

Knowledge Organisers

OCR GCSE (9-1) Business - Year 11 – Business 2

7 - The interdependent nature of business

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| Key words | |
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| Financial information | Includes information about revenues, costs, profit, rates of return, break-even and cash flow. Financial information helps a business to make decisions. |
| Non-financial rewards | To owners, this includes the satisfaction of running a successful business, being in charge, being independent and having an impact on what consumers buy. |
| Non-financial risk | To business owners, this includes their health due to stress and strained relationships with family and friends. |
| Business performance | A measure of how well a business is doing. Key measures are sales, profits and rates of return. |
| Financial reward | The profit made by business. |
| Financial risk | The possibility a business will lose money from decisions it makes. Owners may lose money they have invested. |

The interdependent nature of business operations, finance, marketing and human resources with a business context and how these interdependencies underpin business decision making

The interdependent nature of business refers to the links between different areas of business that affect decision making, the risks and rewards of business activity and the use of financial information to aid business decision making.

The 4 different business functions are business operations, finance, marketing and human resources. The following examples show the interdependent nature of business and some links between departments.

Example

Link

- Business operations (producing goods or services) and human resources (workers).
- The *amount* that a business produces and *how* a business produces will link with the number and type of workers it needs.

Decisions

- A gardening business may want to increase the number of customers it has. It is likely to need to increase the number of gardeners it employs, in order to carry out work for new customers.
- A firm manufactures and fits signs, including road signs and signs placed on or outside buildings. It wants to increase production. It may be able to do this by introducing new technology such as robots to carry out the manufacturing process. This may require more skilled specialists to control the technology. It may need to employ more fitters to fit the signs. It might be able to lay off some workers whose job can now be done by new technology.

Example

Link

- Business operations and finance.

Decisions

- A business wishes to expand production by building a new factory.
- The finance department will have to arrange finance for this, perhaps by selling shares or taking out a bank loan.

Example

Link

- Business operations and marketing.

Decisions

- A firm wishes to increase production.
- The marketing department may decide to increase advertising and other marketing activities to make sure the business can sell the increased output. It may also change its marketing, for example, advertising nationally rather than just locally.

Example

Link

- Finance and marketing.

Decisions

- A firm may want to increase its marketing to introduce a new product or because of increased competition.
- The finance department will have to finance this spending, perhaps by arranging an overdraft or finding the money in the business' reserves.

Questions

Identify the links between different business functions.

Challenge Activity

Analyse how different business functions may be linked.

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7 – The interdependent nature of business (continued)

Impact of risk and reward on business activity and the use of financial information in measuring and understanding business performance and decision making

Businesses use financial information to help make decisions. The information can help to maximise profit and reduce the chances of making a loss. Business information can be either forecasts or records. While business information is useful in making decisions, businesses must think about other things that can affect their decisions eg

- new competition entering a market which could affect sales, prices and expected revenues
- changes in costs eg wages, that will be affected by levels of unemployment, while material costs that will be affected by a world shortage or a change in the exchange rate of the pound

When making decisions, businesses also need to consider the impact of non-financial risk and non-financial rewards. The following examples show how financial information can measure performance and help decision making.

Example

Decision: Is the business making a good profit?

Profit figures may help with this judgement, but a better way to decide is to calculate the average rate of return (ARR), which gives owners a percentage rate of return on their investment. A business' ARR can be compared with that made by other businesses, or with how much they could earn in interest by saving their money. This can help a business decide whether its performance is good enough, if changes are needed to improve **business performance**, if it should switch its investment to a different line of business or simply save its money instead.

Questions

State the financial information a business should use for different types of decisions.

Challenge Activity

Analyse and evaluate financial information to make recommendations about business decisions.

Example

Decision: Increasing sales revenue

A business may decide it needs to increase sales revenue to increase profits. Revenue can be increased by raising the price of what it sells or increasing the amount it sells. A rise in price usually leads to lower sales, although sales revenue may rise if sales do not fall very much. Financial information predicting the effects of changes in price will help the business to make this decision.

Example

Decision: Reducing costs

A business may decide to increase its profits by reducing costs, through the introduction of new technology. Using financial information, it could calculate the cost of buying and using the new technology and any savings that might result by reducing the amount of labour it employs.

Example

Decision: Producing a new product

A business may want to produce a new product. Break-even analysis will help the business decide how many it must sell, and at what price, to make a profit. If the business does not think it can sell this amount, it may decide not to produce the new product so that it does not make a loss on it. Alternatively, it may look at ways of reducing the cost, or raising the price, to make the new product profitable.

Example

Decision: How to finance business activities

A cash flow forecast may show that a business will have a negative cash flow for a time. The business may consider having an overdraft or using trade credit, if possible. From the cash flow forecast the business could find out how much finance it will need, and for how long. This information, and the interest rate it would be charged for the period, could be used to calculate the cost.