

CHAPTER 1

UNDERSTANDING THE CANADIAN BUSINESS SYSTEM

CHAPTER SYNOPSIS

Chapter 1 creates a context for understanding the business concepts that are presented throughout the text. This chapter presents the ideas of business and profit, outlines the world's major economic systems, and describes the basic aspects of Canada's market economy, including markets, demand, supply, private enterprise, and degrees of competition. A supplement at the end of Chapter 1 provides a brief history of business in Canada.

CHAPTER OUTLINE

I. THE IDEA OF BUSINESS AND PROFIT

A business is an organization that seeks to earn profits by providing goods and services to customers. Profit is what remains after a business's expenses incurred are subtracted from its sales and revenues. Profits are what encourage people to open and expand business and are required in order for the organization to be "a going concern." In Canada, not-for-profit organizations such as charities, educational institutions or government agencies are also important. As the term suggests, these are organizations that do not try to make a profit; instead, they use the funds they get from government grants or from the sale of goods and services to provide various services to the public.

II. ECONOMIC SYSTEMS AROUND THE WORLD

An economic system is the way in which a nation allocates its resources among its citizens. Various systems differ in terms of who owns or controls these resources, or "factors of production."

A. Factors of Production—The basic resources used by a business to produce goods and services include natural resources, human resources, capital, entrepreneurs, and information.

1. Labour—The people who work for a company.
2. Capital—The funds needed to operate a business.
3. Entrepreneurs—Those people who accept the opportunities and risks involved in creating and operating a business.
4. Natural resources—Land, water, mineral deposits, trees and other naturally occurring resources that businesses need to operate.

5. Information—Market forecasts, specialized knowledge possessed by employees, and various forms of economic data about the economy and consumers that are used by businesses.

B. Types of Economic Systems—Different types of economic systems manage the factors of production in different ways. Command economies, market economies, and mixed economies are three basic types.

1. Command economies—Government controls many (or all) of the factors of production. The government decides how much will be produced and who will produce it. Command economies have fallen into disfavour during the past decade, and only a few are left (e.g., Cuba and North Vietnam).

2. Market economies—Factors of production are controlled by markets, not by government. Individuals are free to start their own businesses, and consumers are free to buy from whomever they wish.

a. Input and output markets—In input markets, companies buy resources from households; in the output market, companies supply goods and services in response to demand from households.

3. Mixed market economies—Have features of both command and market economies. Most countries of the world, including Canada, have mixed market economies.

III. INTERACTIONS BETWEEN BUSINESS AND GOVERNMENT

A. How Government Influences Business—The government influences business by taking on the roles of customer, competitor, regulator, taxation agent, provider of incentives, and a provider of essential services.

1. Government as a customer—Government buys many services and products which amount to billions of dollars each year.

2. Government as a competitor—Crown corporations at both federal and provincial levels compete with business.

3. Government as a regulator—The federal and provincial governments regulate many aspects of business activity, including the following:

a. Promoting competition—Competition policy seeks to eliminate restrictive trade practices to stimulate maximum business activity. The guidelines for Canada's competition policy are contained in The Competition Act.

b. Protecting consumers—The Canada Consumer Product Safety Act, the Tobacco Act, Weights and Measures Act, Textile Labelling Act, and the Food and Drug Act, are examples of regulations that protect consumers.

c. Achieving social goals—The achievement of social goals promotes the well-being of our society. Social goals include universal access to health care, safe workplaces, employment insurance and decent pensions.

d. Protecting the environment—Legislation to protect the environment includes the Canada Water Act, the Fisheries Act, and the Environmental Contaminants Act.

4. Government as a taxation agent—Taxes are imposed and collected by all three levels of government. Revenue taxes (e.g., income taxes) are levied primarily to fund government services and programs; they form the majority of all taxes. Progressive and regressive taxes are described. Restrictive taxes, such as excise taxes on alcohol, tobacco and gasoline serve as both a revenue source and a “deterrent to excesses.”

5. Government as a provider of incentive programs—These programs are intended to stimulate economic development. Governments offer numerous incentive programs through various government organizations. Several examples of grant incentive programs are described. Incentives are also provided through the services provided to companies by the government (several examples are given).

6. Government as a provider of essential services—Business activity is facilitated by the government services that are supplied, e.g. roads, postal service, police and fire departments.

B. How Business Influences Government—Business can influence governments through the use of lobbyists, trade associations, and advertising.

IV. THE CANADIAN MARKET ECONOMY

A. Demand and Supply in a Market Economy—Markets, demand, supply, the law of demand, the law of supply, equilibrium, surplus, and shortage are defined.

1. The laws of supply and demand—Demand is the willingness and ability of buyers to purchase a product or service. Supply is the willingness and ability of producers to offer a good or service for sale.

2. Demand and supply schedules—Show how many units of a product are likely to be sold at various prices.
3. Demand and supply curves—A demand curve shows how many products will be demanded at different prices, while a supply curve shows how many products will be supplied at different prices.
4. Surpluses and shortages—When the quantity demanded exceeds the quantity business are willing to supply, a shortage exists. When the quantity demanded is less than the quantity businesses are willing to supply, a surplus exists.

