Integrated Business Economics EE488

PEERA CHAROENPORN
ROOM 445
PEERA@ECON.TU.AC.TH

Course Description

- Prerequisite: EE311, EE312 and EE325 (or EE425)

- Economic theories and tools used to analyze business problems and business situations. The analysis includes understanding competition and financial strategies adopted by firms in different industries, as well as forecasting economic and industrial conditions in the future.

Grading

Class Presentations	30%	(Group: 6 presentations, 5% each)
Business Plan	20%	(Group: report (10%) + presentation (10%))
Class Participation	10%	(20 response papers)
Business Case Study	10 %	(present 5% + Report 5%)
Final Exam	30%	(May, 14th, 2015 9.00-12.00 am)
Total	100%	

Enrollment key EE488 for BE-Moodle = 8500

Class	Topics
1	**Introduction:** *Business Economics*
2	**Empirical Industrial Organization**
3	**Management Theory:** *(1) "Management Century" by Walter Kiechel HBR November 2012*
4	**Business Plan / Business Model:** *(2) Reinventing your business model"by Mark W. Johnson, Clayton M. Christensen, and Henning Kagermann, HBR December 2008*
5	*(3) SCB EIC Insight: Thailand's changing consumer demographics and what they mean. April 2010*
6	*(4) SCB EIC Insight: Capturing Thai Gen Y Consumer.* *November 2014*
7	**Public Policy:** (5) *Government in Your Business* by Robert B. Reich. HBR| July–August 2009
8	**Business Analysis:** *(6) When Growth Stalls by Matthew S. Olson, Derek van Bever, and Seth Verry HBR March 2008*
9	**Industry Analysis:** *(7) "What Is Strategy?" HBR 1996 by Michael Porter*
10	**Strategy:**(8) *"The Five Competitive Forces That Shape Strategy" by Michael E. Porter HBR January 2008*

Class	Topics
11	**Demand Forecasting:** (9) *"Four Step of Demand Forecasting" by William Barnett HBR 1988*
12	**Marketing:** *(10) "Rediscovering Market Segmentation"by Daniel Yankelovich HBR Feb 2006*
13	*(11) "Selling into Micro-markets" Manish Goyal, Maryanne Q. Hancock, and Homayoun Hatami by HBR July-August 2012*
14	*(12) "How Smart, Connected Products are transforming Competition" by Michael E. Porter and James E. Happelmann HBR November 2014*
15	**Pricing:** *(13) "How to stop consumer from fixating on Price?" by Marco Bertini and Luc Wathieu HBR May 2010*
16	*(14) "Pricing to Create Share Value: Rethinking the way prices are set can expand the pie for everyone". by Marco Bertini;John T. Gourville HBR June 2012*
17	**Non-Pricing:** *(15) "The Right Game: Use Game Theory to Shape Stategy" by Adam M. Brandenburger and Barry J. Nalebuff. HBR July-August 1995.*
18	*(16) "Strategies to Fight Lost Cost Rivals" by Nirmalya Kumar HBR December 2006*
19	**Production:** *(17) "Don't Let Your Supply Chain Control Your Business" by Thomas Choi and Tom Linton HBR December 2011.*
20	**Vertical Integration:** *(18) "The New M&A Playbook" by Clayton M. Christensen, Richard Altron, Curtis Rising and Andrew Waldeck HBR March 2011*

Class	Topics
21	**Financial Analysis:** *(19) "DO YOU KNOW YOUR COST OF CAPITAL? Probably not, if your company is like most" by Michael T. Jacobs and Anil Shivdasani. HBR July-August 2012*
22	**Financial Analysis:** *(20) "How Much Cash Does Your Company Need?" by Richard Passov HBR November 2003*
23	***Innovation:*** *(21) "Innovation the Classic Traps" by Rosabeth Moss Kanter HBR Nov. 2006*
24	**CSR:** *(22) "Creating Shared Value"* January–February 2011HBR by Michael E. Porter
25	**Human Resource:** *(23) "Economics of personnel and human resource management" by Morley Gunderson. Human Resource Management Review 11 (2001) 431–452*
26	**Organization:** *(24) Transaction-Cost Economics: The Governance of Contractual Relations. by Oliver E. Williamson. Journal of Law and Economics, Vol. 22(2) 1979, pp. 233-261*
27	**Case Study 1:** *Pepsi grows potatoes in China*
28	**Case Study 2:** *Charoen Pokphand Group in China*
29	**Business Plan 1:** Group 1 & 2
30	**Business Plan 2:** Group 3 & 4

Presentation

Group	Round 1	Round 2	Round 3	Round 4	Round 5	Round 6
1	1	5	9	13	17	21
2	2	6	10	14	18	22
3	3	7	11	15	19	23
4	4	8	12	16	20	24

What you will study in MBA?

Functional Skill

- BA.611 Accounting for Decision Making
- BA.621 Financial Management
- BA.631 Marketing Management
- BA.641 Human Resource Management
- BA.642 Leadership and Change
- BA.651 Logistics and Operations Management

Modern Management Concepts and Practices

- BA.605 Innovative Creation for Competitive Advantage
- BA.606 Corporate Governance and Social Responsibility
- BA.701 Performance Management and Value Creation
- BA.702 Seminar in Contemporary Strategic Management

Business Economics

- Business economics as a field in applied economics uses economic theory and quantitative methods to analyze business enterprises and the factors contributing to the diversity of organizational structures and the relationships of firms with labour, Capital and product markets.
- Business economics is concerned with economic issues and problems related to business organization, management, and strategy. Issues and problems include: an explanation of why firms emerge and exist; why they expand: horizontally, vertically and spacially; the role of entrepreneurs and entrepreneurship; the significance of organizational structure; the relationship of firms with the employees, the providers of capital, the customers, the government; the interactions between firms and the business environment

Business Economics

Ambiguity in the use of term

- The term 'business economics' is used in a variety of ways. Sometimes it is used as synonymously with industrial economics/industrial organisation, managerial economics, and economics for business.
- One view of the distinctions between these would be that business economics is wider in its scope than industrial economics in that it would be concerned not only with "industry" but also businesses in the service sector.
- Economics for business looks at the major principles of economics but focuses on applying these economic principles to the real world of business.
- Managerial economics is the application of economic methods in the managerial decision-making process.
- Program at Harvard University uses economic methods to analyze practical aspects of business, including business administration, management, and related fields of business economics

Industrial Organization

- **Industrial organization** is the field of economics that builds on the theory of the firm in examining the structure of, and boundaries between, firms and markets.
- The subject has been described as concerned with markets that "cannot easily be analyzed using the standard textbook competitive model."Industrial organization adds to the perfectly competitive model real-world frictions such as transaction costs, limited information, and barriers to entry of new firms that may be associated with imperfect competition. It analyzes determinants of firm and market organization and behavior as between competition and monopoly, including from government actions.
- There are different approaches to the subject. One is descriptive in providing an overview of industrial organization, such as measures of competition and the size-concentration of firms in an industry. A second uses microeconomic models to explain internal firm organization and market strategy. As to strategic firm interaction, non-cooperative game theory has become the standard unifying method of analysis. A third aspect is oriented to public policy as to economic regulation and antitrust law.

Managerial Economics

- **Managerial economics** as defined by Edwin Mansfield is "concerned with application of the economic concepts and economic analysis to the problems of formulating rational managerial decision." It is sometimes referred to as business economics and is a branch of economics that applies microeconomic analysis to decision methods of businesses or other management units. As such, it bridges economic theory and economics in practice. It draws heavily from quantitative techniques such as regression analysis and correlation, calculus. If there is a unifying theme that runs through most of managerial economics, it is the attempt to optimize business decisions given the firm's objectives and given constraints imposed by scarcity, for example through the use of operations research, mathematical programming, game theory for strategic decisions, and other computational methods.

Managerial Economics

Managerial decision areas include:

1. assessment of investible funds
2. selecting business area
3. choice of product
4. determining optimum output
5. determining price of product
6. determining input-combination and technology
7. sales promotion

