



CHAPTER 1

What Is a Business?

INTRODUCTION TO BUSINESS

Learning Objectives

- To define **what a business is**
- To identify the different **types of businesses** based on legal, size, and primary function
- To describe well-established and modern **business models**
- To choose the appropriate **legal structure** for a business
- To outline the **benefits of a business** as well as its functions



A **business** is an organized group of people involved in professional, commercial, or industrial activities

Business has many possible meanings, depending on its context:

- Company
- Industry
- Service

A business:

- Earns a profit
- Starts with an idea
- Must generate what we refer to as value in business

What would you say is Netflix's value in business?



Benefits of Businesses

From a macro-perspective:

- Sell goods and services that are wanted by consumers
- Connect capital to production to grow economies and produce profits
- Bring employment opportunities
- Source of professional growth and satisfaction for employees
- Create wealth opportunities
- Engage in research and development to improve or create new products and services
- Help develop a country as they invest back into communities and support government activities via tax dollars

When a business runs locally, the community experiences:

- Access to products and services that are needed
- Create job opportunities for residents
- Inject money into the local economy via tax dollars
- Bring a point of pride and satisfaction
- Provide access for minorities and women to establish themselves as entrepreneurs and support their families
- Increased interest in supporting other businesses and the community as these businesses will drive traffic to their own business and to the community where they live

Benefits of Businesses Continued

From an entrepreneurial perspective:

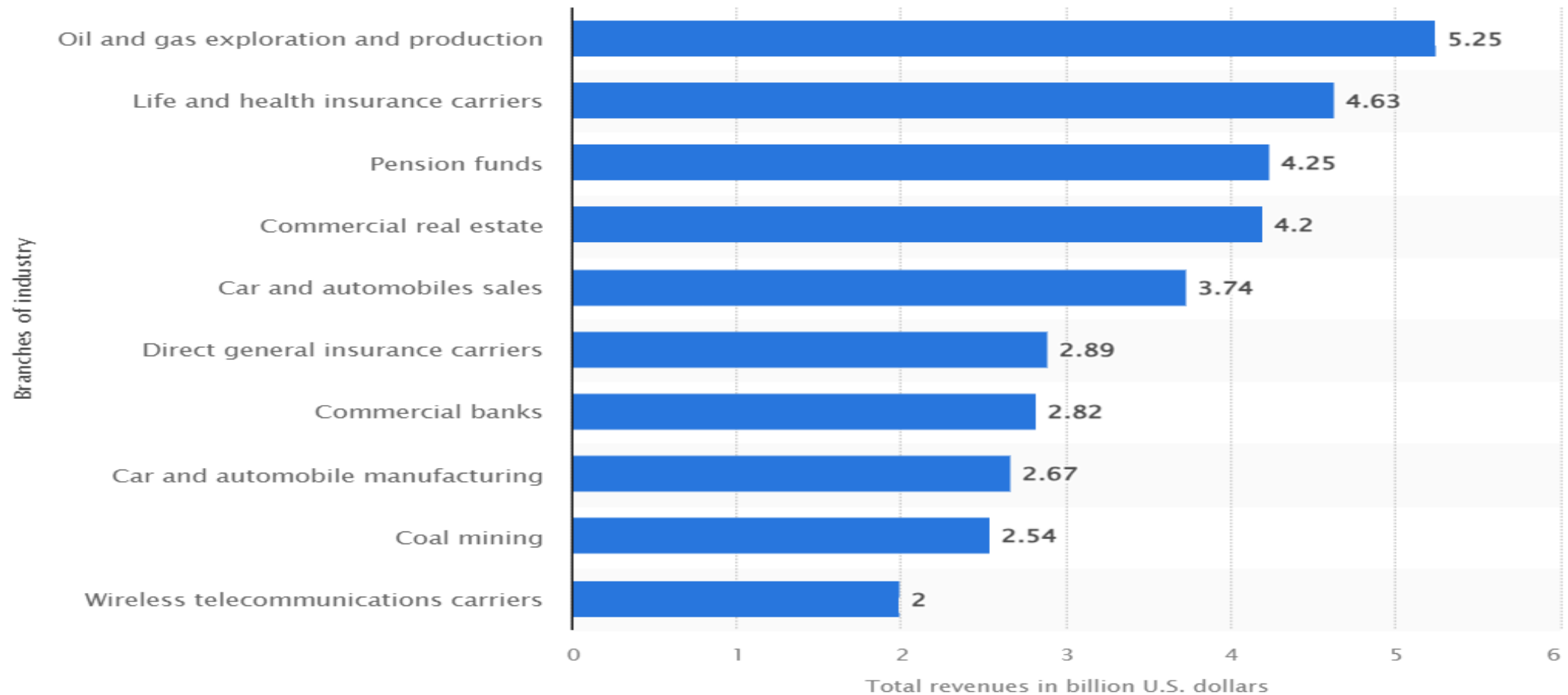
- Personal satisfaction from seeing an idea come to fruition and being dedicated to it
- Personal pride as you build something out of your ideas, hard work, and abilities
- Creative freedom and continuous learning opportunities from being an owner
- Financial rewards from generating income
- Independence to be your own boss and set your own lifestyle
- Deciding the people you work with as you do the hiring
- Happiness of following what you are passionate about



