NEW

AQA Business

TARGET B-A*

Year 12 & 13

Ian Marcousé

A-Z Business Training Ltd

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Ian Marcouse, June 2020

AQA Business A Level

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Environmental issues & fair trade

Grade C/B. Getting the basics

Environmental issues affect costs in two ways. One is that a company's variable costs will increase if they insist on supplies produced to higher standards, e.g. organic eggs or Fairtrade cocoa. The second is the fixed overhead cost of setting up a department with the job to learn about, purchase and supervise/inspect 'greener' supplies and production methods. The higher costs are usually passed on to customers as higher prices for Fairtrade or organic produce. That will decrease demand from consumers with low incomes, but is likely to increase it from a wealthier minority that prioritise environmental or ethical standards. The net effect is unknown, but it may be that Fairtrade adds enough value to boost profits.

Grade B. What's the key issue?

The key issue is whether pressures related to global warming/CO^2 will force firms to rethink global supply chains. Scottish salmon is sent to China to be filleted and sliced, then back to be smoked & packed. It's a 20,000-mile round trip. The saving in labour cost outweighs the transport cost, but a carbon tax could change that by increasing the cost of fuel. Firms won't change their behaviour because they doubt that governments (and voters) mean what they say about global warming. Do people *really* care? Enough to accept higher prices for food? No-one quite knows.

Grade A. Why it matters

It matters because of the possible effect on prices, the cost of living and therefore the standard of living. Fitbit is an American company, but has an R&D centre in Romania and manufacturing in China and Vietnam. So Fitbits sold in the U.S. (60% of global sales) are designed in a low-labour-cost part of Europe and made in low-cost Asia. If concern over emissions forces Fitbit production back to the US, costs could double. That would push prices up and squeeze household spending power.

Grade A. The counter-argument

The counter-argument is that global warming is an environmental emergency that needs to be tackled. Either the current generation takes a small hit to its standard of living or later generations will face far greater economic and environmental pressures. There is no doubt that the overwhelming view on the part of scientists is that global warming is a serious threat to the planet. The UK may not be among the hardest-hit, but we shouldn't ignore the possibly savage effects on others.

Grade A* The critical perspective

Environmental issues are a matter of science and economics, but also ethics. The problem is that ethics can be used manipulatively – to win an argument when logic and evidence fail. But there's no doubting the argument that says it's the rich countries such as ours who have caused global warming over recent centuries. Therefore we have a moral obligation to do our best to correct the problem.

Do remember that western countries don't just emit a lot of CO^2, they also create vast amounts of waste. Globally 50m tonnes of e-waste is created each year, e.g. old mobile phones. Some is recycled but a lot shipped off to China, India and Nigeria. Apparently only 10% of that waste is recycled, with the rest going to landfill. Should trade in waste be banned?

Fair trade: some suppliers offer goods guaranteed to have been made to higher environmental and welfare standards – and producers sell them with a logo such as *Fairtrade*.

Exam tip: don't wait for examiners to ask you about environmental issues. A company might set a growth objective that's logical on business grounds. But if you think it's environmentally dubious, say so. If you have strong 'green' views, use them.

Environment & fair trade: constructing logic (to get to the top response level)

Chain 1. If carbon emissions were controlled by taxing carbon (1)… there would be a strong incentive to use less carbon in the form of fossil fuels (2). This would make companies re-think their product design (3)… and care more about renewable energy (4). But prices would rise, hitting households (5).

Chain 2. Customers who care about the environment and developing country working conditions (1)… can choose fair trade products (2)…as long as they can afford them (3). Others worry that fair trade is an excuse for higher profit margins (4) i.e. a way to exploit ethically-minded customers (5).

The value of PED & YED in marketing decisions

Grade C/B. What decisions?

The value of price and income elasticity to marketing decision makers depends on the business situation. Income elasticity (YED) is used mainly for sales forecasting. A sports car-maker's YED of +5 means a forecast 3% *fall* in real incomes threatens a 15% fall in sales. The marketing manager might decide on a subtle way to boost market share without damaging the car's image (think free servicing for 3 years, not price-cutting). With a longer timescale, the marketing department might look for a new product with a much lower income elasticity, for example a specialised vehicle for the army. For decisions based on PED, see right.

PED affects almost every marketing decision. Not only on price setting and price changes, but on the key strategy question: how to lower a product's price elasticity? To achieve this, every decision must focus on increased differentiation, e.g. by unusual advertising, packaging and display – making your brand seem really different from the majority.

Grade B. Interpreting the data

Here are 3 anonymised products, A, B and C. From their PED and YED figures, think about the nature of these products. What might they be? See the answers in the box, bottom right.

	Product		
	A	**B**	**C**
Price elasticity (PED)	-4	-2.5	-0.1
Income elasticity (YED)	-2	+0.8	+6

Grade B/A. Why it matters

Making decisions based on PED and YED suffers from an obvious problem. The values placed on PED and YED are based on historic data (measuring past correlation data). But these values can and do change over time, e.g. PED was -2.5 but is now -1.5. The first time a company learns about the change is when they put a decision into practice. If the data is outdated, the decision may be wrong. So it's important to find a way to keep PED and YED figures as up-to-date as possible. This might be achieved by regular market research and data monitoring.