V. PRIVATE ENTERPRISE AND COMPETITION

Adam Smith’s belief that allowing individuals to pursue self-interest would eventually benefit society as a whole through “the invisible hand of competition” is discussed. Four elements must be present in private enterprise: private property rights, freedom of choice, profits and competition.

- A. Degrees of Competition—Four degrees of competition within private enterprise are identified. Examples of each are given.
 1. Perfect competition—A market or industry characterized by a large number of small firms producing an identical product so that no one firm is powerful enough to influence the price of their product in the market place. Agriculture (wheat production) is given as an example.
 2. Monopolistic competition—A market or industry characterized by a large number of firms supplying products that are similar but distinctive enough from one another to give firms some ability to influence price. Examples given: detergents, soft drinks, fashion.
 3. Oligopoly—A market or industry characterized by a small number of large firms that have the power to influence the price of their product and/or resources. Generally large initial capital investment is necessary for new competitors to enter the market, therefore, barriers to entry are high. Examples given: automobile, rubber, and steel industries.
 4. Monopoly—A market or industry with only one producer, who can set the price of its product and/or resources. Natural monopolies like provincial utilities are described.

QUICK QUESTIONS

1. What are the factors of production used to produce a litre of orange juice?

2. Entrepreneurship involves risk-taking, which is an important ingredient in a free-market system. What characteristics of our free-market system encourage risk-taking?
3. Give an example of a country with a planned economy. What makes this economy planned? Give an example of country with a market economy. How is the economic system different in this country?
4. What is an equilibrium price? What happens if incomes rise and demand increases? What happens if producers have a surplus and supply increases?
5. Which level of competition best describes the market in each of the following scenarios: Your local Pizza Hut? A local farmer selling apples for applesauce? Gap jeans?

IN-CLASS EXERCISES

Exercise #1: What Do You Know About Business?

Activity Overview:

This activity helps students assess their level of knowledge about business and set their own learning goals for the class.

Time Limit: 20 minutes

What to Do:

1. Ask each student to take out a piece of paper and divide it into two columns. In the first column, students should write the most important four or five things they currently know about business, and in the second column, the four or five things they would like to learn. Tell them if they are having difficulty coming up with items to list, take a look at the table of contents of the text. It will give them some clues so that this task doesn't frustrate them. (5 minutes)
2. Divide students into groups of three to five people and ask them to share their lists with each other. As they listen, they can delete or add anything that seems relevant. (5 minutes)
3. Ask them to switch groups so that they are with all new people, and repeat the process of sharing their lists. (5 minutes)
4. Ask students to switch to a third group of all new people. With this group, the goal is to synthesize their lists into one big idea of what they know, and one big idea of what they want to learn. (5 minutes)

Don't Forget:

This activity allows students to get to know each other as well as set expectations for the course. The underlying agenda is to get them talking to each other, setting the stage for active participation throughout the class.

Wrap-Up:

Wrap up the discussion by having each group report back to the class. You may want to record their responses and post them in the room for reference as you move through the course.

Exercise #2: Comparing Economic Systems

Activity Overview:

This activity gets students talking about the similarities and differences between the Canadian economic system and other economic systems.

Time Limit: 30 minutes

What to Do:

1. Divide the class into small groups. Ask the groups to assume they have just overheard a classmate say, “Canada is becoming more socialist everyday—with all the government control.” Have each group list reasons why the statement could be true and reasons why the statement could be false. (15 minutes)
2. Reassemble the class and discuss each group's thoughts. (15 minutes)

Don't Forget:

Remind students that a government's level of control distinguishes capitalism from socialism. If you have foreign students in your class, it will be very interesting to hear them describe the characteristics of the economic system in their native country.

Wrap-Up:

Wrap up the discussion by reminding students that the Canadian economic system and a socialist system have many similarities and differences. For example, workers in socialist economies often work fewer hours, have longer vacations, and receive more health, education, and child-care benefits than do workers in capitalist economies. On the other hand, the federal government does control some basic services in Canada as well as various aspects of the market through agencies such as the Hazardous Products Act, The Food and Drug Act, and the Canadian Radio-Television and Telecommunications Commission.

Exercise #3: Case Study: Supply and Demand for Pollution Permits

Activity Overview:

This activity asks students to apply chapter concepts to a case study.

Time Limit: 30 minutes

What to Do:

1. In advance, make copies of the following case study and distribute to students:

*Case Study
Pollution Permits*

When Julie Hardwick, a manager for a division of BP Amoco PLC, checks her computer every day, she's not looking for information about her company's stock. She's finding out whether other divisions of BP are looking to trade their permits to emit pollutants that cause global warming. Units that have leftover permits after meeting their emission-reduction quotas are allowed to sell them to other units that need them to cover shortfalls in their own efforts to meet their goals. The company reports that it is saving millions of dollars through creative reductions in fuel consumption, prompted by the use of permits. Other firms in the developed countries are using permits as well, hoping to reduce pollution before their governments make it mandatory.