The setting where businesses conduct their operations and generate value is known as an **industry**.

- **Industry:** Group of businesses that are classified together based on their primary business activities.
 - Examples: banking, broadcasting, financial services, transportation (railroads), investment and asset management, software, and real estate
- ❖ Give me your examples...

Leading industries worldwide from 2019 to 2023, by revenue *(in trillion U.S. dollars)*



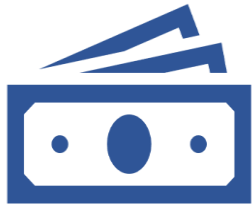
There are several ways to look at types of businesses.



Businesses can also be found depending whether we are focusing on size and primary function.



1) A business can legally be formed under three types:



For profit
Focused on
gaining a
financial
benefit



Non-Profit
Aim at pursuing
a charitable,
religious, artistic,
educational,
scientific, or
literary purpose



Government
Legal entities
who act on
behalf of the
country's
government
while providing
commercial
activities



2) Types of Businesses Based on Size



Small Business

Usually no more than
1,500 employees
Revenues based on industry

The USA



Medium Business

1,500 to 2,000 employees
Annual revenues between \$10
million and \$1 billion



Large Enterprise

Over 2,000 employees
Annual revenues are
over \$1 billion

KG

No more than 50 employees
Revenue no more than 500
thousand Som

51 to 200 employees
Revenue between 500 - 2000
thousand Som

Over 201 employees
Revenue over 2000 thousand
Som

1.1. Number, number of employees and the amount of the gross added value of small and medium-sized enterprises						
Items	2017	2018	2019	2020	2021	2022
<i>Total</i>						
The number of subjects, units						
small businesses	13,858	14,520	16,199	16,302	16,252	16,587
medium-sized enterprises	795	769	779	717	798	788
individual entrepreneurs	389,778	401,658	411,405	418,763	429,985	442,507
(peasant) farms ¹	428,730	439,602	452,308	461,581	467,423	473,161
Number of employees², thousand persons	479.2	492.7	519.2	519.6	522.9	534.6
small businesses	53.2	56.6	73.4	69.0	58.9	58.9
medium-sized enterprises	36.2	34.4	34.4	31.8	34.0	33.2
individual entrepreneurs	389.8	401.7	411.4	418.8	430.0	442.5

3) Types of businesses based on their primary function



Retail

This is a function where a business sells goods and services to consumers, usually in small quantities for personal consumption



Services

Businesses who provide services do not sell a tangible item or commodity. They sell the benefit of completing a task for the consumer.



Manufacturing

Focuses on the large production of raw materials into finished products. To achieve this, manufacturing companies employ human labor, machines, tools, processes, chemicals, and technologies based on their finished product.



3) Types of businesses based on their primary function (cont.)



Franchising

Focuses on expanding a business by licensing to others (franchisees) by selling a franchise.



Distribution

It is the activity of delivering products and services usually from manufacturer to the consumer. A company who moves the products and services is part of a distribution channel.



Multilevel and Network Marketing

Multilevel marketing: companies recruit people as distributors to generate sales and to recruit people by selling the opportunity to make money.

Network marketing: hiring or recruiting new individuals that will become part of one's network while selling without a hierarchy



CHECK YOUR UNDERSTANDING



Ford can be classified as what kind of primary business function?