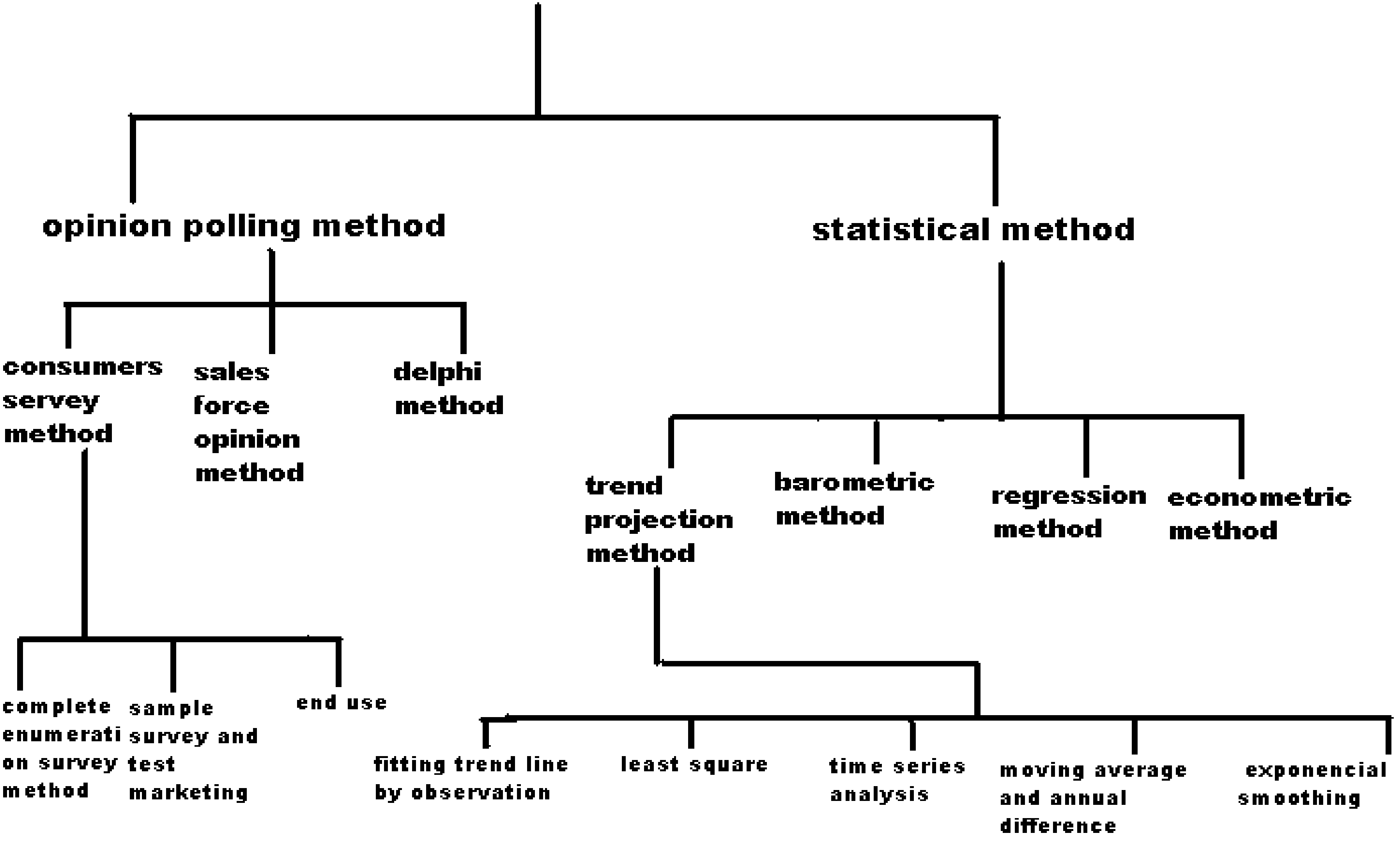
- **Risk analysis -** various models are used to quantify risk and asymmetric information and to employ them in decision rules to manage risk.
- **Production analysis -** microeconomic techniques are used to analyze production efficiency, optimum factor allocation, costs, economies of scale and to estimate the firm's cost function.
- **Pricing analysis -** microeconomic techniques are used to analyze various pricing decisions including transfer pricing, joint product pricing, price discrimination, price elasticity estimations, and choosing the optimum pricing method.
- **Capital budgeting -** Investment theory is used to examine a firm's capital purchasing decisions

FAMOUS OPTIMIZATION PROBLEMS IN ECONOMICS

Optimization Problem	Objective Function	Constraint	Control Variables	Parameters	Solution Functions	Optimal Value Function
Consumer's Problem	$U(x_1,\ldots,x_n)$ utility function	$p_1 \cdot x_1 + \ldots + p_n \cdot x_n = I$ budget constraint	$x_1,\ldots,x_n$ commodity levels	$p_1,\ldots,p_n, I$ prices and income	$x_i(p_1,\ldots,p_n,I)$ regular demand functions	$V(p_1,\ldots,p_n,I)$ indirect utility function
Expenditure Minimization Problem	$p_1 \cdot x_1 + \ldots + p_n \cdot x_n$ expenditure level	$U(x_1,\ldots,x_n) = \bar{u}$ desired utility level	$x_1,\ldots,x_n$ commodity levels	$p_1,\ldots,p_n, \bar{u}$ prices and utility level	$h_i(p_1,\ldots,p_n,\bar{u})$ compensated demand functions	$e(p_1,\ldots,p_n,\bar{u})$ expenditure function
Labor/Leisure Decision	$U(H,I)$ utility function	$I = I_0 + w \cdot (168 - H)$ budget constraint	H, I leisure time, disposable inc.	w, I_0 wage rate and nonwage income	$168 - H(w, I_0)$ labor supply function	$V(w, I_0)$ indirect utility function
Consumption/ Savings Decision	$U(c_1,c_2)$ utility function	$c_2 = I_2 + (1+i) \cdot (I_1 - c_1)$ budget constraint	c_1, c_2 consumption levels	I_1, I_2, i income stream and interest rate	$c_1(I_1, I_2, i)$, $c_2(I_1, I_2, i)$ consumption functions	$V(I_1, I_2, i)$ indirect utility function
Long Run Cost Minimization	$w \cdot L + r \cdot K$ total cost	$F(L,K) = Q$ desired output	L, K factor levels	Q, w, r desired output and factor prices	$L(Q,w,r)$, $K(Q,w,r)$ output-constrained factor demand functions	$LTC(Q,w,r)$ long run total cost function
Long Run Profit Maximization (in terms of Q)	$P \cdot Q - LTC(Q,w,r)$ total profit	none	Q output level	P, w, r output price and factor prices	$Q(P,w,r)$ long run supply function	$\pi(P,w,r)$ long run profit function
Long Run Profit Maximization (in terms of L and K)	$P \cdot F(L,K) - w \cdot L - r \cdot K$ total profit	none	L, K factor levels	P, w, r output price and factor prices	$L(P,w,r)$, $K(P,w,r)$ factor demand functions	$\pi(P,w,r)$ long run profit function

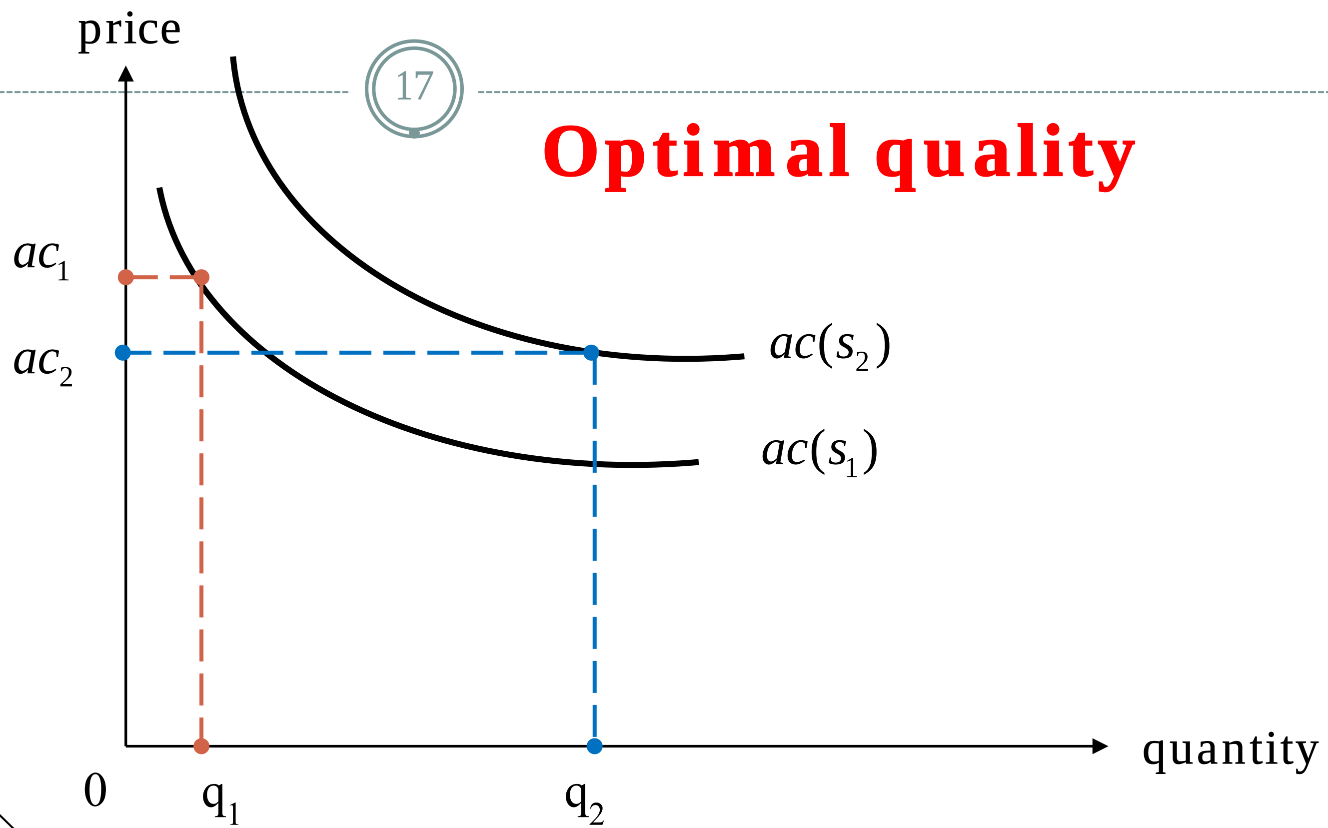
Year = 0	1	2	3	4
Sale (Revenue)= (P x Q) Quantity Demand (PRODUCT) (PRICE) – in the pocket	Size? Growth? Seasonal?			
Cost of goods sold (Expense) Production (Make or Buy) Fixed Cost Machineries/Equipment Factory/ Land –rent or buy Variable Cost Raw Material Overhead Cost Transportation cost	% of Sale Growth?		New !	Salvage Value
HR (Salary x Person)---month/day/job				
Shelf/ Office Rental (PLACE)				
Advertising exp (PROMOTION) Commission				
Gross Profit				
Free Cash Flow—cash vs. accounting				