Some believe that trading permits between companies or across national borders will prove difficult because of the wide variety of sources of pollution and the problem of maintaining fairness in the use of the permits. For instance, should heavy polluters be made to clean up pollution instead of being able to trade for permits to continue to pollute? Some corporations already use an alternative called offset rights, which are positive steps that offset the pollution a company can't easily control. Some typical offsets include the use of clean energy, such as solar or wind power, and the planting or protecting of forests and fields that absorb carbon dioxide, a major pollutant. The Nature Conservancy has used several offset deals to fund rain forest preservation projects, for example.

*Others believe that trading can succeed, and that measuring each country's use of fossil fuels will provide a usable gauge of how many permits it should be allowed. Once rules for trading have been established, the cost of complying with pollution controls will drop, and opportunities to come up with creative new sources of energy will proliferate. (Source: Janet Ginsberg, "Letting the Free Market Clear the Air," *Business Week*, November 6, 2000, 200, 204.)*

2. Divide students into groups and ask them to read the case and answer the following questions in their small groups. (15 minutes)
 - (a) How does trading in pollution permits at BP demonstrate the laws of demand and supply?
 - (b) What would influence the demand for pollution permits if they were traded globally?

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- (c) Should companies be allowed to trade permits? Should countries be allowed to? Why or why not?
3. Once students have answered the questions, discuss their answers as a class. As students discuss their answers, make sure they touch on the following points: (15 minutes)
- (a) Those who want to buy permits and those who want to sell them have created a market where the price is set by the action of supply and demand.
- (b) The strictness of government controls on emissions and the individual company's ability to meet the quota, as well as the cost of failure and the price of the needed permit must be considered.
- (c) Answers will vary, though there will be much debate about the ethics involved in buying and selling permits.

Don't Forget:

Make sure that you keep students on the topic of supply and demand.

Wrap-Up:

Wrap up the discussion by asking students for other examples of environmental issues affecting supply and demand.

Exercise #4: Flying into Trouble: The OneWorld Alliance and Antitrust Laws

Activity Overview:

This activity asks students to apply chapter concepts to a case study.

Time Limit: 30 minutes

What to Do:

1. In advance, make copies of the supplemental case study below and distribute to students.

Case Study

Flying into Trouble: The OneWorld Alliance and Antitrust Laws

Over the last number of years, airline alliances have become an increasing reality in international travel. The Star Alliance is currently the largest of these with twenty member airlines including Lufthansa, Continental Airlines, United Airlines, British Midland International, Singapore, Air China and U.S. Airways. Another significant player is the OneWorld Alliance that has eleven member airlines including British Airways, American Airlines, Cathay Pacific Iberian, Finnair and Royal Jordanian. SkyTeam is the third of the main groupings and includes Air France, Delta Airlines and Aeroflot.

The U.S. Department of Justice, however, does not always think these alliances are good for business. In a recent ruling against give members of the OneWorld Alliance including British Airways and American Airlines, the Department of Justice indicated that OneWorld's third proposal to expand their alliance could result in "competitive harm" on six transatlantic routes. As a compromise the Department of Justice proposed that OneWorld give up some of its lucrative slots at congested airports including London's Heathrow Airport.

To make matters more complicated, it is the Department of Transportation, not the Department of Justice that has the final say on airline regulation in the U.S.. OneWorld points out that the Department of Transportation overruled similar concerns from the Department of Justice to approve a Star Alliance proposal earlier this year. As a result, OneWorld have indicated that they will issues a "robust response" to the Department of Justice recommendations.

In Europe the European Commission have also expressed reservations about the OneWorld proposal. In addition, Virgin Atlantic, which isn't a member of any alliance, has repeatedly called for the Department of Transportation to reject OneWorld's anti-competitive application.

Source: Doug Cameron "Justice Department Objects to OneWorld Extension" Wall Street Journal, 12/21/09.

Questions for Discussion

1. Why would large airlines want to join alliances such as OneWorld, Star, or SkyTeam? What are the potential advantages and disadvantages?
2. Why do you think Virgin Atlantic refuses to join an airline alliance?
3. Do you think the government should have a role in overseeing these alliances? Is it good for competition for the government to keep intervening?
4. Does it make sense to have several government departments involved in antitrust regulations?

2. Divide students into groups and ask them to answer the questions in their small groups. (15 minutes)

3. Once students have answered the questions, discuss their answers as a class. As students discuss their answers, make sure they touch on the following points: (15 minutes)

- (a) What role should any government play in regulating an industry?

- (b) If government prevent expansions of global airline alliances will this force smaller, non-aligned, airlines out of business?

Exercise #5: Is Competition Good?

Activity Overview:

This activity asks students to think about competition and the role that it plays in our economic system.

Time Limit: 45 minutes

What to Do:

1. Ask students to think about competition as an essential ingredient in a free-enterprise system.” (10 minutes)
2. Divide the class into small groups and ask them to discuss and make notes on some situations in which competition is good for the Canadian economy and some situations in which competition is bad for the Canadian economy. Group members should try to reach agreement. (15 minutes)
3. Regroup the class and ask the groups to explain the rationale for their answers, asking for feedback from the class as the various situations are discussed. On what parts of the discussion does the class agree or disagree? (15 minutes)
4. Ask the class to come to a consensus: Is competition good or bad? (5 minutes)

Don’t Forget:

If the class cannot arrive at a consensus, they might consider voting.

