Cambridge

AS - Level

Business studies

CODE: (9609)

Unit 01- Chapter 03

Size of business

Introduction

Businesses range from small traders to multinational corporations, with measurements being used to compare sizes and assess growth or contraction. This information is important for managers, investors, and governments, as small firms provide benefits to the economy and often receive special assistance. The chapter focuses on how businesses can expand and their impact on stakeholders.

Measuring business size

It is common to compare businesses by their size. Who wants to know how large a particular business is? The government might wish to give assistance to 'small' firms, so will need a measure of size.

There are two problems with these and other requirements for a way of measuring business size:

1. There are several different ways of measuring and comparing business size and they often give different comparative results. A firm might appear large by one measure but quite small by another.

2. There is no internationally agreed definition of what a small, medium or large business is, but the number of employees is often used to make this distinction.

Different measures of size

1. **Number of employees**. This is the simplest measure. It is easy to understand – for example, it is obvious to everyone that a shop run by just the owner or their family is small.

2. **Revenue** - **Revenue** is often used as a measure of size – especially when comparing fi rms in the same industry. It is less effective when comparing fi rms in different industries because some might be engaged in 'high-value' production, such as precious jewels, and another might be in 'low-value' production, such as cleaning services.

KEY TERM

Revenue: total value of sales made by a business in a given time period.

3. **Capital employed** Generally, the larger the business enterprise, the greater the value of capital needed for long-term investment, or the greater the amount of **capital employed.**

KEY TERM

Capital employed: the total value of all long-term finance invested in the business.

KEY TERM

Market capitalisation: the total value of a company's issued shares.

4. **Market capitalisation** - Market capitalisation can be used only for businesses that have shares quoted on the stock exchange (public limited companies). It is calculated by this formula:

$$\text{Market capitalisation} = \text{current share price} \times \text{total number of shares issued}$$

5. **Market share -** Market share is a relative measure. If a fi rm has a high market share, it must be among the leaders in the industry and comparatively large.

$$\frac{\text{total sales of business}}{\text{total sales of industry}} \times 100$$

KEY TERM

Market share: sales of the business as a proportion of total market sales.

Other measures that can be used

These will depend very much on the industry. The number of guest beds or guest rooms could be used to compare hotel businesses. The number of shops could be used for retailers.

Which form of measurement is best?

There is no 'best' measure. The one used depends on what needs to be established about the fi rms being compared. This could depend on whether we are interested in absolute size or comparative size within one industry.

The significance of small and micro-businesses

Even though we have not established a universally agreed definition of small fi rms, it will be easy to identify them within your own economy. They will employ few people and will have a low turnover compared to other firms. The official definition within your own country could be discovered from the trade and industry department.

Encouraging the development of small business units can have the following benefits:

■ Many jobs are created by small firms and, even though each one may not employ many staff , collectively the small business sector employs a very significant proportion of the working population in most countries.

■ Small businesses are often run by dynamic entrepreneurs, with new ideas for consumer goods and services. This helps to create variety in the market and consumers will benefit from greater choice.

■ Small firms can create competition for larger businesses. Without this competition, larger firms could exploit consumers with high prices and poor service. The cost of air travel has been reduced in recent years due to the establishment of many small airlines competing with the large, established companies.

■ Small firms often supply specialist goods and services to important industries in a country. For example, the global car industry is dominated by major manufacturers such as Toyota, BMW and Ford.

■ All great businesses were small at one time. The Body Shop began in one small, rented store in 1976. Hewlett-Packard started assembling electrical equipment in Packard's garage! The large firms of the future are the small firms of today – and the more small firms are encouraged to become established and expand, the greater the chances that an economy will benefit from large-scale organisations in the future.

■ Small firms may enjoy lower average costs than larger ones and this benefit could be passed on to the consumer too. Costs could be lower because wage rates paid to staff may be less than the salaries paid in large organisations, or the sheer cost of the administration and management structure of bigger enterprises may increase their costs dramatically.