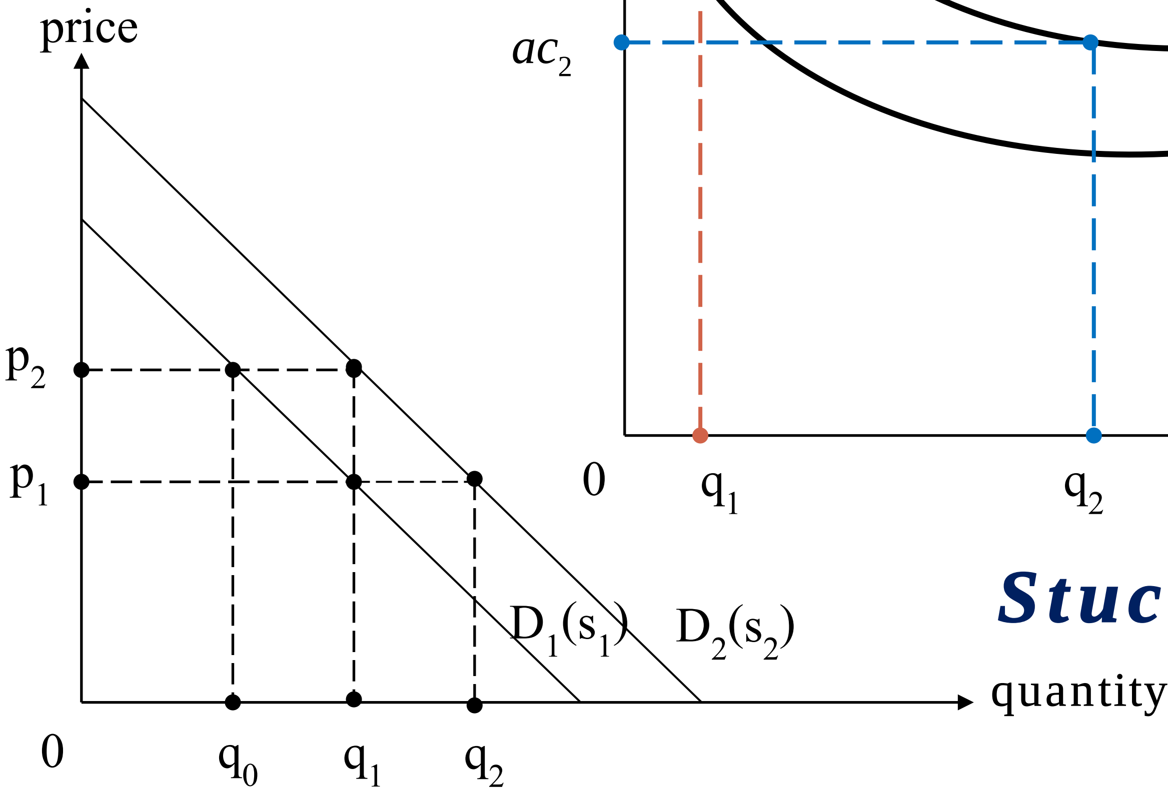
Methods Of Demand Forecasting



PRODUCT

Optimal quality

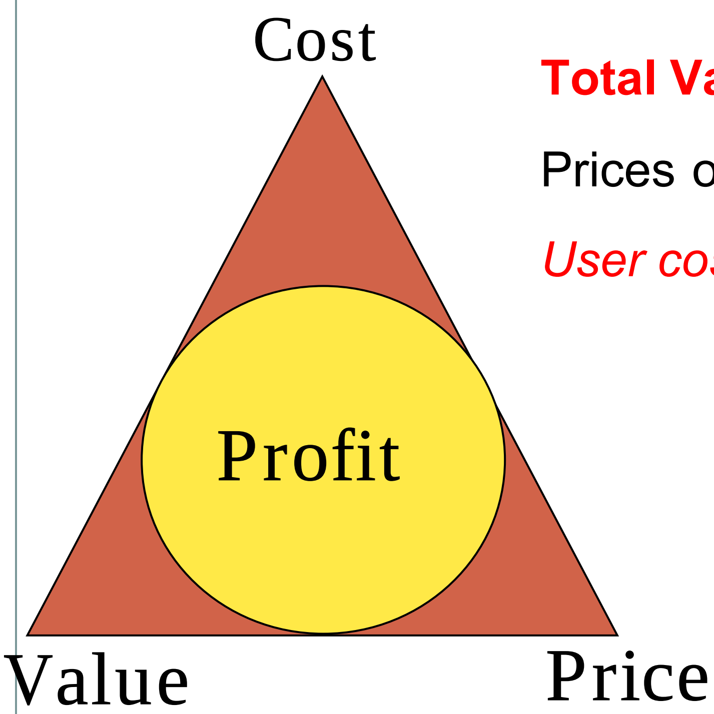




Stuck in the middle?

Target customer

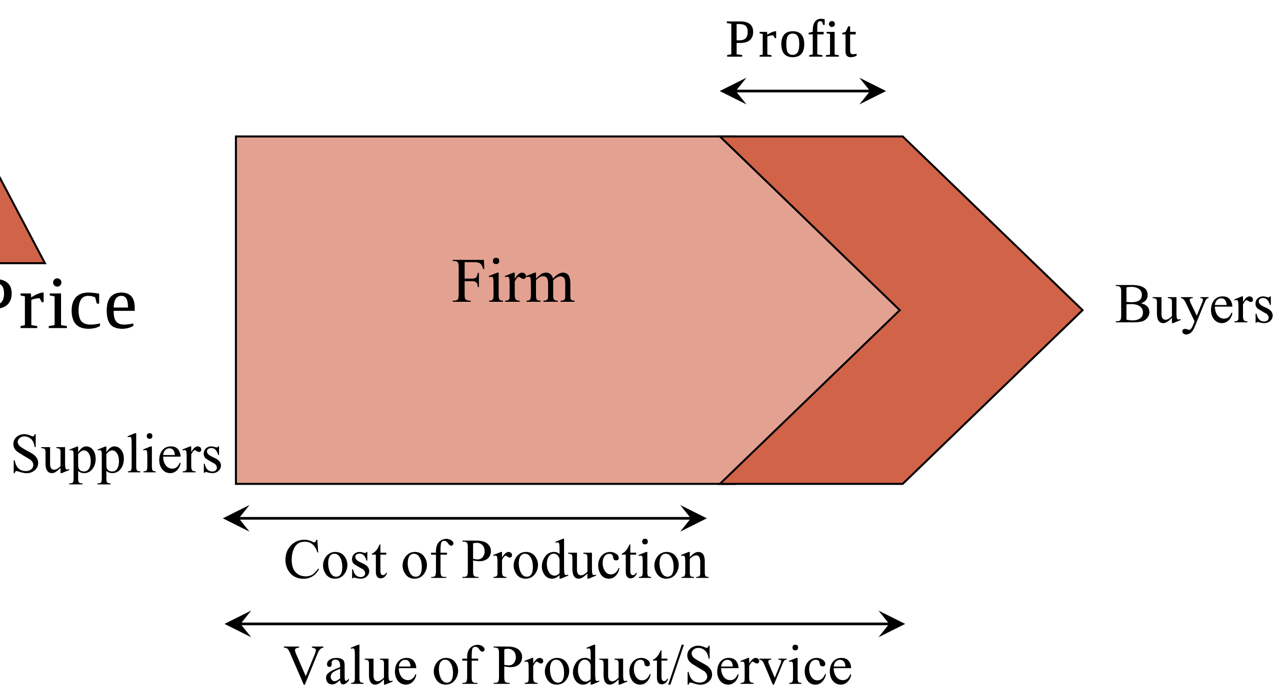
Firm's Value Creation and Profit



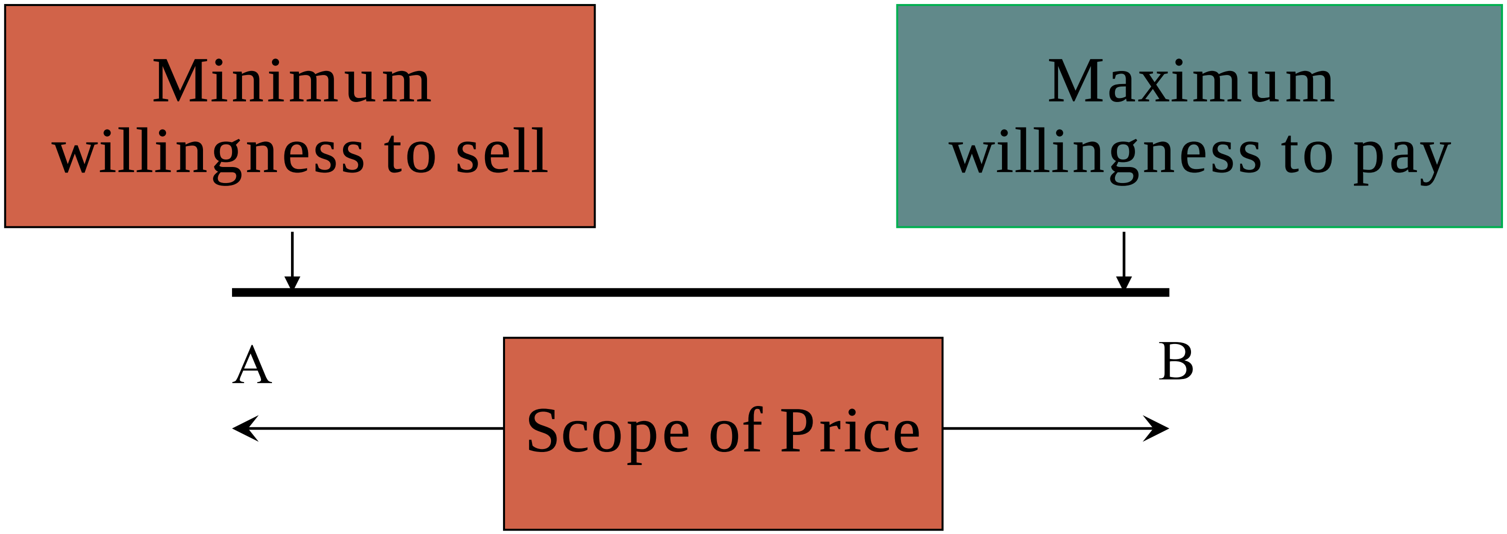
Total Value – Price –Consumer Cost = Consumer Surplus