- ☐ Retail
- ☐ Services
- ☐ Manufacturing
- ☐ Franchising
- ☐ Distribution
- ☐ Multilevel and Network Marketing

Check My Answer

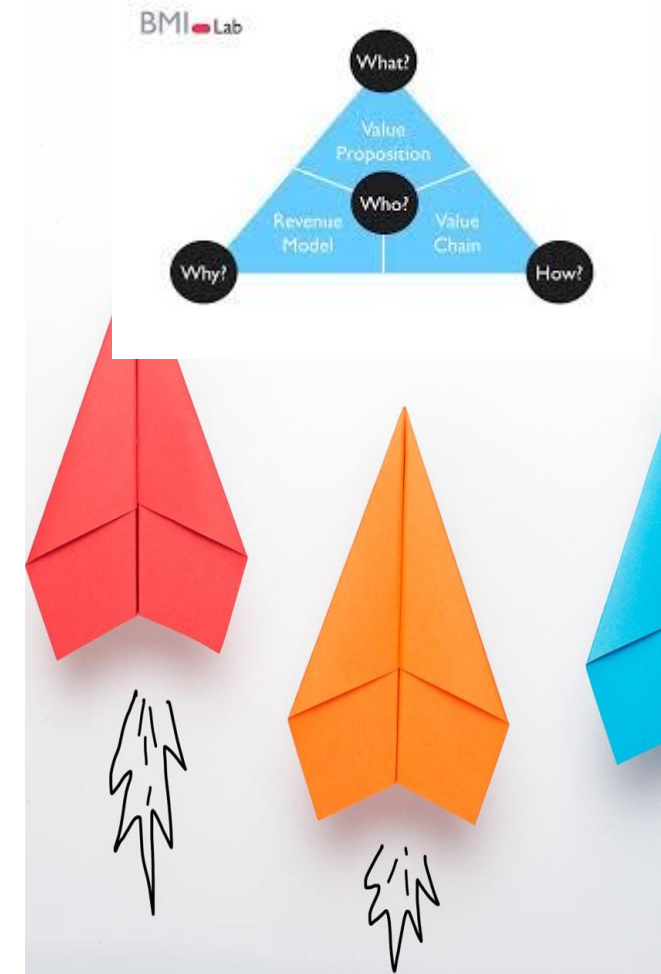


However, classifying businesses based on their type is not enough to become knowledgeable and understand how businesses work and generate profits.

To do so, we also need to talk about **business models**.

Business models are the primary way in which a business functions and makes money

- A great business model answers 4 questions:
 - Who is the customer?
 - What does the customer value?
 - How do we make money?
 - What is the economic logic that describes how we provide value to customers at an appropriate cost?
- Think of it as a description of how the business operates



Newer (or modern) business models we enjoy today, continued:



Subscription Business

- Consumers pay a subscription fee to enjoy a product or service. Popular types of subscription businesses are:
- Software as a Service (SaaS) (e.g., Salesforce, Dropbox, Slack, and Hubspot),
- Ecommerce (e.g., Dollar Shave Club), and
- Accessibility (e.g., Netflix, Spotify, and Amazon Prime).



Bundling

- Selling together goods and services that related usually at a discount. This is done to make what the business offers more attractive to consumers and generate demand.
- Geico's insurance bundles (home and car) and McDonald's combo (burger, fries, and drink)



Newer (or modern) business models we enjoy today, continued:



Freemium

- The basic services are offered for free and the premium or improved service for a charge, e.g., LinkedIn, Dropbox, and MailChimp



Leasing

- Rather than own, businesses and consumers are encouraged to rent products and services. We Work encourages businesses to rent office space rather than own it



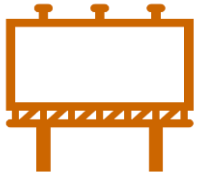
Crowdsourcing

- Businesses receive the knowledge, ideas, and work from people via a digital space, known as a crowdsourcing platform or micro-labor site or in a specific place and assign the micro-tasks.
- Qmarkets.net is a crowdsourcing platform and Waze is a crowd-powered app that allows users to report traffic jams and automatically gives directions for the best route to take



Newer (or modern) business models we enjoy today, continued:

Advertising supported revenue



- Now a new model but it has been revitalized. Traditionally used by mass media (TV, radio, etc.), it provides content for free to users while selling ads to generate revenue to businesses
- New platforms include ad revenue for Facebook and Instagram

Low Cost



- Providing the product or service at the lowest possible costs to pass on the savings to the consumers.
- Think Walmart or Southwest Airlines



Peer-to-peer

- The company acts as an intermediary to facilitate exchanges between providers of goods and services and consumers.
- Think Uber and Airbnb: online platform connects hosts (owners) with guests worldwide.

