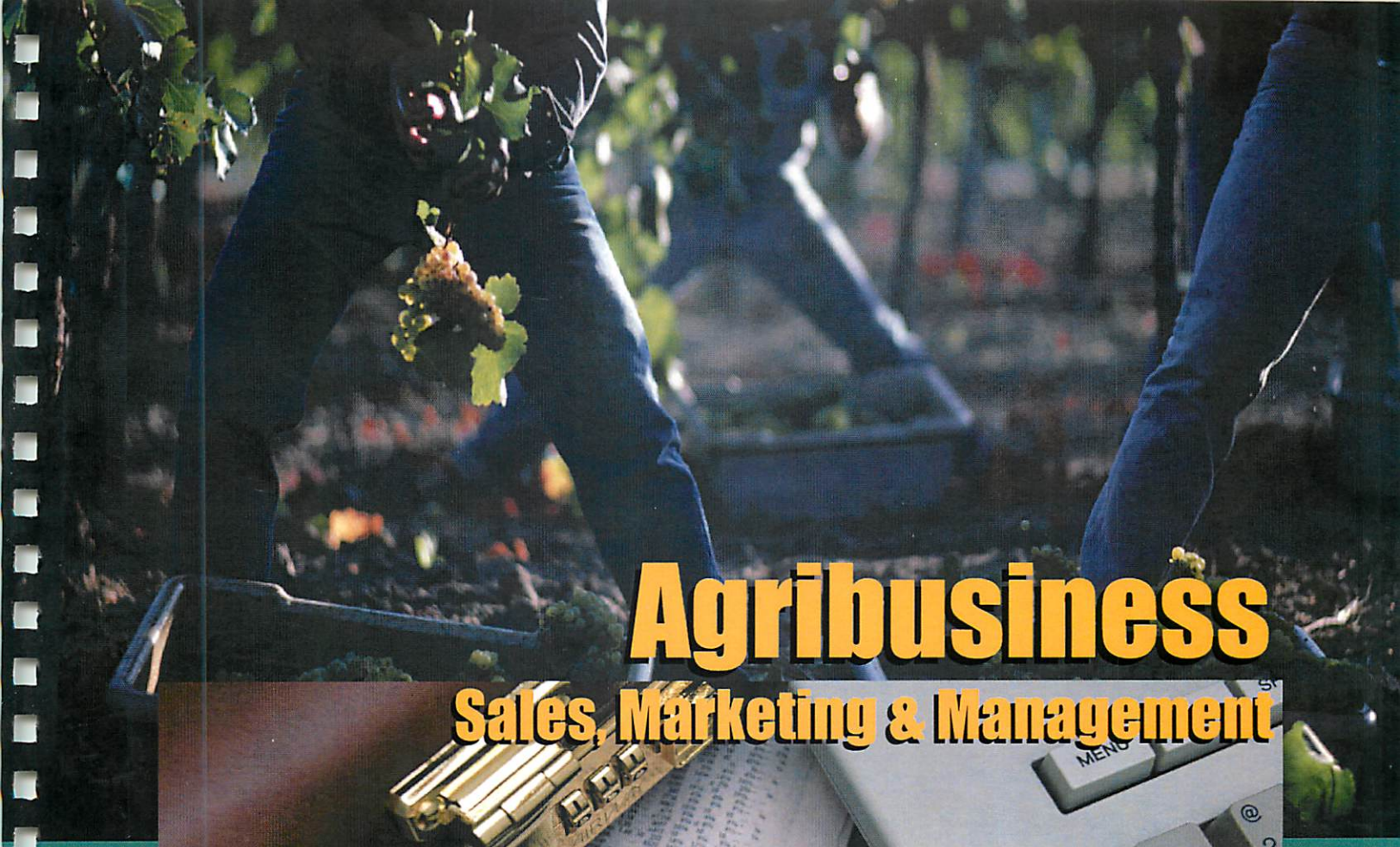
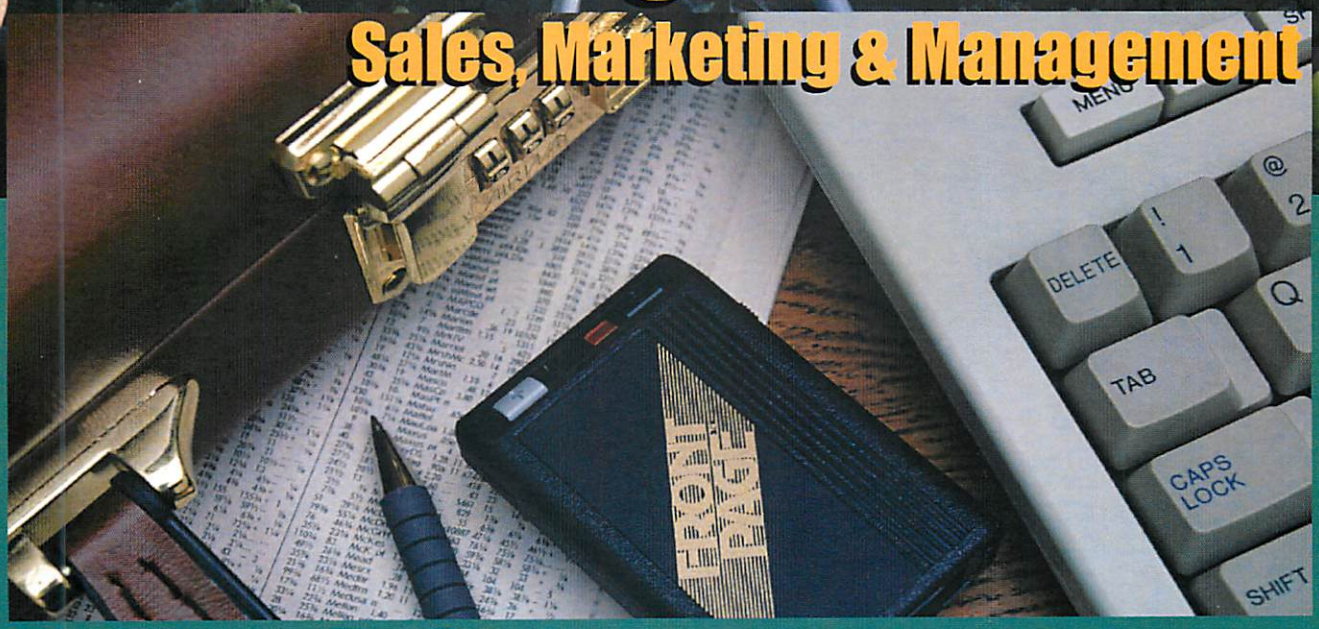