Wrap-Up:

Remind students that competition is an essential part of a free-enterprise system, as entrepreneurship invites competition in many industries. Not every enterprise will succeed in the marketplace, but competition does hold prices at market level and contributes to a high quality of goods and services.

TEACHING TIPS

1. Individuals set up businesses in Canada with the intention of making a profit. As a course opener, ask students to provide a definition for the term “profit.”
2. Though the definition of business includes profit as a motive, remind students that most business principles also apply to not-for-profit organizations.
3. There have been business people who have said: “For me, making a profit is NOT the most important thing about operating my business!” Ask students to identify some

other good reasons for opening a business and going through the work of making that business a successful venture.

4. Have the students imagine a typical new small business that has just completed its first period of operation. If there are profits from operations, where are some places to which these profits might be allocated? Have students make the list as long as possible.
5. Most, if not all, of the students have heard of non-profit or not-for-profit organizations. Ask the students to explain what such terms mean. Is there really such a thing as a non-profit organization?
6. Profits reward owners for taking the risks involved in investing their money and time in a business. Ask students to describe some of the risks involved.
7. Remind students that inputs used to produce outputs are also called factors of production; they include physical resources, labour, capital, entrepreneurship, and information resources.
8. As a way to make the factors of production—labour, capital, entrepreneurs, and natural resources—stay with the students, engage in a synonym game. Ask students, perhaps in teams, to develop a string of synonyms for the four factors. Here’s an example: “people, money, risk takers, and raw materials.”
9. Ever since the factors of production were first proposed, various individuals have attempted to indicate which of the four is most important. Have students do the same. Usually entrepreneurs come out ahead. However, you can point out that all are needed and making one of them the “star” could be a mistake.
10. It has been said that entrepreneurs are a special breed. Encourage some students to indicate why they would or would not like to be an entrepreneur.
11. Ask students to evaluate this statement: “An owner of a business can take more time away from work than a hired employee can.”
12. Remind students that an economic system is defined by how it allocates factors of production. In a planned economy, the government owns and controls these factors; in a market economy, producers/consumers buy and sell what they choose.
13. Encourage students to see the logic behind some of the ideas that Karl Marx espoused. Students should also be encouraged to take from Marxian theory several notions that we accept in Canada today.
14. If students agree that some Marxian ideas truly have merit, they are ready to tackle a timely question: “What has gone wrong in so many nations that have tried to follow the teachings of Marx?”

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15. Ask students to do some investigative research on the status of human rights in communist countries like Cuba, North Korea, and Vietnam. Is there a common thread? If students find a common thread, ask them this: “What seems to be the relationship between communism and the value placed on the rights of the individual?”
16. Cuba is on the list of communist countries. Assume that tomorrow morning, Castro calls the Canadian Prime Minister and says: “I want to restore economic stability to my country. Please help me!” Appoint one of your students (or a student team) as High Commissioner for Economic Restoration in Cuba. What will that student (or student team) do to help Cuba?
17. Have students reveal what picture comes to mind when someone uses the term “capitalist.” Is the first reaction positive or negative? Why?
18. Make sure students understand that a mixed market economy is characterized by government ownership of major industries working alongside privately owned industries.
19. Ask students to give examples of how government plays each of the roles mentioned in the text (customer, competitor, regulator, taxation agent, provider of incentives and financial assistance, and provider of essential services).
20. Price represents a balance between supply and demand, so consumers should be able to do a lot to determine prices of products and services. Why do consumers often feel that they have little or no power over prices they are charged?
21. Ask the students to show ways in which consumers can cause the price of certain products to fall.
22. Degrees of competition are best taught through liberal use of examples. Moderate a class discussion where the goal is to develop examples of each of the four degrees of competition.
23. What degree of competition exists in professional hockey? In major league baseball?
24. Remind students that perfect competition is characterized by (a) many buyers, (b) many sellers, and (c) buyers and sellers who accept a going price.
25. Remind students that monopolistic competition is characterized by (a) many buyers, (b) many sellers, and (c) products that are differentiated.
26. Reinforce that oligopoly is characterized by (a) many buyers, (b) few sellers, (c) products that are quite similar, and (d) a change in price by one seller often means a change in price by all sellers.

27. The concept of the “invisible hand of competition” is often hard for students to grasp. Help them understand the concept by working through an example which begins with an individual perspective and show how many individuals working for their own benefit actually benefit a much larger group of people. Price reductions, which occur over time in products (e.g., electronic calculators or computers) are good examples.
28. Remind students of the importance of learning the key terms in the text. Although the “jargon” of a field of study can be annoying to some, it provides a useful shorthand for describing concepts and learning about the field.
29. Remind students that in an introductory course the material is not covered in depth. Rather, the approach is to “sample” all the important areas of business.
30. One of the review questions at the end of the chapter asks students to give examples of the four basic degrees of competition. Ask students to share these in class.
31. Have students interview an entrepreneur and ask the person about their experiences. Have students make a brief report to the class about their findings.
32. Have students make a list of products they use every day. Compile a master list as part of a class discussion. Most will be surprised at how long the list is.
33. One way to end the chapter discussion is to play a form of Jeopardy with the class. Divide the class into teams and ask teams quick questions about the chapter material. The winning team continues to get the first chance to answer until they lose to another team. You, the instructor, serve as timekeeper, scorer, and moderator.