Prices or tariffs;

User costs; Transaction costs; Search costs; Psychic costs



PRICE: Value, Cost, and Price → Profit



Value creation

PLACE: Approaches to Distribution

- These strategies require tradeoffs: ➔*Cost*
  - **Wide**--essential to low involvement goods
  - **Selective**--desire to maintain image
  - **Exclusive**--very high prestige needed or very high service requirements
- Direct-to-Customer Sales
  - High need for customization—especially if the work can be done by the customer
  - Rapid decline in the value of inventory
  - High value/bulk ratio
  - Low need for customer to manually inspect the product
  - Highly specialized product requiring a very large assortment of inventory

PROMOTION: Advertising

- A Rule of Thumb for Advertising

$$(A/Q)(\Delta Q/\Delta A) = E_A = \text{Adv. elasticity of demand}$$

$$(P - MC)/P = -1/E_P$$

$$A/PQ = -(E_A/E_P) = \text{Rule of Thumb}$$

❑ The proportion of sales revenue that a profit-maximizing monopolist spends on advertising is thus determined by a simple elasticity ratio.

❑ The advertising intensity must equal the ratio of elasticities of demand with respect to advertising and price

❑ The demand function is more price inelastic (i.e., when εP is smaller), a monopolist chooses a high advertising intensity and a large markup.

Industrial Economics

Industrial Organization: Theory and Policy

Study of structure, conduct and performance of firm, relationship of various market structures and business operations and resource allocation, as well as an analysis of firm's strategic behavior

Chapter 1
Introduction to Industrial Organization

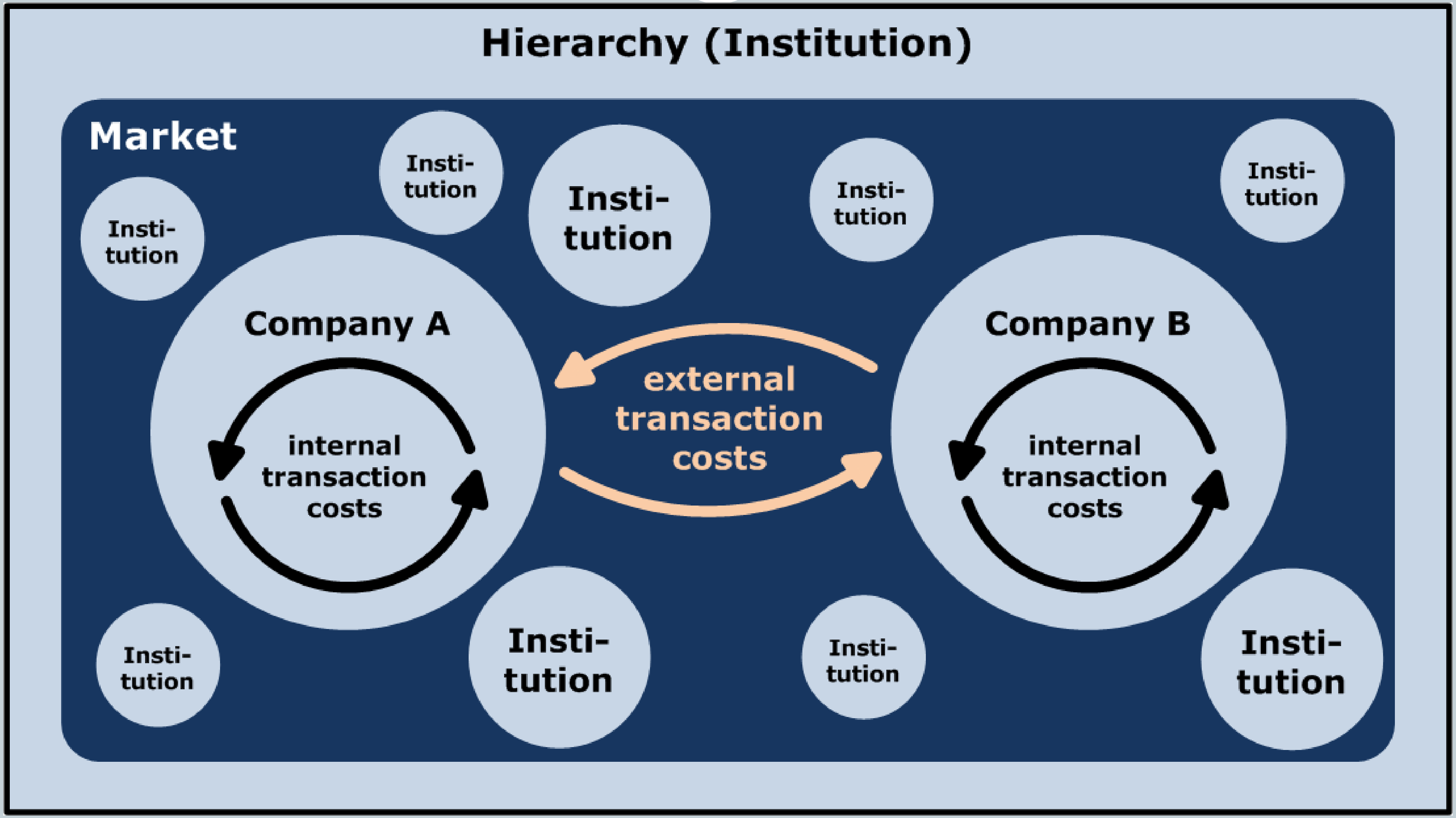
- **Industrial Organization:** the study of the structure of firms and markets and of their interactions

- **Models:** There are at least two major approaches to study of industrial organization.

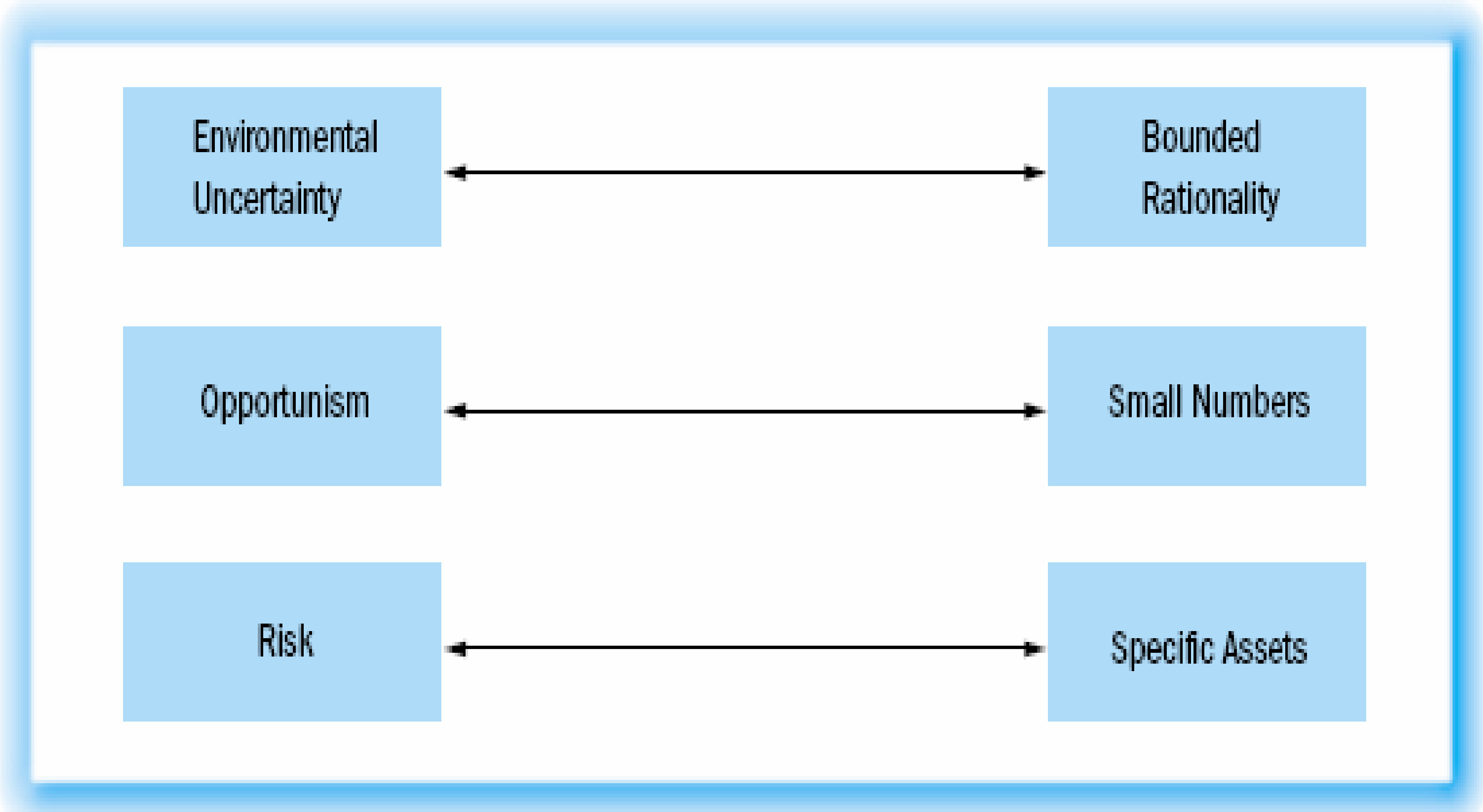
1. Structure – Conduct – Performance *(SCP approach)* and
2. Price Theory : uses microeconomics models to explain firm behavior and market structure. *(Transaction Cost Economics; Game theory; Contestable Market)*