Agribusiness

Sales, Marketing & Management



Student Reference

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AGRIBUSINESS: SALES, MARKETING, AND MANAGEMENT

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FOREWORD

The development of the *Agribusiness Sales, Marketing, and Management* curriculum guide is the result of suggestions by the MVATA Teaching Aids Committee. The Agribusiness Sales, Marketing, and Management Advisory Committee suggested the topics to be included and reviewed the materials.

This curriculum contains nine units. Topics include agriculture as an industry, economic principles in agribusiness, financial management, personal development, communication skills, preparing for a sale, making a sale, promotional tools, and entrepreneurship. An instructor guide can be purchased separately.

During the summer of 1981, the Missouri State Board of Education formally adopted the concept of "Instructional Management Systems" (IMS) as a priority for the 1981-82 school year. The Missouri Commissioner of Education described the IMS concept as a practical way of "organizing for excellence" in education. To meet the demand for greater productivity and accountability, the director of Vocational Education applied the elements of IMS to form the Vocational Instructional Management System (VIMS). The VIMS process provides a framework to use in planning and organizing to assure excellence in Missouri's vocational education system by focusing greater attention on the management of teaching and learning.

The instructor's guide to accompany this student reference incorporates the needed component parts to aid agriculture teachers in the implementation of VIMS.