Answers:
Product A is a highly price elastic, inferior good, such as supermarket own-label tinned food. B is price elastic but a 'normal' good, e.g. petrol. C is a highly different-iated, super-luxury good, e.g. a £250 bottle of Krug champagne.

Grade A* The critical perspective

The only sure-fire success in marketing decision-making is to increase the price of a price inelastic product/service. Sales will fall, but by a lower % than the % rise in price. Therefore both revenue and profit will be boosted. And because of the low price elasticity for your products, actions taken by rivals (such as price cutting) will have little effect on you. This is why most marketing departments focus their efforts on ways to cut price elasticity – in the hope of gaining the market power of an Apple, a Chanel or a Tesla.

PED, YED and marketing decisions: transmission (to the top response level)

Chain 1. A holiday company may find its Spanish holidays are highly price elastic (1) … forcing the business to cut prices down to match the cheapest in the market (2). To fight against this, higher differentiation is needed (3)… such as creating a more specialised sub-brand (4)… focusing on activities rather than sun, such as more serious water sports. (5)

Chain 2. If you make luxury products that have high, positive income elasticity (1) … your business is vulnerable to an economic slowdown (2). The finance director may tackle this with high levels of cash in the balance sheet (3)… but the best marketing decision might be to diversify (4) … by launching new products that are not luxuries, and therefore have lower YEDs. (5)

Elkington's Triple Bottom Line

Grade C/B. Getting the basics

Coined in the 1990s by John Elkington, the triple bottom line attempts, like Kaplan & Norton, to provide a more balanced way of measuring business success. The triple bottom line is 3Ps: profit, people and planet. In other words Elkington was proposing a 'social profit & loss account' based on the company's internal profit plus its external impacts on its staff (people) and the environment (planet). This should create a figure comparable with cost-benefit analysis, which takes into account external costs and benefits. The problem is, who's doing the counting?

People can be developed by an employer to increase their human capital, i.e. make them more valuable to society/the economy. This is worth a huge amount and fully deserves to be accounted for on a P&L account. The problem is who's making the valuations and how is the data used. Credit Elkington for the idea, but the accounting method was never resolved.

Grade B. What's the key issue?

	Standard Income statement (£ms)	Triple bottom line Income statement	The problem here is that the financial calcul-ation of profit is subject to well-known accounting conventions and heavily regulated. The risk is that the business then uses its own rules to create the other two figures.
Revenue	420	420	
Operating costs	(370)	(370)	
Finance costs	(20)	(20)	
Profit for the year	30	30	
Net benefit to People		15	
Net benefit for Planet		25	
Triple Bottom Line		70	

Grade B/A. Why it matters

In recent years there have been many problems with official, audited accounts, in the U.S., U.K. and Germany. Yet accounts have clear rules and there are implicit penalties for fraudulently cooking these books. So you can have some confidence in the figure 'profit for the year'. Yet to this accounting-derived figure are added two creations: our net impact on People and on the Planet. Who on earth would take the Triple Bottom Line figure seriously? It's like marking your own exam.

Planet: if People are hard to account for, the environment is even more of a problem. Short-term impacts on air or sea pollution are hard enough to 'value' The impacts on long-term global warm-ing give too much scope for creative accounting.

Grade A. The counter-argument

The counter-argument would come from Elkington himself. He would suggest that the triple bottom line gave impetus to those within business who cared about sustainability and social responsibility. The phrase 'triple bottom line' was a way to get directors to take Fairtrade or staff training more seriously, perhaps bearing in mind that outside pressure groups might attempt a 3P assessment of the business – and negative numbers on People & Planet might be embarrassing.

Exam tip: be prepared to compare the 3Ps with K&N. The 3Ps were perhaps too prescriptive so the scorecard won

Grade A* The critical perspective

Whereas K&N's balanced scorecard still seems current, the triple bottom line has aged less well. Academics still write about it, but it's hard to find evidence of companies that still use it. The 3Ps haven't got the legs of marketing's 4Ps.

Triple bottom line: constructing logic chains (to get to the top response level)

Chain 1. To value the impact of a business on people (1)… you could account for taxpayer savings from jobs provided in an area of unemployment (2)… and value the personal training given to young recruits (3). But unless there were agreed rules (4) ... companies could make up their own figures (5).

Chain 2. The real problem with the triple bottom line (1) …is that the companies wanting to use it have something to say or to mask (2)… such as an oil company with a bad reputation because of an oil spill (3)…which wants to highlight its new ethical stance (4)…by 'using' Elkington's 3P approach (5).

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Ian Marcousé is a former A Level Business Chief Examiner and Chair of Examiners. He advised Edexcel on its current A Level courses in Business and Economics. He now teaches at a central London school and at London University's Institute of Education. He is the Founding Editor and lead writer for Business Review magazine.

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