- **Organization:** Basic Theory; Market Structure; Business Practices: Strategies and Conduct; Information ,Advertising ,and Disclosure; Dynamic Models and Market Clearing; Government Policies and their Effects

Transaction Cost Theory



Sources of Transaction Costs



Matching Governance Structures with Commercial Transaction

Frequency	Investment Characteristic		
	Non-Specific	Mixed	Idiosyncratic
Occasional	Market Governance	Trilateral Governance	
Recurrent		Bilateral Governance	Unified Governance (Vertical Integration)

Examples of ***trilateral governance*** structures include long-term contracting, reciprocal trading, regulation and franchising

Make-or-Buy Re-Examined

by Carter C. Higgin

Reasons of Making:

1. Cost studies indicate it is cheaper for you to make than to buy
2. Making fits your know-how, your equipment, and your tradition.
3. Idle capacity is available to absorb overhead.
4. What you are considering is unusual or complex ; direct supervision is needed to assure control.
5. Making will facilitate your control of parts changes, inventories, and deliveries.
6. The part is hard to transport.
7. The design of the part or its processing is confidential.
8. You do not wish to depend on a single outside source of supply.

Make-or-Buy Re-Examined

by Carter C. Higgin

- **Reasons for Buying:**

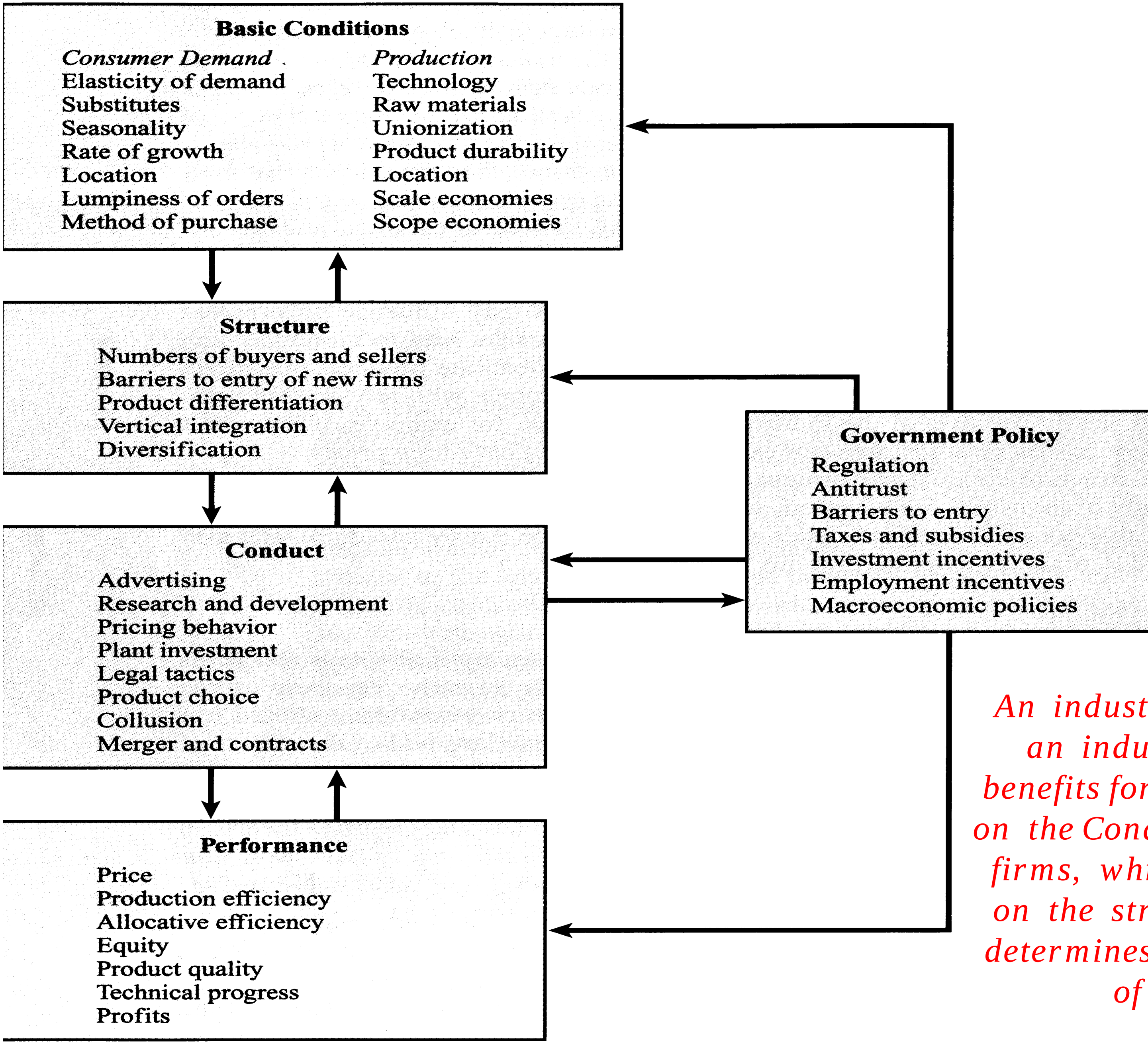
1. Cost studies indicate it is cheaper for you to buy than to make.
2. Space, equipment, time, and/ or skill are not available for you to develop the necessary production operations.
3. Because of small volume or because of other capital needs, the investment in making is not attractive.
4. You wish someone else to face seasonal, cyclical, or risky market demands.
5. The need for special techniques, or equipment, makes buying more logical. Your supplier will help you produce a better engineered end product.
6. You think it is best for your executives to concentrate on your specialty.
7. You want a check on your own operations.
8. Patents or customer-supplier relationships favor going outside.

Economics of personnel and human resource management
Morley Gunderson

- Economic phenomenon: fixed hiring costs, asymmetric information, option values
- Deferred compensation
- Pensions and Mandatory retirement)
- Superstar salaries
- Compensation as tournament prizes
- Teams, cooperation, and egalitarian pay structures
- Option values

- Long-hours and overtime coexisting with unemployment and underemployment often within the same organisation;
- The reluctance of seemingly risk averse workers to accept small wage cuts to avoid the possibility of a layoff
- The payment of fringe benefits that may not be valued by many employees

- The "regular" hiring of temporary workers when permanent workers are available;
- Egalitarian pay structures and fairness in compensation
- Monopsony market structure: The persistent reporting of vacancies on the part of firms but a reluctance to raise wages to fill those vacancies
- The use of piece rates in some jobs and salary structures that are based on relative ranking of workers in other jobs;
- Tenure or "up-or-out" rules where people who are not promoted are required to leave rather than work for lower pay.



An industry 's performance of an industry in producing benefits for consumers depends on the Conduct (behavior) of its firms, which , in tern, depends on the structure (Factors that determines the competitiveness of the market)

Part1: Introduction and Theory

Chapter1: Overview
- Models
- Organization

Chapter2: The Firm and Costs
- The Firm
- Mergers and Acquisitions
- Cost Concepts
- Economies of Scale
- Cost Concepts for Multi-product Firms

Chapter3: Competition
- Perfect Competition
- Elasticities and the Residual Demand Curve
- Efficiency and Welfare
- Entry and Exit
- Externalities
- Limitations of Perfect Competition

Chapter4: Monopolies, Monopsonies, and Dominant Firms
- Monopoly Behavior
- The Costs and Benefits of Monopoly
- Creating and Maintaining a Monopoly
- Profits and Monopoly
- Monopsony
- Dominant Firm with a competitive fringe

Part2: Market Structures

Chapter5: Cartels (Oligopoly Joint Decision Making)

- Why Cartels Form
- Creating and Enforcing the Cartel
- Consumers Gain as Cartels fail Price-Fixing Laws

Chapter6: Non-cooperative Oligopoly

- Game Theory
- Single-Period Oligopoly Models
- Multi-period Game
- Testing Oligopoly Models

Chapter7: Product Differentiation and Monopolistic Competition

- Differentiated Products
- The Representative Consumer Model
- Location Models
- Hybrid Models

Chapter8: Industry Structure and Performance

- Theories of Price markups and profits
- Structure Conduct Performance

Part3: Business Practices (Strategies and Conduct)