Business category	Employees	Revenue	Capital employed
Medium	51–250	over €10m to €50m	over €10m to €34m
Small	11–50	over €2m to €10m	over €2m to €10m
Micro	10 or fewer	up to €2m	up to €2m

Table 3.1 EU classifications of business size

Government assistance for small businesses

Most governments provide special assistance for small businesses (see also Table 3.2). These include:

1. Reduced rate of profits tax (corporation tax) – this will allow a small company the chance to retain more profits in the business for expansion.

2. Loan guarantee scheme – this is a government-funded scheme that guarantees the repayment of a certain percentage of a bank loan should the business fail.

3. Information, advice and support will be provided through the Small Firms agency of the Department for Business, Innovation and Skills.

4. Other aid is designed to help small firms overcome the particular problems that they frequently experience. These include:

■ Lack of specialist management expertise – often the owner has to undertake all management functions, such as marketing, operations management, keeping accounts and dealing with staff matters, because the business cannot afford to employ specialists in each of these areas.

■ Problems in raising both short- and long-term fi nance – small firms have little security to off er banks in exchange for loans and this makes obtaining finance much more difficult than for most larger firms.

■ Marketing risks from a limited product range – many small firms produce just one type of good or service – or at least a very limited range of them.

■ Difficulty in finding suitable and reasonably priced premises.

India	Trinidad and Tobago	United Kingdom
Small Industries Development Organisation: ■ credit guarantee scheme ■ micro-finance programme ■ capital subsidy scheme for technology upgrading National Small Industries Corporation: ■ marketing support scheme for small firms ■ credit support scheme, e.g. for marketing activities and purchase of raw materials ■ technology support scheme, e.g. application of new technologies in small businesses	Venture Capital Incentive Programme: ■ increase in supply of share capital to new enterprise sector ■ tax credits offered to investors in new businesses National Enterprise Development Company: ■ financial support to small businesses ■ professional advice to entrepreneurs on marketing, business management and business planning Ministry of Social Development: ■ offers financial assistance to underprivileged persons to set up micro-businesses ■ help with writing business plans	■ National Department for Business and Enterprise Grant for Research and Development by Small Businesses ■ Regional Selective Assistance scheme offers grants to small firms that invest capital in areas of high unemployment and create jobs – up to 35% capital grants available ■ England Rural Development Programme offers grants to farmers for conversion of rural buildings for use by small businesses and for farm diversification programmes

Advantages of small businesses	Advantages of large businesses
■ can be managed and controlled by the owner(s) ■ often able to adapt quickly to meet changing customer needs ■ offer personal service to customers ■ find it easier to know each worker, and many staff prefer to work for a smaller, more 'human' business ■ if family-owned, the business culture is often informal, employees well-motivated and family members perform multiple roles	■ can afford to employ specialist professional managers ■ benefit from the cost reductions associated with large-scale production (see Chapter 23) ■ may be able to set low prices that other firms have to follow ■ have access to several different sources of finance ■ may be diversified in several markets and products so that risks are spread ■ are more likely to be able to afford research and development into new products and processes

Table 3.3 Potential advantages of small and large businesses

Strengths and weaknesses of family businesses

Family-owned businesses are those that are actively owned and managed by at least two members of the same family. In many cases, the family that founded the business retains complete ownership of it.

Business growth

The owners of many businesses do not want the fi rm to remain small – although some do, for reasons of remaining in control, avoiding taking too many risks and preventing workloads from becoming too heavy.

Why do other business owners and directors of companies seek growth for their business? There are a number of possible reasons:

■ Increased profits – expanding the business and achieving higher sales is one way of becoming more profitable.

■ Increased market share – this will give a business a higher market profile and greater bargaining power with both suppliers (e.g. lower prices) and retailers (e.g. best positions in the shop).