USING THE BOXED INSERTS

Opening Case: Combining the Whopper and the Timbit

The opening case describes the high-visibility merger of Tim Hortons and Burger King, and notes the interesting fact that Burger King moved its headquarters to Canada as part of the deal. The material in the opening case should be of considerable interest to students because it deals with two companies that are very prominent on the retail scene in Canada. The case helps students understand the complex world of business activity in the 21st century.

Questions for Discussion

1. What are the advantages of the merger for Burger King? For Tim Hortons? What are the potential disadvantages for each company?

For Burger King, the merger means that the company will have a popular and iconic Canadian brand as part of its organization. This will mean increased sales and greater visibility for the company in Canada. There is also the matter of lower corporate tax rates for Burger King since it moved its corporate headquarters to Canada. For Tim

Hortons, the most obvious advantage is its new access to the U.S. market. As noted in the case, Tim Hortons has been trying for years to get a foothold in the U.S. market, and can now take advantage of Burger King's knowledge of that market to improve its performance in the U.S.

There are two potential disadvantages associated with the merger. First, Burger King's movement of its corporate headquarters to Canada caused concern in the U.S. that the company made the move because it wanted to lower its corporate income taxes. That may (or may not) negatively influence the perception that U.S. and Canadian consumers have of Burger King. Second, anytime two companies merge there is always the potential that it won't work as well as intended. Only time will tell whether there are unanticipated negative consequences of the merger for either Burger King or Tim Hortons.

2. What kind of economic system is evident in Canada? What roles does government play in the economic system? How are those roles evident in the Burger King-Tim Hortons merger?

Canada has a mixed market economic system. That means that the Canadian economy is not a "pure" command or market economy. Rather, it has some characteristics of each. Governments in Canada are involved in regulating business activity, but not nearly as involved as governments in command economies are. Free market operations are also evident in Canada, but business is not completely free to do anything it wants. Canada is not unique in having some aspects of a command economy and some aspects of a market economy. Most countries in the world have some mix of the two basic types of economies.

The text describes the various roles that government plays in the Canadian economy (customer, competitor, regulator, provider of essential services, taxation agent, and provider of incentives).

In the Burger King-Tim Hortons merger, the most important role that government played was that of regulator. The merger had to be approved by two Canadian government agencies. The Competition Bureau analyzed the situation and concluded that the merger would not unduly lessen competition in the Canadian market because there is so much competition in the fast food industry. Investment Canada imposed several conditions: Burger King had to agree to keep the Tim Hortons brand separate from the Burger King brand, to maintain significant employment levels at Tim Hortons, to guarantee that at least 50 percent of the Tim Hortons board of directors would be Canadians, and to maintain Tim Hortons pre-merger level of charity work in Canada. The Canadian government's role as taxation agent was also relevant in the merger, since Burger King knew that if it moved its headquarters to Canada it would pay less corporate tax than it had been paying in the U.S.

3. Are the restrictions that were imposed on the merger by the Canadian government consistent with our economic system? What potential problems might arise as a result of these restrictions?

If we assume that Canada has a “pure” market economy, then the restrictions imposed by the merger are inconsistent because government should not restrict business activity. But, of course, we do not have a “pure” market economy. Instead, we have a mixed market economy, and the restrictions that were imposed are consistent with that kind of economic system. That is not to say that there won’t be controversy about mergers such as this one. For example, the Canadian Centre for Policy Alternatives warned that there would be layoffs and cost-cutting in the merged companies. They were in effect saying that the government’s ruling was not restrictive enough. Other individuals and organizations took the opposite view and argued that the government’s decision was too restrictive. In any mixed market economy, there will always be debate about whether there is too much or too little government intervention in the economy.

An obvious potential problem that might arise is financial difficulties for Burger King. If it runs into significant difficulties it might have to engage in serious cost-cutting and laying off of employees. But the company could run afoul of government regulations if it tries to do this, given the terms of the merger that they accepted (for example, Burger King agreed to maintain significant levels of employment in Canada). But what does “significant” mean?

Entrepreneurship and New Ventures: Riversong: Innovative Canadian Guitars

Mike Miltimore is an entrepreneur who started Riversong Guitars, a brand which is built on innovative guitar manufacturing. Mike is now trying to increase consumer awareness and demand for his improved guitar design.

Critical Thinking Question

1. What else does Mike Miltimore need to do to get his brand to be noticed in an industry dominated by well-known brands with long storied histories?

There will be great variation in student answers here. Individuals who are assigned this question early in the term are likely to have fewer ideas than those who are assigned this question later in the term. This is particularly true for those who have been exposed to the information in the two marketing chapters (12 and 13). If the question is assigned early in the term, it is probably best for the instructor to moderate an in-class discussion which is designed to solicit student ideas. This will generate more ideas and will be more interesting to the class. It will also allow for a group critique of the ideas that are suggested.