In-class exercise.
In pairs or individually identify by matching the business model for each of the businesses listed

Businesses:

1. Hulu (paid streaming TV service)
2. Birchbox (paid personalized makeup and beauty products)
3. Hootsuite (basic free software, additional features for a price)
4. Jetworks (rent airplanes)
5. Dollar Stores (low-cost products)
6. Lyft (get a ride for a great price)
7. Lego submit your design (toy company)
8. Bloggers placing ads from other businesses in their blogs
9. My Starbucks idea (submit your product/flavor ideas to this coffee company)

Available answers:

- Premium
- Accessibility (subscription service)
- Leasing
- Crowdsourcing
- Advertising supported revenue
- Low cost
- Peer-to-peer
- Boxes (subscription service)

Business model ANSWERS

Businesses:

1. Hulu (paid streaming TV service)
2. Birchbox (paid personalized makeup and beauty products)
3. Hootsuite (basic free software, if one wants additional functions then one must pay)
4. Jetworks (rent airplanes)
5. Dollar Stores (low-cost products)
6. Lyft (get a ride for a great price)
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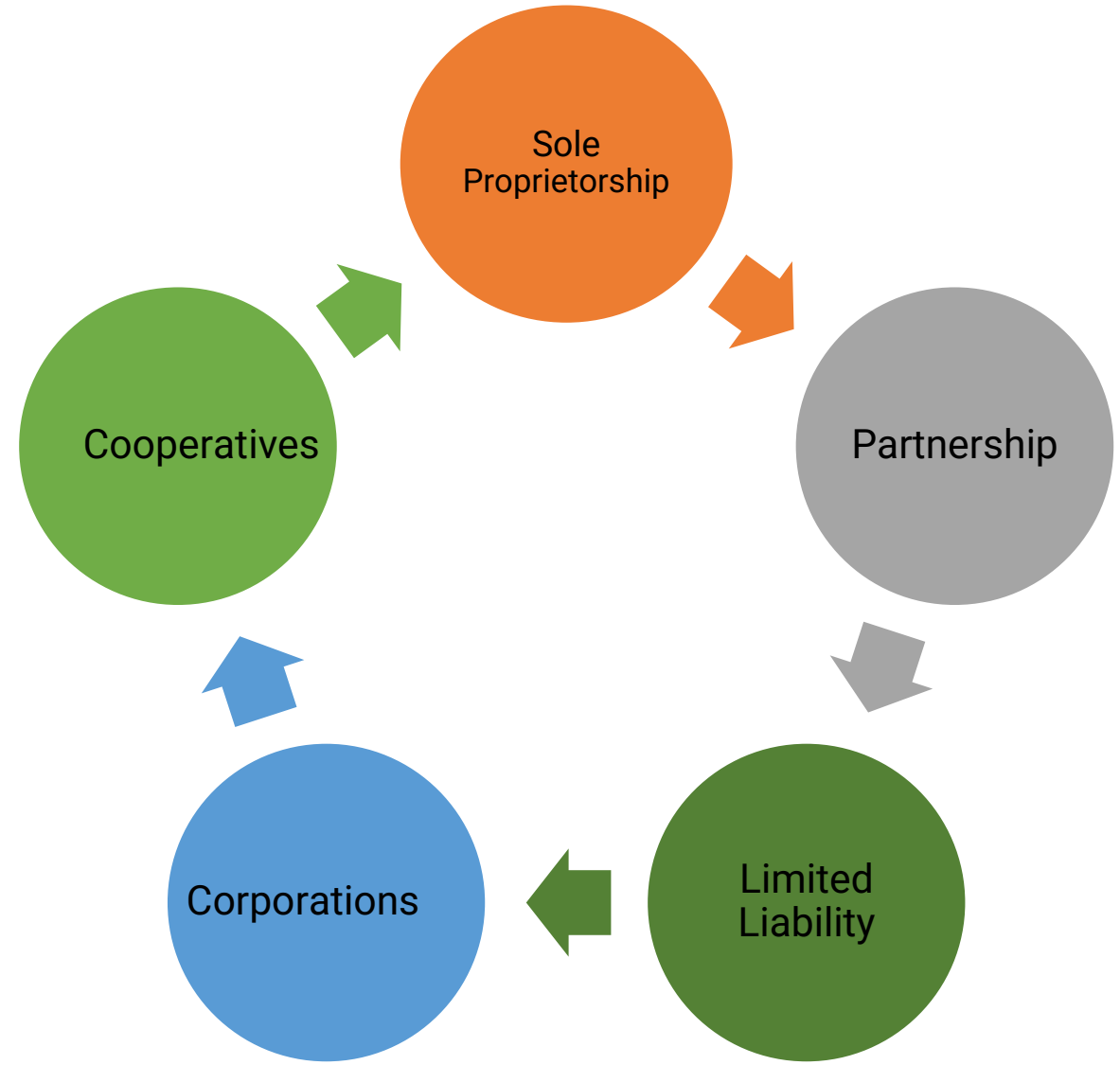
1. Accessibility (subscription service)
2. Boxes (subscription service)
3. Freemium
4. Leasing
5. Low cost
6. Peer-to-peer
7. Crowdsourcing
8. Advertising supported revenue
9. Crowdsourcing