■ Increased economies of scale
■ Increased power and status of the owners and directors
■ Reduced risk of being a takeover target – a larger business may become too large a target for a potential 'predator' company.

Strengths	Weaknesses
Commitment: The family owners often show dedication in seeing the business grow, prosper and get passed on to future generations. As a result, many family members identify with the company and have the incentive to work harder and reinvest part of their profits into the business to allow it to grow in the long term. **Reliability and pride:** Because family businesses have their name and reputation associated with their products, they strive to increase the quality of their output and to maintain a good relationship with their stakeholders. **Knowledge continuity:** Families in business make it a priority to pass their accumulated knowledge, experience and skills to the next generation. Many family members become involved in the family business from a very young age. This increases their level of commitment and could provide them with the necessary tools to run their family business.	**Succession/continuity problem:** Many family businesses fail to be sustainable in the long term. On average only around 15% continue into the third generation of the descendants of the founder(s). This high rate of failure among family businesses can often be explained by the lack of skills and ability of later generations or the splitting of management responsibilities between several family members to give them all a role in it. **Informality:** Because most families run their businesses themselves, there is usually little interest in setting clear and formal business practices and procedures. As the family and its business grow larger, this situation can lead to inefficiencies and internal conflicts. **Traditional:** There is quite often a reluctance to change systems and procedures, preferring to continue to operate as it was historically run. Lack of innovation could be a consequence. **Conflict:** Problems within the family may reflect on management of the business and make effective decisions less likely.

Table 3.5 Strengths and weaknesses of family businesses

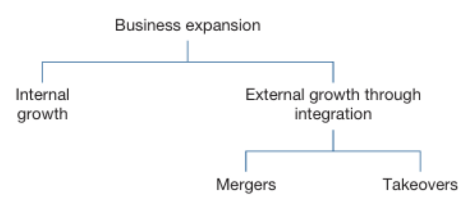

Figure 3.1 Different forms of growth

Internal growth

Business growth can be achieved in a number of ways and these forms of growth can lead to differing effects on stakeholder groups, such as customers, workers and competitors. The different forms of growth can be grouped into internal and external growth.

> **KEY TERM**
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> **Internal growth:** expansion of a business by means of opening new branches, shops or factories (also known as organic growth).

Revision questions

Q1.9707/12/O/N/2011/Q4 (b)
Explain two objectives a small business might have in the first year of trading. [3]

Q2.9707/11/M/J/2011/Q1 (b)
Describe two methods for measuring the size of a business. [3]

Q3.9707/12/O/N/2009/Q1 (b)
Briefly explain two objectives a small business might have, other than profits maximization. [3]

Q4.9707/11/O/N/2012/Q1
(a) Define the term 'limited liability '. [2]
(b) Briefly explain two advantages (other than limited liability) a private limited company has over a sole trader. [3]

Q5.9707/13/O/N/2015/Q1
(a) Define the term 'internal growth'. [2]
(b) Briefly explain two reasons why many businesses set growth as an objective. [3]

Q6.9707/12/O/N/2015/Q3
Explain why small business is important for many economics. [5]

Q7.9707/11/O/N/2014/Q1 (a)
Explain the weakness of 'family owned' businesses. [8]

Q8.9707/13/M/J/2011/Q5 (a)
Explain the strengths and weakness of small business. [8]

Q9 .9609/13/M/J/2019/Q5 (a)
Analyse the impact of small business on the development of a country. [8]

Q10.9707/13/M/J/2012 /Q5
(a) Explain the strengths and weakness of 'family owned' business. [8]
(b) Explain internal growth as a way of expanding a business. [12]

Q11.9707/11/M/J/2012/Q5 (b)
Discuss the importance of small businesses to the economy of your country. [12]

Q12.9707/12/M/J/2012/5 (b)
Discuss the factors that could influence the success of a small business. [12]

Q13.9609/12/F/M/2018/Q6
Family retail businesses should stay small rather than setting growth as an objective.' Do you agree? Justify your answer. [20]