Chapter9: Price Discrimination

- Non-Uniform Pricing
- Incentive and Conditions for Price Discrimination
- Types of Price Discrimination
- Welfare Effects of Price Discrimination

Chapter10: Advanced Topics in Pricing

- Nonlinear Pricing
- Tie-in-Sales
- Quality choice
- Other Methods of Nonlinear Pricing

Chaper11: Strategic Behavior

- Strategic Behavior Defined
- Non Cooperative Strategic
- Cooperative Strategic Behavior

Chaper12: Vertical Integration and Vertical Restrictions

- The Reasons for and against Vertical Integration
- The life cycle of a firm
- Vertical Restrictions
- Franchising

Part4: Information, Advertising, and Disclosure

Chapter13: Information

- Why information is limited
- Limited information about quality
- Limited information about price
- Providing Consumer Information lower price

Chapter14: Advertising and Disclosure

- Information and advertising
- Effects of Advertising on welfare
- False advertising

Part5: Dynamic Models and Market Clearing

Chapter15: Decision Making Over Time (Durability)

- How long should durable good last?
- Renting vs Selling by a Monopoly

Chaper16: Patents and Technological Change

- Patents, Copyrights and Trademarks
- Incentives for inventions are needed
- Patents Prize, Research Contracts and joint ventures
- Market Structure

Chapter17: How markets Clear (Theory and Facts)

- How markets clear: 3 simple theories
- Empirical Evidence on the role of price in allocating goods
- Explaining the evidence
- Market structure is more than concentration

Part6: Government Policies and Their Effects

Chapter18: International Trade

- Reasons for Trade between countries
- Tariffs, Subsidies, and Quotas

Chapter19: Antitrust Laws and Policy

- The antitrust Laws and their purposes
- Market power and the definition of markets
- Cooperation among competition
- Exclusionary actions and other strategic behavior
- Price Discrimination
- Effects of Antitrust Laws on the organization of firms

Chapter20: Regulation and Deregulation

- The objectives of Regulators
- Making monopolies more competitive
- Making competitive industries more monopolistic
- Deregulation

Business Economics & the Development of Strategic Business Plans

- ✓MACROECONOMIC FORECAST
- ✓ANALYSES OF THE INDUSTRY, COMPETITORS
- ✓RELEVANT REGULATORY AND TRADE ISSUES

Macroeconomic Forecast

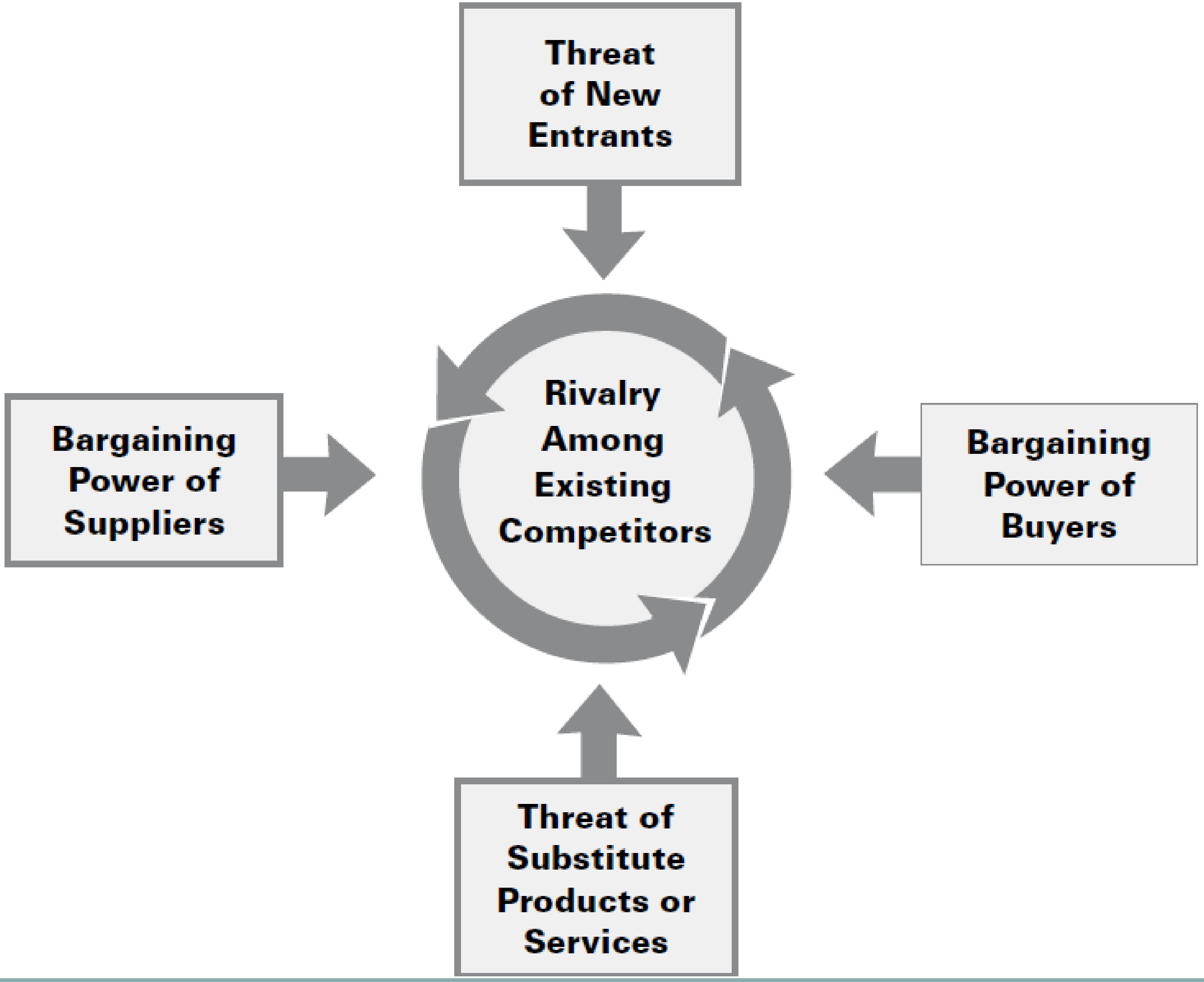
- The macroeconomic forecast that drives industry demand and overall cost levels is critical at every phase of planning
- The forecast is an integral part of an analytical effort to understand and plan for an uncertain future rather than a discreet set of data points for cranking out budget and earnings projections.
- Long-term, trend forecasts spanning the planning horizon (typically five years) of growth in GNP, disposable income, personal consumption expenditures, employment, inflation, interest and exchange rates and energy and other raw materials prices are all essential inputs into the strategic planning process.
- They are essential not only as basic drivers of demand and cost, but also as determinants of competitive advantage and changing business opportunities and threats.

Macroeconomic Forecast

- These macroeconomic forecasts must take on a global dimension, which does not mean simply generating forecasts for the various regions of the world in which the company operates.
- Companies in global industries need integrated, worldwide design, research, production and marketing strategies to compete successfully.
- The strategic business planner therefore needs to understand the implications of developments in one region of the world for interdependent operations in others, and how the economies of the different regions of the world are linked together through global financial and product markets.
- For example, forecasts of slowing U.S. consumption and growing exports to reduce the huge U.S. trade deficit must be accompanied by the implications for demand, imports and growth in large trade-surplus nations such as Germany and Japan, the NICs and the debt-ridden countries of South America.

Industry Analysis

- The role of the business economist changes dramatically with the added responsibility for the analysis of the competitive structure of the industry (ies) in which the company (SBUs) competes.
- Analyses of the number and size distribution of sellers and buyers in the industry, potential new entrants, capacity utilization and expansion, economies of scale, entry barriers, vertical integration, diversification, distribution channels and downstream component suppliers all are undertaken to provide strategic business planners with the information they need to plan effectively.
- These analyses help planners understand the nature of competition in the industry; identify current and future business opportunities and risks; and assess the long-term profit potential of alternate strategies.


Threat of New Entrants
Bargaining Power of Suppliers
Rivalry Among Existing Competitors
Bargaining Power of Buyers
Threat of Substitute Products or Services

Competitive Analysis

- Competitive analysis is typically conducted at the SBU, division and corporate levels within the firm. The business economist contributes to competitive analysis primarily at the corporate level.
- This analysis is directed at providing a broad strategic perspective on the company's competitors, which is needed to supplement the more product or functional-specific analysis conducted at the SBU and divisional levels.
- The business economist also helps avoid costly duplication by conducting competitive analyses needed by several SBUs competing against common rivals.
- Finally, the competitive analyses conducted by the business economist, who has no line responsibilities, often provide a more objective assessment of competitors' strengths, and the probable success of their strategic initiatives

Competitive Analysis

- The business economist is well equipped to conduct analyses of competitors' production and distribution systems, sourcing strategies, R&D programs, incentive systems, capital structures and financial position.
- But the most important contribution of the business economist to competitive analysis is the analysis of cost differences among companies in the industry, and the reasons for those differences.
- The tools of the business economist are particularly useful for analyzing differences in labor, materials and capital cost, and differences in productivity.
- For global industries, the tools of the business economist are absolutely essential because these comparative cost analyses must include the important effects of exchange rates on costs, and country-specific cost advantages arising from differences in relative factor endowments, culture and the institutional relationships among business, government and labor.