Suggestions for getting the brand noticed will likely revolve around the “promotion” aspect of marketing, whether or not that is explicitly recognized by the individuals who make the suggestions. As well, it is likely that student ideas will focus on social media as a promotion tool because that is what they are familiar with. Whatever ideas are put forward (and whether the question is assigned early or late in the term), the instructor should make it clear that (a) promotion is important, and (b) it is only one of the 4 P’s of marketing and must not be considered in isolation. For example, if a

suggestion is made that “buzz” marketing should be used, it is important to state specifically how this would work, how the promotion aspect interacts with price and distribution of the product, and the advantages (and disadvantages) that may be evident in buzz marketing. Likewise, since the question focuses on increasing brand recognition, the section in Chapter 13 on brands must be considered during the discussion. For example, it is difficult, expensive, and time-consuming to establish brand recognition for a product. Given that, the issue of what a start-up company like this one can reasonably achieve in the short-run must be assessed.

Students may be less likely to suggest more traditional promotion ideas (e.g., a traditional television or radio advertising campaign), but the possible benefits of such approaches should at least be recognized and examined. Essentially, the instructor should monitor the discussion to ensure that all aspects of promotion are examined and then the most promising and appropriate approach chosen.

E-Business and Social Media: Taking a Bite Out of Internet Radio

This insert describes Apple’s movement into streaming radio, the fastest growing form of music listening. In 2013, Apple rolled out the iTunes Radio service with more than 200 stations; it allows users to create custom stations to fit their personal musical tastes. Apple has entered this market rather late, and it remains to be seen if its venture will be successful, given such competitors as Pandora and Spotify.

Critical Thinking Questions

1. In terms of degrees of competition, how would you describe the market for Internet radio? Do you think that this will change in the next five years? If so, how?

Students should focus on the number of service providers that currently exist in this market. They can then determine what degree of competition exists in the market. Their comparisons should be based on information provided in the text regarding degrees of competition. For example, this is clearly *not* a case of perfect competition or monopoly because the market does not have the characteristics of either of these markets. So that leaves us with the two middle ground markets (monopolistic competition or oligopolistic competition). There are fewer sellers than in perfect competition, but more sellers than are typically found in an oligopoly, so monopolistic competition seems to be the most appropriate. [Note: The four degrees of competition described in the text are basic types, and it can be difficult to decide where one type ends and another one begins. For example, in the early days of the automobile in North America, the industry illustrated the characteristics of monopolistic competition. Over the years, many companies disappeared and the industry came to represent perhaps the classic case of an oligopoly, with just three domestic suppliers. But during the last 30 years, numerous foreign car makers have entered the North American market, and now there are once again many sellers of automobiles. It is still difficult to start up an automobile company because of the large capital investment that is required, and that is consistent with an oligopoly. But the existence of automobile manufacturers in numerous countries around the world does not fit with the traditional conception of an oligopoly. Perhaps a global oligopoly will

eventually emerge in the auto industry like the one that exists in the large commercial airliner industry, with Boeing, Airbus, and Bombardier being the only sellers.]

If this industry proceeds like others have in the past, there will be a gradual weeding out of many of the sellers over the next five years and the industry will be dominated by a few large sellers. But it remains to be seen whether this industry becomes a “classic” oligopoly situation such as that found in the rubber, steel, and large commercial airline industries.

2. Do you think that Apple will be successful in this new venture? Do you think that it was a wise decision for them to enter the already crowded market?

There will be two distinct patterns in student answers here. Some students will think that the market is too crowded, and that Apple should not have undertaken this venture. Students who take this position will likely be influenced by the opinions expressed in the boxed insert that Apple is simply copying Spotify. Other students will take the position that the previous success that Apple has had with other products and services will positively influence potential buyers to use Apple’s new service rather than some other competing service.

QUESTIONS AND EXERCISES

Questions for Analysis

1. On various occasions, government provides financial incentives to business firms. For example, the Canadian government provided export assistance to Bombardier Inc. with its Technology Transfer Program. Is this consistent with a basically free market system? Explain how this might distort the system.

Government incentive programs may or may not have the desired effect of stimulating the economy. The free market is one in which decisions about what to produce and in what quantities are made by the market- that is the buyers and sellers negotiating prices for goods and services. Financial incentives by government are inconsistent with a free market system.

2. In recent years, many countries have moved from command economies to market economies. Why do you think this has occurred? Can you envision a situation that would cause a resurgence of command economies?

In many countries, the disastrous failures of communism precipitated the move from a command economy to a market economy. It is unlikely that command economies will re-emerge. Extreme civil unrest leading to authoritarian rule could cause a country to revert to a command economy.

3. In your opinion, what industries in Canada should be regulated by the government? Defend your arguments.

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Answers will vary, but students will most likely identify those industries which appear to act as monopolies, such as the cable industry. This question is a good basis for an in-class discussion of the broader issue of government regulation of business. The extent and specific types of government regulation and its effect on the economy will elicit vigorous opinions from students.

4. Familiarize yourself with a product or service that is sold under conditions of pure competition. Explain why it is an example of pure competition and identify the factors that make it so. Then do the same for a product in each of the other three competitive situations described in the chapter (monopolistic competition, oligopoly, and monopoly).