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AGRIBUSINESS SALES, MARKETING, AND MANAGEMENT

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Lesson 1:
Agriculture Today

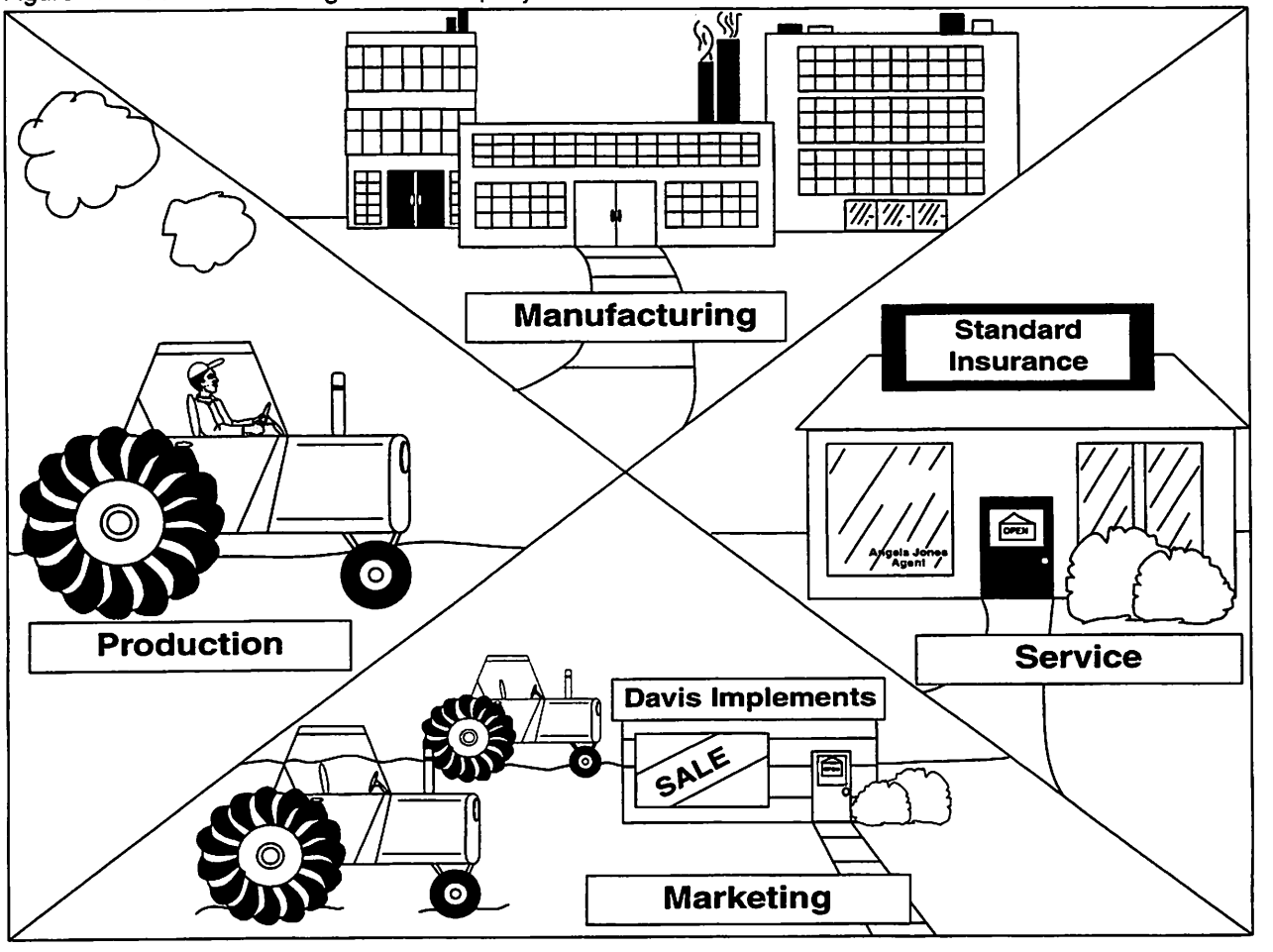
Agriculture is an industry critical to the United States. The improved technology used in agricultural production has enabled the producers of food and fiber to produce more and better products with the labor of fewer people. Production is a very important part of agriculture, but today's agricultural industry encompasses much more. It consists of thousands of agricultural businesses and millions of employees who process, transport, and sell food and fiber products. It also consists of businesses that supply producers with machinery, seeds, fertilizer, supplies, and the finances necessary for the production of agricultural goods. The U.S. agricultural industry is a diverse industry that plays a vital role in the economies of the United States and the world.

Sectors of the Agricultural Industry

The different sectors of the agricultural industry are production, manufacturing, service, and marketing (see Figure 1.1). The production sector of agriculture in the United States is very diversified, including the production of food, fibers, and specialized agricultural products. The manufacturing sector makes the inputs necessary for the production of agricultural goods and processes those goods for sale to the consumer. The service sector provides financing, service, or support to the production sector to enable it to produce. The marketing sector transports and sells the outputs of the manufacturing sector to producers and the outputs of the production sector in domestic and international markets. Together the various sectors form the world's largest source of agricultural products.

