



Section 3.2

Activity 3.2.1

1. Examples of overhead/indirect costs Dakota would have include:
 - Marketing
 - Administration
 - Rent.
2. Examples of direct costs Dakota would have are:
 - Labour
 - Materials.
3. Overhead/indirect costs are often considered fixed costs because they do not change with a business's level of production.
4. Problems Dakota might encounter when trying to reduce its direct cost might be:
 - Redundancy payments
 - Unions protecting wages
 - Quality of the product falls if cheaper materials are used.
5. Benefits Dakota might derive from a reduction in costs include:
 - It can reduce prices and gain market share
 - Higher profit margins
 - It can use funds the saved cost brings, in another area.

Activity 3.2.2

1. Classified costs:
 - Rent – indirect, fixed
 - Management salaries – indirect, fixed
 - Electricity – indirect, semi-variable
 - Piece-rate labour – direct, variable
 - Depreciation – indirect, fixed
 - Lease of company cars – indirect, fixed
 - Wood and production materials – direct, variable
 - Maintenance – direct, semi-variable



2. Reasons for the classification:

- Rent, management salaries, depreciation, lease of company cars and maintenance do not change with output and are spread across the different activities of the organisation
- Piece-rate labour and materials do change directly with output and can be attributed to a part of the organisation
- Maintenance and electricity is spread across the organisation but have a fixed and variable element.
- The maintenance of the chair can be attributed to part of the organisation but the cost does not vary directly.

Activity 3.2.3

1. A 'revenue stream' is the income a business receives from a particular type of business activity.
2. It might be expensive for PepsiCo and Facebook to develop a range of revenue streams because of the cost to:
 - Pepsi of promoting Gatorade and Tropicana
 - Facebook of acquiring Instagram.
3. Benefits to Facebook of developing a range of revenue streams from Instagram might be that it:
 - Is a growing market
 - Spreads risk
 - Is complementary to other Facebook products.

Exam practice question

1. 'Total revenue' is the income of the business calculated as price multiplied by quantity sold.
2. Twitter can report an overall loss when total revenue is rising if:
 - Costs are rising faster than revenue as output increases
 - Initial fixed costs of setting up Twitter are still not covered.
3. Benefits to Twitter of developing new revenue streams might be:
 - Greater revenue
 - Spreads risks
 - Complementary revenue streams.
4. The advantages of Twitter's decision to increase its scale of production includes:



- Economies of scale
- Profit growth
- Revenue rises to quickly cover set-up costs
- Growth in market influence.

The disadvantages might be:

- Diseconomies of scale
- If variable costs rise faster than revenues
- Threat to cash flow if outflows rise faster than inflows
- Pressure on staff.

Key concept question

The different strategies a business might adopt to increase revenue in a globalised business environment include:

- Exporting goods to overseas markets, but there are transport costs
- Franchising production into overseas markets, but there are issues of control
- Licensing production to overseas markets, but there are issues of control
- Setting up production in overseas markets, but there are set-up costs
- Joint venture with another company to produce in an overseas market, but there needs to be agreement with another business.