KRAFT
Coca-Cola
PEPSICO
Kellogg's
MARS
WRIGLEY
Nestlé
P&G
Johnson & Johnson
Unilever
GLACEAU
L'ORÉAL
IAMS
Yum!
QUAKER
DASANI
Tropicana
pepsi
Dole
VICHY
BOSS
DIESEL
Vittel
NESCAFE
PURINA
ALPO
Gillette
TAMPAX
Pampers
DURACELL
BRAUN
Tide
Cascade
IVORY
Crest
Scope
LISTERINE
Dove
AXE
MAGNUM
Triscuit
Snapple
Cheerios
Chex
fibre1
Nutri-Grain
ALTOIDS
m&m's

Public Policy Analysis

- The business economist must analyze the impact on the company of a broad array of safety, health, environmental, energy and industrial policies (e.g., plant closing legislation).
- These regulations can have an important impact on the demand for the company's product, its cost and performance and on the company's relative competitive position.
- The tools of the business economist are especially helpful in analyzing the impact of regulation on product cost and performance as viewed by the consumer, who may well discount any social benefits in his purchase decision.
- Even more importantly, the business economist must analyze the differential competitive effects these regulations can have on individual competitors, or between current and potential competitors or domestic and foreign competitors.

Public Policy Analysis

- Environmental regulations that limit plant or product emissions illustrate the full range of public policy analysis required of the business economist.
- These regulations add to the cost of the product and often reduce its performance, while the social benefits in terms of cleaner air are not adequately valued by the individual consumer because of a classic free-rider problem.
- These regulations often benefit existing firms, which may be "grandfathered-in" under the regulations, over new entrants that are required to install the best available (and most expensive) technology.
- They often disadvantage domestic firms relative to foreign producers who face less stringent or perhaps no regulation. If economies of scale are significant in reducing emissions, large manufacturers also may be advantaged over smaller producers.

Trade Policy

- Trade policy has become a critical element in strategic planning for international companies. Trade policy also can have an important impact on the competitive position of domestic companies.
- A company cannot avoid international competition by restricting its operations to its home market. Indeed, such a strategy may only increase the company's exposure to global competitive risks by limiting its access to international product and financial hedging strategies.
- Trade restraints, local content and export requirements, exchange rate policies and nontariff barriers to trade all can have significant effects on a company's competitive position and on its efforts to implement an integrated, global strategy.
- Like domestic regulations, they can have an important impact on the company's competitive position.

Trade Policy

- The strategic opportunities and risks created by international trade policies are illustrated by the current effort to improve the integration of the European Common Market by harmonizing regulations, standardizing border taxes and lowering trade barriers among the Common Market nations.
- This development will create important strategic opportunities and risks for different companies.
- This integration should lower costs and increase overall economic growth and consumer demand. It also will change relative prices, and thus the demand for the goods and services of particular companies.
- For countries outside the Common Market, there is the risk of heightened trade barriers as the internal barriers within the Common Market are dismantled.

Business Economics and the Implementation of the Strategic Plans

- The business economist can assist in the implementation of the business plans by helping ensure that a good strategic fit exist among the company's strategy and its organizational structure and internal management systems.
- The internal organizational structure of the firm is critical to the successful implementation of the business plan because it effects the basic flow of information to decision makers (including the information provided by business economists); the decision makers' collective capacity for processing that information; and the incentives facing those decision makers.
- An ill-conceived organizational structure will result in decision makers receiving inadequate or biased information; being unable to process that information in a timely manner; or facing incentives for decisions inconsistent with the company's long-term strategic goals.

Business Economics and the Implementation of the Strategic Plans

- Business economists can provide substantial assistance to strategic planners attempting to design internal organizational structures that will ensure the effective implementation of their strategic plans.
- A rich tradition of organizational efficiency analysis in business economics traces its origins to the fundamental insights of Ronald Coase, who first noted that "a firm will tend to expand until the costs of organizing an extra transaction within the firm become equal to the cost of carrying out the same transaction by means of exchange on the open market or the cost of organizing in another firm."Subsequent work has added to the richness of this analysis in especially relevant ways.
- This work now provides both a theoretical and empirical foundation for assessing the impact of different organizational structures (e.g., functional and multi-divisional structures) on the firm's ability to process complex information, eliminate sub-goal pursuit and monitor SBU performance.

Business Economics and the Implementation of the Strategic Plans

- Following the dictum that "structure follows strategy," General Motors, after extensive analysis, undertook a massive reorganization in 1984.
- General Motors had developed strategies to shorten product lead times, to increase the differentiation of its vehicles and to improve quality and lower cost through better coordination among product design, engineering and manufacturing.
- Implementing this strategy required a new, less centralized organizational structure to improve the coordination and speed of decision making.
- The company created two new car groups (C-P-C and B-O-C) that were given total responsibility for engineering, manufacturing and marketing their products and that were held accountable for the quality and performance of their vehicles and for the profitability of their operations.

Business Economics and the Implementation of the Strategic Plans

- Business economists have an important role to play in the design of the all-important incentive systems. The incentive systems must be congruent with the strategic business plan to ensure the successful implementation of that plan.
- The rewards of key decision makers must be tied to accomplishment of the long-term goals of the business plan to ensure an identity of corporate and self interests.
- This typically requires incentives to be tied to external benchmarks of long-term financial or stock performance.
- Establishing and measuring progress against such external benchmarks is vastly more difficult than basing rewards on annual performance relative to historical norms for the company.
- The business economist, utilizing his knowledge of competitors and competitive conditions, can play an important role in helping to establish appropriate external benchmarks that account for differences in financial and business risks.

Writing an Effective Business Plan

THE NEED FOR PLANNING

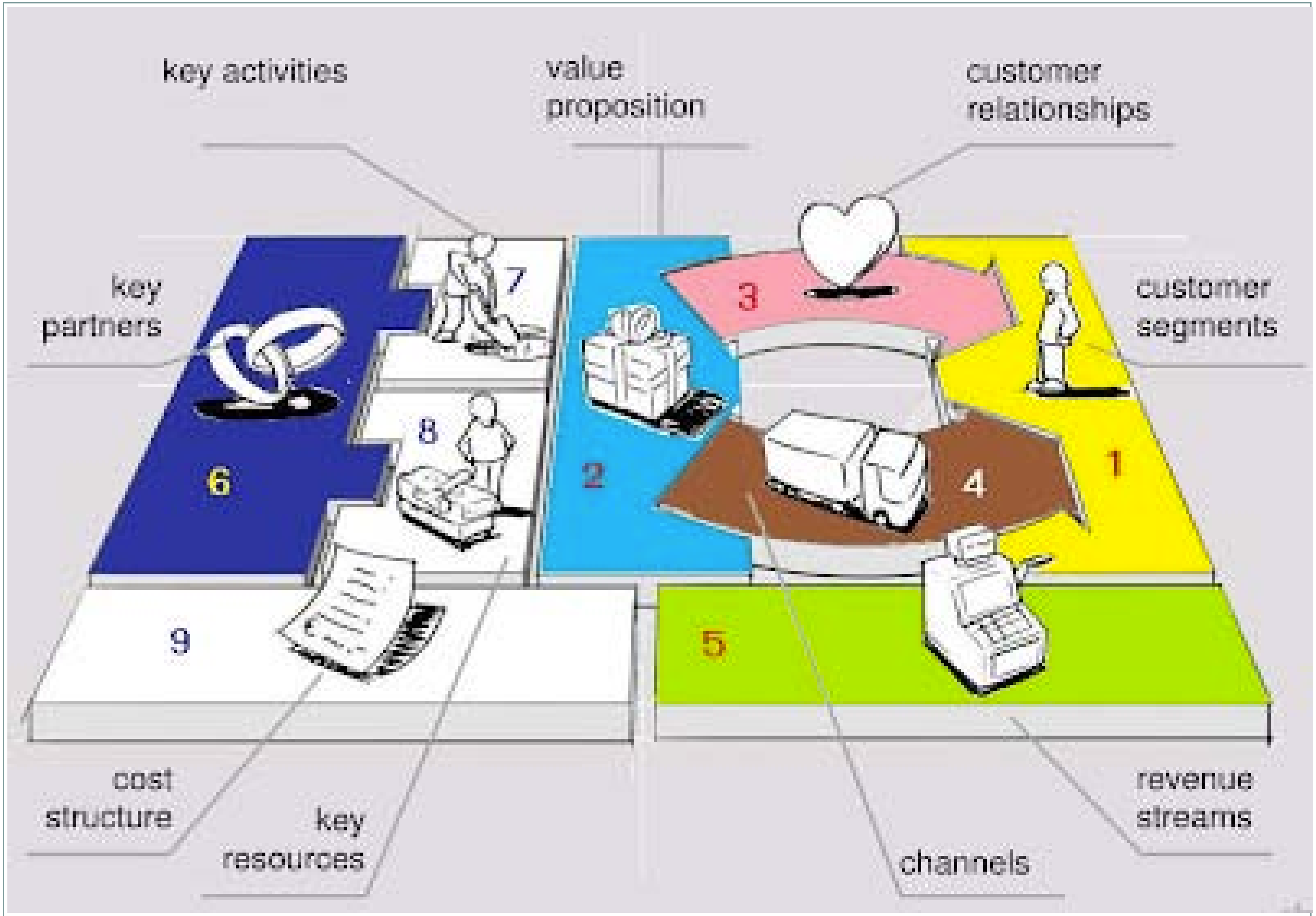
- ➢ Discuss the company's goals for the near-term and long-term future
- ➢ Show how the goals can be achieved
- ➢ Demonstrate that realization of the plan will satisfy the reader's requirements.

