- 3 Panels are stitched together into the shape of a football.
- 4 The bladder is inserted into the ball.
- 5 The ball is moulded into the correct shape and inflated to the correct pressure.



Making a football

TASK

- a Identify an example of the factor of production, 'capital'.
- b Use the information here to explain what is meant by 'division of labour'.
- c Identify **two** reasons why Global Sports benefits from specialisation.
- d Identify and explain **one** benefit to Global Sports and **one** benefit to its customers of specialisation.



Labour productivity: see Chapter 15, page 204.

**KEY TERM**

Division of labour: production is divided into separate tasks and each worker does just one of those tasks.

**EXPLORE!**

Use the internet, newspapers and other resources to research businesses in your country which only produce or supply one type of product. For example, look at farmers to see if they only grow one type of cereal, or only rear one type of animal. Are there any retailers or professionals who only supply one type of good or service?

What do you think are the benefits and limitations to these businesses of specialising in the production or supply of just one type of good?

Specialisation of labour is now commonplace in the workplace. Instead of workers producing one product from start to finish, they focus on just one skill. The production of a product now requires several workers, each using their skill. This is an example of the **division of labour**. Since each worker is now specialising in just one skill, they become far more efficient and this increases the productivity of labour.

In the past, most products were made by workers with only basic tools and equipment. The development of machinery and advances in technology have changed the production process. Machinery and equipment have become far more specialised and this has greatly increased the efficiency of capital.

Even entrepreneurs have realised the benefits of specialisation. There are many examples of businesses that specialise in the production or supply of just one type of product.

Purpose of business activity

We have already learned that businesses take scarce resources – factors of production – and use these to produce the goods and services demanded by consumers. Without the activity of business there would be no products and services.



Figure 1.4 The purpose of business activity

Businesses produce different types of goods and services. These are known as:

- consumer goods
- consumer services
- capital goods.

Consumer goods

Consumer goods are those goods which are sold to the public that they can see (physical goods) and touch (tangible goods). These can be divided into durable and non-durable consumer goods:

- Durable consumer goods can be used over and over again, for example televisions, computers, cars, table and chairs.
- Non-durable consumer goods can only be used once, for example food and drink.

**KEY TERM**

Consumer goods: products which are sold to the final consumer. They can be seen and touched, for example computers and food.



Figure 1.5 Consumer goods



KEY TERMS

Consumer services: non-tangible products such as insurance services, transport.

Capital goods: physical goods, such as machinery and delivery vehicles, used by other businesses to help produce other goods and services.

Consumer services

Consumer services are products which are also sold to the public, but they cannot be seen or touched (intangible), for example insurance, banking and bus journeys. You can see and touch the buildings where insurance and banking services take place and you can obviously see and touch a bus, but you are not buying these items, you are using a service which they provide and this service cannot be seen or touched.



Figure 1.6 Consumer service

Capital goods

Capital goods are products which are sold to other businesses to help them in their production process. These are physical goods such as machines, computers and delivery vehicles.

CASE STUDY

RT Products (RTP) is a manufacturer of printers. It also manufactures replacement ink cartridges for its printers. Each worker assembles all of the different components into making one computer. The Operations Director is considering introducing division of labour into the production of computers.

RTP has recently invested in new computer-controlled equipment to help manufacture printer cartridges. Last year it produced 600,000 printer cartridges. RTP will be able to produce 30% more cartridges this year.

RTP sells its printers to businesses and private individuals for use with their computers at home.

TASK

- Calculate the number of printer cartridges RTP will be able to produce this year.
- Use the information here to explain the difference between 'consumer goods' and 'capital goods'.
- Do you think the Operations Director should introduce division of labour into the production of printers? Justify your answer.

Adding value

Whatever good or service a business produces, it will try to add value at every stage of the production process. It does this by taking raw materials and turning them into a good or service which it sells to customers at a price greater than the cost of the raw materials used in their production. Added value is one of the most important objectives of business. Figure 1.7 shows how value is added in the production of a cake.



Figure 1.7 Adding value

How businesses increase added value

Added value is not the same as profit. You will learn later how a business calculates profit. All you need to know now is that other costs such as workers' wages and energy costs must be deducted from the added value to calculate profit.

Profit will increase if a business is able to increase its added value without increasing its costs. In practice, it is difficult to increase value without increasing costs. If the increase in added value is greater than the costs of achieving it, profits will rise.

There are a number of different ways a business can increase its added value.

Branding

Have you ever wondered why Coca-Cola, Sony, and other well-known companies spend huge sums of money on advertising and other promotional activities? They do this to build and then maintain their brand. The products produced by each of these companies all have close substitutes – that means you can buy other brands of drink and electronic goods. However, these companies are able to charge a higher price than their competitors, even though the costs of production are likely to be quite similar. Branding increases added value because people want or feel they should buy the item from this particular company.



A Subway outlet in Asia



How a business calculates profit: see Chapter 21, page 269.



TOP TIP

Try to read local and national newspapers as often as you can. There are lots of business articles. You may not understand everything, but it will help you to have a better understanding of business, especially in your country. You could cut out any articles or advertisements you think may be useful later in the course. You could bring them into school for your teacher to keep as a resource for future lessons.

ACTIVITY 1.4

Name your top ten brands. Then cut out advertisements from newspapers and magazines and make a poster.

**Excellent service quality**

In some industries providing a high quality, personalised service, can be the difference between able to charge a high price or one which is much lower. The price of a made-to-measure suit will be higher than the price of a ready-made suit. The cost of the materials used will be very similar, but the personalised service increases the added value.



Personalised service increases the cost of the product

Product features

Products that have more features and functions than similar products on the market will allow the producer to charge a higher price. Although these additional features will increase costs, consumers are prepared to pay a much higher price than they would pay for a product with fewer features or functions. The mobile phone market is a very good example of how features and functions are used to increase the product's added value.

Convenience

Many consumers lead busy lives and they are often prepared to pay a higher price for goods and services which they can have immediately or which save them time, for example ready meals.

ACTIVITY 1.5

Explain how these businesses add value:

- restaurant
- shoe manufacturer
- house builder
- florist.