Legal Structures: Choosing one that works!

Choosing a legal structure that works

- It is the **legal roadmap** that guides the business for the rest of its life or until the owners decide to change it.
- It will have an influence in daily operations, how much a business pays in taxes, and whether the founder(s) personal assets are protected
- A business structure is chosen before registering a business with the state.
 - Tax id number and trade name



Legal structure: Sole Proprietorship

- **Default structure:**
 - Easy to set up (there are no partners or boards), have a low cost of formation (only license fees and business taxes)
 - Offer additional tax deductions that other structures do not (such as health care deduction)
 - Provide an easy exit by being dissolved without paperwork
- **Challenges:**
 - It does not produce a separate business entity
 - Owner is also required to pay self-income tax
 - It is harder to raise capital as there are no partners

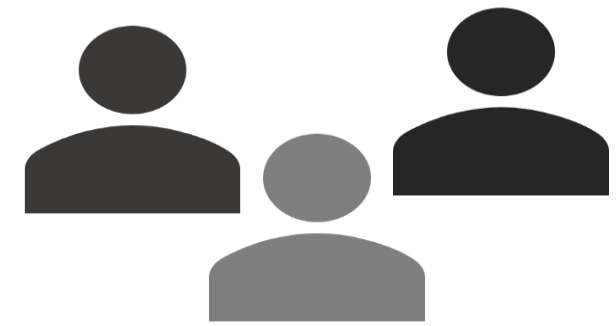


Sole Proprietorship is the simplest and most common type of business, where **one person owns and runs the business** and is personally responsible for its profits and losses

- **Examples of sole proprietorships:**
 - Single-person art or photography studio,
 - a small local grocery store,
 - an information technology (IT) service,
 - a bookkeeping business, and
 - home healthcare services.



Legal structure: Partnership



- Association where two or more individuals join a legal agreement to form a business for profit
- The partners become co-owners. They invest money, buildings, land, or vehicles
- There are two popular types:

Limited Partnership (LP)

- One partner(s) has unlimited legal responsibilities (personal liability) while the rest has limited responsibility and limited control
- Created to incentivize that limited partners invested without personal liability

Limited Liability Partnerships (LLP)

- Provide limited liability to every owner (a great protection for partners)
- Partners are also not responsible for the actions of the other partners



Legal structure: Limited Liability Company LLC



- An LLC is a business structure that protects owners' personal assets while allowing flexible management and favorable taxation

Key Features:

1. Limited Liability: Owners (called members) are generally not personally responsible for business debts.
2. Flexible Management: Can be managed by members or appointed managers.
3. Separate Legal Entity: The company exists independently of its owners.