Answers will vary. This is a good exercise for assisting students in understanding that not all industries are equally competitive.

5. Analyze how the factors of production (labour, capital, entrepreneurs, natural resources, and information) work together for a product or service of your choice.

Answers will vary. Make sure that students are correctly identifying the factors of production in the examples they develop.

6. Government plays a variety of roles in the Canadian mixed economy (customer, regulator, taxation agent, provider of services, etc.). Consider each of the roles discussed in the text and state your view as to whether government involvement in each role is excessive, insufficient, or about right. What criteria did you use to make your assessment?

Answers will vary. Some government rules and regulations are necessary to make sure that all of a business's stakeholders are protected and that people who are unable to work get the basic care they need.

Application Exercises

7. For a product that is not discussed in Chapter 1, find an example where a surplus of a product led to decreased prices. Then find an example where a shortage led to increased prices. What eventually happened in each case? Why? Is what happened consistent with what economics predicts?

Answers will vary. Students may have difficulty coming up with an example of a product where a surplus has led to decreased prices, but most of them will use oil as an example of a product where a shortage has led to increased prices.

It is very likely that the examples students come up with will be consistent with what economic theory predicts. That is, the law of demand states that buyers will purchase (demand) more of a product as its price drops. Conversely, the law of supply states that producers will offer more for sale as the price rises. If there seem to be

inconsistencies, analyze why they might exist (for example, too short a time frame of analysis).

8. Choose a locally owned business. Interview the owner to find out (1) how demand and supply affect the business, (2) how the business uses the factors of production, and (3) how the owner acquires each factor of production. \

This should be an interesting exercise for students. Have them categorize the factors of production to make class comparison easier. After the information is brought back to class, have a class discussion about (1) whether supply and demand issues vary across businesses, and (2) whether some businesses have an “easier” time locating the factors of production and why.

9. Visit a local shopping mall or shopping area. List each store you see and determine what degree of competition it faces in the immediate environment. For example, if there is only one store in the mall that sells shoes, that store represents a monopoly. Note the businesses with direct competitors (for example, two jewellery stores) and describe how they compete with each other.

This assignment will provide students with an opportunity to understand different degree of competition in a setting where they spend a fair bit of their time.

10. Pick a specific product that you use. Explain how the factors of production work together to make that product available.

There are many examples that students could use. One example is a meal purchased at a restaurant. The restaurant owner is the entrepreneur who is operating the business for profit and risking the possibility of failure. The business employs a variety of chefs, cooks, managers, wait staff, kitchen staff, and cleaners. The entrepreneur may or may not be employed in the operation of the restaurant, and may or may not do the hiring of all the staff members, depending on the size of the restaurant. While most of the staff members are hired for their physical skills, the chef must have creative talents to make the business successful. Most restaurants are privately owned, and therefore financed by the owner’s personal resources, credit from suppliers, bank or credit union financing, and possibly loans from friends and family. Another important source of financing is cash flow provided by the profitable operation of the restaurant. The natural resources employed are limited, but include the land on which the restaurant is situated.

TEAM EXERCISES

Building Your Business Skills: Analyzing the Price of Doing Business

Follow-Up Questions

1. Discuss the role that various inducements other than price might play in affecting demand and supply in the market.

Encourage the students to think about “what do they look for when they are considering a service provider.” They should look at the company (e.g., its reputation and reliability) as well as the actual services that it offers (e.g., the range of fitness equipment that is available, the variety of classes that are offered, other inducements that are designed to attract customers, etc.).

2. Is it always in a company’s best interest to feature the lowest prices?

No, it depends on many factors, including the reputation of the company, the image that it is trying to portray, competitive factors in the market, the company’s financial position and cost structure, the company’s market share, etc. Sometimes a business fails because it cuts prices below the cost of providing the products or services.

Another factor that should be brought into the discussion is the impact of the decisions that teams made as they responded to the requirement to develop specific pricing strategies to deal with the five different competitive situations that are presented in the exercise. Ask teams what criteria they used to set prices, and how much thought they gave to the impact of their pricing strategies on the company’s profitability and market share.

3. Eventually, what form of competition is likely to characterize this market?

The trend in some industries (e.g., airlines) is for bigger firms to buy out the smaller firms to the point that an oligopoly emerges. But most firms in an oligopolistic industry avoid price competition because it reduces profits. As well, entry into the market is limited because of the large capital investment that is required. Neither of these characteristics is evident in the gym and fitness studio market that is described in this exercise. It seems that the most likely form of competition in this market will be monopolistic competition (fewer sellers than in perfect competition, but still many buyers). There may be some large companies, but small companies can successfully compete by focusing on a niche image and product differentiation. This will allow competition on the price dimension.

Exercising Your Ethics: Team Exercise: Making The Right Decision

Activity Overview:

This activity asks students to examine the ethical issues that can arise when making business decisions.

Time Limit: 35 minutes

What to Do:

1. Divide students into four-member teams and ask them to read and follow the instructions for the Exercising Your Ethics exercise entitled “Making the Right

Decision,” which is found near the end of Chapter 1. Students should each choose one of the different roles in the exercise. (20 minutes)

2. Reassemble the class as a whole and discuss what disagreements came up within each group. How did the role that students were assigned affect their perspective? (15 minutes)

Don’t Forget:

Remind students to stay within their assigned “roles.”

