

## Chapter 10

**1. What factors do you think influenced Sainsbury's strategic decision to buy HRG?**

Desire for growth and economies of scale; desire for synergy

**2. Why do you think it decided to do this rather than invest in its own internal growth?**

Faster; buys in existing skills, expertise and links

**3. What risks do you think this strategy of growth brings?**

Culture clashes; management challenges; dangers of diseconomies of scale through coordination, control and communication problems

**4. What actions can Sainsbury's managers take to reduce these risks?**

Prepare for cultural differences; train and educate staff; employ better management and information systems

## Questions

**1. Consider the scale of small businesses in the UK in terms of employment, turnover, and number of businesses. Can you explain this data?**

Most businesses in the UK are small but they account for much smaller proportion of employment and turnover

**2. Look at the trends in Figure 10.3. What do you think has caused these trends?**

Could be more incentives or more pressures to set up on your own e.g. could be easier in terms of government support, regulations; could be more necessary to find employment after redundancy. Could be more of an entrepreneurial culture.

## 10.1 DOING THE BUSINESS MATHS

At which level of output does the business stop benefiting from internal economies of scale? 5,000 units

Output (units)	Total cost (£)	Unit cost (£) = total cost ÷ output
2,000	30,000	15
3,000	42,000	14
4,000	48,000	12
5,000	50,000	10
6,000	60,000	10
7,000	77,000	11

Unit cost

- 15
- 19
- 12
- 10
- 10
- 11

### 10.1 Quick check

For each of the following statements, say whether it is true or false.

- a. A merger occurs when two or more organizations join together to form a new one. TRUE
- b. A takeover occurs when one business gains control over another. TRUE
- c. Vertical integration occurs between businesses at the same stage of the production process. FALSE
- d. Horizontal integration may lead to internal economies of scale. TRUE

### Question

Why do you think consolidation is important in the cinema sector?

- May enable lower unit costs and ability to be more price competitive with rivals and substitutes
- May increase power to bargain with film companies

### Question

#### **Why did Campbell buy Snyder's-Lance?**

To have brands in growing market segments – needs some “healthier products”; using funds from well established but mature markets to develop presence elsewhere.

### Questions

#### **1. What problems with management might have led to the disastrous bid by the Royal Bank of Scotland for ABN Amro?**

Lack of experience; poor decision making; lack of information; culture of risk taking and sense of infallibility

#### **2. What systems and processes could you put in place to make sure a business was well managed at the top?**

Improve recruitment processes, improve selection processes, train better, support better, have better systems in place to monitor actions

### Question

#### **1. Should the regulators have been concerned about the Tesco takeover of Booker's?**

Wanted to investigate the impact of the deal in terms of competition.

Potentially meant Tesco had control of supplies and could increase prices for its competitors. However it was felt there was sufficient competition in the wholesale market for this not to be a problem.

#### **2. On what grounds would you, as a regulator, stop a takeover or merger?**

In there was monopoly power and less choice for customers. If there was a fear that it would lead to higher prices and a poorer service

### 10.2 Quick check

For each of the following statements, say whether it is true or false.

- External growth is often faster than internal growth. TRUE
- Takeovers can lead to internal diseconomies of scale. TRUE
- Horizontal integration can increase the four-firm concentration ratio. TRUE
- Vertical integration can reduce input costs. TRUE

### Question

#### **Explain how a company can be growing its revenue and yet have falling profits.**

Costs may be rising faster than revenue e.g. due to costs of acquisition or acquiring resources

### Quick questions

#### **1. What is an SME?**

Small and medium sized enterprise

#### **2. Why might managers want a business to grow?**

To gain internal economies of scale; to gain power; prestige; for their own CV

#### **3. What is the difference between a takeover and a merger?**

A takeover involves one business gaining control of another – takes over B; a merger involves organisations joining together e.g A joins with B to create a new organisation C

**4. What is the difference between vertical and horizontal integration?**

Vertical is between organisations at different stages of the same production process; horizontal is between organisations at the same stage of the same production process.

**5. What are typical reasons behind conglomerate mergers and takeovers?**

To spread risks by operating in several markets at once; to move into new growth areas

**6. What are the common advantages and potential disadvantages of selling a franchise?**

Benefit: raise funds; get access to motivated individuals; grow fast

Disadvantage: do not gain all the profits; lose some control

**7. What are the common advantages and potential disadvantages of buying a franchise?**

Benefit: access to existing product and brand; access to track record; access to experience of others

Disadvantage: costs of acquiring, ongoing fees

**8. What are the common challenges of growth?**

Diseconomies of scale due to the challenges of coordination, control and communication

**9. What is the difference between external and internal growth?**

External growth is through acquiring others e.g, merger and takeover; internal growth is through more sales

**10. Why do mergers and takeovers often fail?**

Culture clashes and diseconomies of scale.