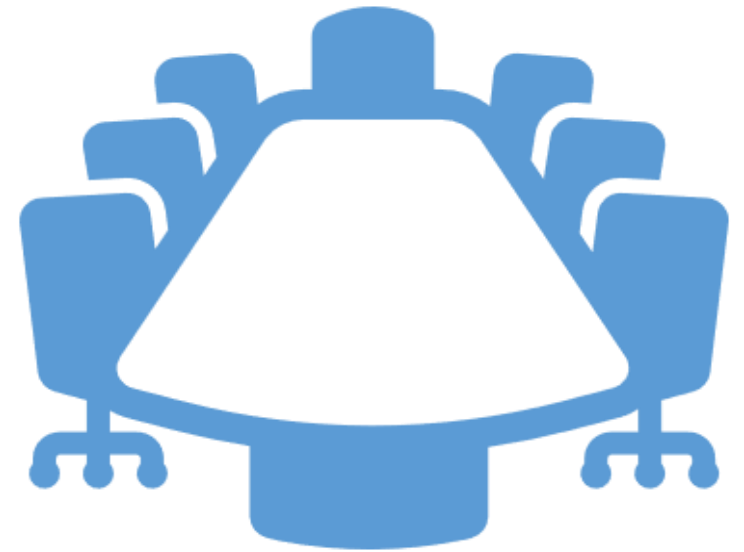
Famous LLCs

- Ebay,
- Sony,
- Nike,
- Coca Cola,
- Pepsi Cola, and
- J.P. Morgan Chase & Co (banks)



Legal structure: Corporations

- Legal entity with its own rights that is separate from its owners.
 - Thus, they can be sued, sue, and sell property and the rights to its ownership using stocks.
- People owning stocks become shareholders.
- Corporations are required to hold formal meetings and keep minutes of such meetings.
- Corporations have a board of directors, officers, and shareholders.



There are several types of corporations:



C Corporations

- Can have an unlimited number of investors and are owned by the shareholders
- They are taxed as separate entities
- Subject to double taxation
- Examples are Amazon, Bank of America, Walmart, McDonald's, Apple, Microsoft

S Corporations

- Better for smaller corporation as it allows up to 100 shareholders
- No double taxation – shareholders pay taxes
- Some disadvantages are:
 - required ongoing fees to stay in compliance
 - provide less management flexibility
 - all shareholders must be U.S. citizens or residents



Legal structure: Cooperatives

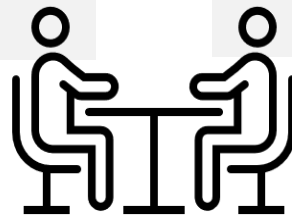
- Cooperatives (Co-ops) are businesses owned and run by a group of people for their mutual benefit, rather than by individual owners or external shareholders.
- Examples:
 - Agricultural cooperatives (farmers pooling resources to sell crops)
 - Credit unions (members pool funds for financial services)
 - Consumer cooperatives (grocery stores owned by shoppers)
 - Housing cooperatives



To operate, a business engages in **business functions**

- Processes and activities carried out to support operations and generate income.
- Business functions are:
 - *interdependent* of each other
 - should have *objectives and standards*
- *Communication* among functions and people is encouraged

- The business functions:
 - Supply Chain
 - Accounting
 - People
 - Marketing
 - Sales
 - Management



Business functions are the main activities or roles that a business performs to operate successfully and achieve its goals.

Businesses impact many individuals and groups inside and outside of their operations known as **Business Stakeholders**



- Individual or party with an interest in the business and the outcome of the business' actions.
 - Thus, as a business makes decisions it has to consider what will be the effect of its decisions on such groups.
- Stakeholders can also impact a business' course:
 - What the business sells, decisions and processes,
 - The level of financial support and investment they give,
 - The business's goals and plans by whether they support it,
 - Sales and loyalty, and participation and commitment in the operations and functions.



TYPES OF STAKEHOLDERS





Business Stakeholders are divided into two types:

Internal Stakeholders

Have a direct or financial part in the business's operations:

- Employees
- Owners

External Stakeholders

Individuals or groups who can have an impact on the business if they buy the product or service or if they have a relationship with the business:

- Customers
- Competitors
- Shareholders
- Communities
- Government



Assignment: Identifying External Stakeholders

Instructions

In teams, students will select a business (for-profit or nonprofit) and identify and briefly describe the following external stakeholders

Pick two of the following scenarios and discuss how these stakeholders would be impacted by:

1. A natural occurrence (hurricane, pandemic, earthquake, floods, wildfires)
2. An economic downturn (no economic growth, lack of employment, low consumer confidence in markets, falling house prices)
3. Product change (the business decides to buy lower quality materials from suppliers to save in costs)
4. Company expansion (the business decides to open a second location in a different part of the city)

