

## Growing a business

### Introduction

The growth of a business is when it expands in size. The size of a business can be measured by the following means:

- ▶ **Sales turnover (or sales revenue)**
- ▶ **Number of employees**
- ▶ **Share capital** (the number of shares times the price of each share)
- ▶ **Market share** – the sales of the business of a particular product as a proportion of all sales of that type of product. A 5% market share would mean that 1 in 20 of all products sold are sold by that business.
- ▶ **Number of outlets** (e.g. shops)

They may mean to grow in size or sometimes it just happens without the business making a conscientious effort to do so. Businesses either grow organically or by acquisition and mergers.

- ▶ **Organic growth** means the business grows by expanding its sales or their operations and is financed through its own profits.
- ▶ **Acquisitions and mergers** are when the business joins or buys other businesses, not necessary of the same type.

Businesses may wish to expand for the following reasons:

- ▶ Benefit from **economies of scale** – lower unit costs due to an increase in size
- ▶ A larger **market share** (selling more products than before) means they can charge higher prices and gain more profit
- ▶ As **means of survival** if they wish to compete with other growing businesses

Some businesses start selling or acquiring businesses that are not in the same market as the markets they are presently selling in. This is known as **diversification**.

Businesses may wish to diversify because:

- ▶ Helps **spread the risks across a number of products**. If one product fails due to market conditions then other products in different markets should not be affected.
- ▶ Good way of **expanding** if present market seems already full.
- ▶ Gives the business **fresh objectives** and may act to motivate managers and staff.

A business can **grow organically** in the following ways:

- ▶ **Lower price** - People will buy more at lower prices.
- ▶ **Increase advertising** - Customers are made more aware of the attraction of the products.

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- ▶ **Sell in different location** - Selling to a new set of customers, more potential.
- ▶ **Sell on credit** - Customers are attracted by the ability to buy now pay later.

### Mergers and Acquisitions

A merger is where two or more businesses **AGREE** to join together to become one larger firm. An acquisition is when one firm **BUYS** another firm.

When a one business buys another it is possible that the acquisition or merger integrates the new product with the existing product. This integration can either be vertical or horizontal integration.

Mergers and acquisitions are an important option for larger businesses that wish to grow rapidly. However, they are a high risk strategy – it is easy to buy the wrong business, at the wrong price for the wrong reasons!

The advantages of mergers and acquisitions are:

- Economies of scale, which reduces unit costs.
- Greater market share for horizontal integration, which means the business can often charge higher prices.
- Spreads risks if products different.
- Reduces competition if a rival is taken over.
- Other businesses can bring new skills and specialist departments to the business.
- It is easier to raise money if a larger business.

The disadvantages of mergers and acquisitions are:

- Diseconomies of scale if business becomes too large, which leads to higher unit costs.
- Clashes of culture between different types of businesses can occur, reducing the effectiveness of the integration.
- May need to make some workers redundant, especially at management levels – this may have an effect on motivation.
- May be a conflict of objectives between different businesses, meaning decisions are more difficult to make and causing disruption in the running of the business.

### Constraints on Growth

Though a business may wish to grow in size, there may be reasons why it cannot do this:

- ▶ **Financial limitations** – a business may not be able to raise the necessary finance to grow any bigger – perhaps it has not made enough profits to generate the cash or the bank is not keen to lend it more money at the moment.
- ▶ **Size of the market** – there is often a limit to number of people who are willing to buy the type of product that the business is producing – e.g. a printing press manufacturer will know that there are only a small number of publishers in the UK who will be able to buy the product.

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- ▶ **Government controls** means that a business cannot necessarily have more than 25% of the market share. This often arises when one business joins with another. If the government thinks it is not in the public interest to have such a large business, then the joining together may not take place.
- ▶ **Human resources** are limited in terms of the skills available. Especially in more specialised areas it may be difficult to find enough qualified staff in the area to expand the business. In the South East of England, where unemployment is very low for some types of jobs, businesses have struggled to expand for this very reason.

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