E X T E R N A L U S E S F O R T H E P L A N

- ➢ The track records of the company, the market, and the key executives
- ➢ The feasibility of achieving the forecasts
- ➢ The uniqueness of the product and its technology
- ➢ The quality of the management.

Question:

- ➢ What are the long-term goals of your company? The near-term?
- ➢ What do you wish to gain from your business plan (e.g., funding, reconciled internal vision, etc.)?
- ➢ What are the likely needs and requirements of the readers?


key activities
value proposition
customer relationships
key partners
7
3
customer segments
6
8
2
4
1
9
5
cost structure
key resources
channels
revenue streams

THE PROCESS OFWRITING A BUSINESS PLAN GATHERING THE RIGHT DATA

- **Company Description**
  - Name
  - Legal form
  - Location
  - Financial highlights
  - Shareholders
- **Management and Organization**
  - Organization chart
  - Key management
  - Board of Directors
  - Consultants and advisors
  - Compensation and other employee agreements
  - Other shareholders, rights and resolutions
- **Market and Competitors**
  - Market statistics
  - Competitor data
  - Market and customer surveys
- **Product or Services**
  - Product literature and technical specifications
  - Contracts and/or purchase orders
  - Competitive advantages
  - Patent, license, and trademarks
  - Regulatory approvals or industry standards
  - Operations plan
  - Research and development plans
- **Marketing and Sales**
  - Marketing plan
  - Marketing vehicles
  - Marketing materials
- **Financial Information**
  - Financial statements for up to past5 years
  - Financial forecasts and projections/assumptions
  - Amount and timing of needed funding

Does the Executive Summary demonstrate?

- ➢ that the business has been thoroughly planned and researched?
- ➢ a business proposition that makes sense?
- ➢ an accurate understanding of the value proposition of your product or service?
- ➢ that the business proposition offers real competitive advantages?
- ➢ a knowledge of the industry and target market?
- ➢ a sense of enthusiasm for the business?
- ➢ a realistic picture of the risks inherent in the business?

The Company, Strategy, and Management Team

- What business are you in?
- What is the purpose of your business?
- What are your products and/or services? How are they related to your mission?
- What benefits do your products and/or services provide to your customers?
- What led you to develop your business, its products or services?
- What is your vision for your business? How large do you want to become?
- Is your vision statement based in reality and is it aligned with realistic growth objectives?

The Company, Strategy, and Management Team

- ➢ Why are you uniquely qualified to be in this business?
- ➢ How you are distinctive from your competition?
- ➢ What is the legal name of your business?
- ➢ What is your legal structure and is it appropriate for your future plans?
- ➢ Where are you located?
- ➢ What stage are you presently at? Conceptual phase? Start-up? Mature business?
- ➢ What is your current financial position?
- ➢ What are your company's weaknesses and how are you addressing them?
- ➢ Who are the key members of your management team?

MANAGEMENT AND ORGANIZATION

- ➢ Why is the CEO qualified to lead the company?
- ➢ Do the strengths and experience of the management team match the goals and strategies of the business?
- ➢ Does the management team have both technical and business acumen?
- ➢ Are your compensation arrangements aligned with the goals and objectives of the business?
- ➢Do you have any strategic alliances that give you access to talent that is not resident in your management team? If your management team is not complete, what is your action plan to add the necessary talent? What impact is this having on current operations?
- ➢Are your compensation programs competitive enough to attract and retain the right human resources?
- ➢ How will you address the ongoing development needs of your workforce?
- ➢ Who are your outside experts and what will it cost to retain them?
- ➢Does your Board of Directors or advisors bring relevant experience to your management team?

THE MARKET AND COMPETITORS

- In which industry or industries do you operate?
- How are these industries changing? How fast?
- What changes will affect the need for your product or service?
- Are there changes in the political or regulatory landscape, or social values, that affect the need for your product or service?
- How will changes in technology change your industry?
- What is/are your specific target market(s)?
- Who are your customers today and are they in the identified target market(s)?
- What market trends/changes may affect your customers' ability to afford your product or service?

THE MARKET AND COMPETITORS

- ➢ What is the approximate size and geographic spread of your target market(s)?
- ➢ What is the approximate growth rate of your target market(s)?
- ➢ Which companies and which types of companies make up your competition?
- ➢ What are the barriers to entry for your competition?
- ➢Have you honestly analyzed your competitors' strengths and weaknesses?
- ➢What are the key factors motivating customers to buy your product or service?
- ➢How does your product or service integrate with other products or services? Does the sale of your product or service depend on the sale of another product or service?

THE MARKET AND COMPETITORS

- ➢Is it costly for your customer to change product or service providers? Are they loyal to your competitors?
- ➢ Is your product or service vulnerable to substitution?
- ➢How is your product or service differentiated from the competition's on a basis other than price?
- ➢Is your market price sensitive? If so, where is your product or service positioned on the price curve?
- ➢ Is there perceived value in higher prices?
- ➢How are you pricing related items such as service and support? What are your credit terms?
- ➢How will your competition respond to your pricing strategy?

The Product or Service

- What are the key milestones in the research and development process? At what stage are you in that process? When will your product be ready to sell?
- What are costs to complete the development of the current product? What are the ongoing costs?
- Are you capable of monitoring the need for product improvements and changing the production cost structure as the industry, competitor products, and customer needs change?
- How much are you spending on research and development? How much is the competition spending?
- How do you select new products for research and development?
- Do you have any intellectual property?
- Is your product or product name registered with appropriate governmental bodies? If your business is expected to be global, have you taken into account international patent, intellectual property and other legal influences?

The Product or Service

- How much manufacturing space will you need?
- What type of capital equipment will you require? What impact will changing technology have on your equipment needs?
- Will you build all of the product in house or subcontract out a portion of the production process?
- Are there any critical processes that have not been developed?
- Are any parts or supplies difficult to get, or do they require long-lead times? How reliable are key suppliers?
- Are there any parts that can be obtained only from a single source or only from overseas?
- What are the backup sources for these materials?
- How will you monitor quality? How can customers contact you if they have comments or problems?
- Have you identified business risks and developed a risk management strategy to address them?

MARKETING AND SALES

- How are you positioning your product or service?
- What are the key messages that you want to convey in your marketing materials?
- What types of marketing media will you use to promote your product or service?
- What is your marketing plan? What mix of media will you use? How much will you spend? How do these compare to similar efforts deployed by the competition?
- How will you use public relations to help promote your product or service?
- What distribution channels are you using and what selling methods are appropriate for each channel?
- Do you need your own sales force? Dealers? Representatives?
- What is your commission structure?
- Do you have any strategic alliances that will allow you to reach your target market(s) efficiently and cost effectively?

THE FINANCIAL INFORMATION

- ➢ Have you carefully analyzed your current and historical financial statements in order to explain your results to investors and to form the foundation for your projections?
- ➢ Are your assumptions consistent with the results of your market analysis and the other sections of the business plan?
- ➢Have you completed several different financial projections to understand the impact of different scenarios on the key financial metrics of your business?
- ➢ How much capital do you need and over what period of time?
- ➢ What form of investment are you seeking?
- ➢ How will you use the funds obtained?
- ➢ How do you plan to finance further company growth?
- ➢ What is the exit/payback strategy for lenders and investors?

What to expect from your business plan?

- ➢ Is the business concept solid and feasible? Can it be implemented in a reasonable time frame?
- ➢ Is your product or service viable? Does it add significant value to the customer?
- ➢ Does a real market exist?
- ➢ Are your strategies consistent with your evaluation of the marketplace and your capabilities?
- ➢ Is your strategy ethical and legal?
- ➢ Have you thoroughly evaluated different strategies? Can you defend your choices among the alternatives identified?

What to expect from your business plan?

- ➢ What are the target markets and are they large enough to support the business plan?
- ➢ Is the target market growth potential high?
- ➢ Have you thoroughly and honestly evaluated your competition?
- ➢ Are your goals focused, tied to the strategy, measurable, specific, and understandable?
- ➢ Is the financial plan realistic?
- ➢ Does the funding request match the investors' criteria?
- ➢ Is management experienced and capable?
- ➢ Do you have a detailed and realistic timetable and set of benchmarks by which to measure progress?
- ➢ How and when will the investors get their investment back?

Outline of Business Plan

- Company Description
- Management and Organization
  - Organization chart
  - Key management
  - Compensation plans and policies
  - Staffing plan by department
- Market and Competitors
  - General description
  - Market statistics
  - Customer data *(Demographics; Needs; Loyalty; Buying behavior and purchasing criteria)*
  - Competitor data *(Type and number; Location; Strengths and weaknesses; Turnover ;Barriers to entry ; Strategy; Potential future competitors)*
  - Market and customer surveys *(Pricing; Sensitivity; Segmentation)*

Outline of Business Plan

- Product or Services
  - Product literature and technical specifications
  - Competitive advantages
  - Current development stage
  - Product life span information
  - Impact of technology
  - Patent, license, and trademarks
  - Regulatory approvals or industry standards
  - Business risks
  - Operations plan *(Production process; Facilities; Capacity; Security of supply channels; inventory requirements)*
  - Research and development plans
  - Quality control plans
  - Customer service plans

Outline of Business Plan

- Marketing and Sales
  - Marketing plan
  - Marketing vehicles
  - Marketing materials
  - Strategic alliances
  - Distribution channels
  - Sales force
- Financial Information
  - Financial statements from the past five years
  - Financial forecasts, projections, and assumptions
  - Amount and timing of needed funding