Wrap-Up:

There is seldom a yes/no, right/wrong, black/white answer to ethical decisions in business. Remind students that a rule of thumb might be, in some instances, to make the decision that positively affects the greatest number of people.

CASE ANALYSIS

Business Case 1: Where Are Gasoline Prices Headed?

Questions for Discussion

1. Consider the arguments in support of peak oil theory and the arguments against it. Then draw a graph that shows your predictions of world oil production from now until the year 2100 (measure annual world oil production in billions of barrels on the vertical axis and time on the horizontal axis). Defend your predictions.

Students will come up with many different specific predictions, but they will fall into one of three basic categories. The first category of graphs will illustrate an acceptance of the peak oil theory, i.e., the graphs will show that peak production is reached in a certain year and output never again achieves that level. The second category of graphs will illustrate a rejection of peak oil theory (i.e., the graphs will show that oil production will continue to increase because new sources of supply will be discovered and new technologies will be developed to extract more oil). The third category of graphs will illustrate neither acceptance nor rejection of peak oil theory (i.e., the graphs will show various up-and-down patterns of production, with perhaps several peaks in the future, based on the assumption that those high points might be surpassed sometime in the future).

Whatever the basic pattern, the important point is to make sure that students have a sound empirical and theoretical base for their predictions. Much conflicting data about oil production is presented in the case, and these uncertainties should be addressed in student answers.

2. What do your predictions imply about the price of gas at the pump over time?

Students who accept peak oil theory will conclude that the price of gasoline at the pump will become more and more expensive as time passes. They may even conclude that gasoline will become so expensive that large numbers of consumers will no longer be able to afford to drive their cars and trucks.

Students who reject peak oil theory will conclude that gasoline prices will continue to behave as they have in the past (i.e., they will vary up and down, depending on supply and demand factors).

Students who neither accept nor reject peak oil theory will also conclude that gasoline prices will vary over time, depending on a variety of factors. Their graphs may resemble those of some students who reject peak oil theory.

3. It appears that the supply of oil and natural gas is very large. Discuss some potential problems that might arise even with such a large supply.

Even if the supply of fossil fuels is, in fact, very large there are potential problems. For example, there may be large fluctuations in the price of the fuel which create problems for both companies and individuals. The natural gas industry is a good example. With the dramatically increased supply of natural gas due to new technologies for extracting it, the price plummeted during 2011. Companies then had to decide whether it was profitable to drill new wells given the very low price they were receiving for the commodity. Consumers also had to decide whether switch from one fossil fuel (oil) in favour of another fossil fuel (natural gas). The same thing happened in 2014 with regard to the price of oil. New drilling techniques meant that the supply of oil increased rather unexpectedly and the price therefore dropped.

A second problem concerns pollution. The burning of fossil fuels creates pollution, and the more abundant the fuel is, the cheaper it is. This will induce consumers to rely more on fossil fuels than on more environmentally-friendly sources of energy such as solar and wind power. Concerns have already been expressed by experts that the relatively low price of natural gas and oil will inhibit the development of solar and wind power.

4. Consider the following statement: “*There are so many uncertainties that must be taken into account when trying to predict the supply of, and demand for, oil that it is impossible to have any confidence in anyone’s predictions.*” Do you agree or disagree with the statement? Explain your reasoning.

Students who agree with this statement are essentially saying that predicting the supply and demand characteristics of natural resources may be an interesting exercise, but in the end it is rather fruitless. The answers of students who take this position should include clear evidence of just what the uncertainties are and how they make predicting the supply of natural resources a very difficult exercise. For example, on the *supply side*, it is difficult to know for certain whether new oil discoveries will continue to offset the decline in production in existing oil fields. As well, it is difficult to know whether new

technologies will continue to be developed that essentially increase the supply of oil. On the *demand side*, increasing efficiency in the use of various resources means less demand for those resources. As well, the normal ups and downs in the business cycle can either increase or decrease demand. As just one of many examples, consider the use of copper. Demand has dropped because of the development of alternative ways (other than copper) to carry information from one point to another. Uncertainties regarding both supply and demand issues do indeed make it difficult to accurately predict the future of natural resources, so students who agree with the statement have considerable empirical evidence to back up their position.

Students who disagree with the statement may be either strong supporters of ideas like the peak oil theory *or* strong opponents. In other words, whether they support, or don't support, peak oil theory they will think that the supply of natural resources is predictable. They will cite their analysis in question #1 as support for their position that things like oil production can be accurately forecast. But this argument is difficult to defend, given the rapid change in supply of commodities, as well as the ups and downs of demand for these commodities.

A better understanding of the complexities of prediction can be found in a WorldOil.com online magazine article from April 2007. The article describes how many different predictions about world oil production have been made, how much these predictions vary, the differing assumptions the predictions are based on, and the different definitions of "oil" that are used. This will give students a good sense of how complicated this issue is, and why it is important to think critically about media reports about the supply of natural resources.

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