The manufacturing, service, and marketing sectors of the agricultural industry support the activities of

Figure 1.1 - Sectors of the Agricultural Industry



the production sector. For example, producers rely on businesses in the manufacturing sector to make such things as fertilizer and chemicals, feed, and machinery that are needed for production; producers may belong to this sector if they supply feed and breeding stock directly to other producers. The manufacturing sector also includes processing plants that transform raw agricultural goods into foodstuffs and textiles for consumers. In the service sector, credit agencies provide financial support for production, while insurance companies protect producers against losses. Federal and state government agencies are also a part of the service sector. They provide price supports, conservation and planning services, and information on agricultural research to producers. The marketing sector includes businesses that transport raw and processed agricultural goods to wholesalers and retailers who sell them to other businesses or to consumers, as well as businesses engaged in the transport and sale of the goods made by the manufacturing sector for agricultural production.

Agriculture and the U.S. Economy

The United States has an abundance of agricultural resources and leads the world in agricultural production, producing enough for both domestic consumption and export. The agricultural industry is the largest industry in the United States. It plays a very important role in the U.S. economy.

The agricultural industry generates a great deal of revenue. In 1990, agricultural production contributed over 71 billion dollars to the total gross national product (GNP) of the United States, while agricultural food processing alone added 83 billion dollars. That same year, agricultural manufacturing, transportation, wholesaling, and retailing combined contributed over 320 billion dollars to the GNP. The international trade in agricultural products is also important, with over 30 billion dollars worth of products being exported each year. Over 20 percent of net agricultural production income in the United States in 1990 came from exports. All the agricultural producers and agribusinesses in the agricultural industry together generated over 700 billion dollars, which is equal to 18 percent of the gross national product of the United States.

In order to produce this revenue, the agricultural industry employs a large number of people, more than any other industry in the United States. In 1990, the agricultural industry employed around 20 million people, which was equal to 18 percent of the total national employment. The exportation of agricultural products alone has created one million jobs for American workers.

The size of the agriculture industry is due in part to improved technology and specialization, which has helped the United States to produce, process, market, and distribute a large selection of quality products at lower prices than any other nation in the world. Many citizens of other countries spend a much larger portion of their income on food. In 1990, consumers in the Philippines spent an average of 52 percent of their income on food, while consumers in Korea spent 36 percent of their income, and consumers in West Germany and Sweden spent over 18 percent of their income on food. In comparison, the average family in the United States spent only 11 percent of its total income on food.

The international market for U.S. agricultural products has also had an effect on the economy of the country. The volume of international trade has contributed to the large size of the agricultural industry in the United States.

In addition to the revenue it generates and the jobs it creates, the international trade in agricultural products has had a number of other benefits. The expanding market caused by international trade creates a greater demand for U.S. agricultural products, so producers get better prices for their goods. Trade and competition have also guided producers in the United States to put precious resources to their best use. The production sector thus works closer to capacity, increasing efficiency, which results in lower prices for the consumer. In addition, agricultural exports allow the United States to establish trade balances and import from other countries food products that are unavailable from U.S. producers. Trade thus increases the variety and lowers the price of these foods for consumers. Trade balances affected by agricultural exports also influence the volume of non-food products imported from other countries.

U.S. Agriculture and the International Economy

The United States agricultural industry has become a source of not only domestic but also international economic growth. The United States agricultural industry plays an important role in international markets. It has become a source of food and fiber products for the world, with many countries relying on the U.S. agricultural industry as a source of food.

Agricultural importing and exporting also allows nations to rely on each other for products they want and need but may not be able to produce, helping to increase the standard of living throughout the world.

Expanding markets through international trade improves the use of resources for agricultural production and increases economic output in other countries as well as the United States. For example, bananas could be grown in the continental United States. To grow them so far north, producers would have to build special greenhouses. Importing bananas from the countries in Central America that specialize in their production is a much more efficient use of resources, since the costs of producing bananas in Central America are not as great as they would be in the United States. Each nation is therefore able to devote its resources to what it produces well, and the economies of all the nations involved benefit from the trade of agricultural products.

The U.S. agricultural industry also benefits other industries in the countries engaged in trade with the United States. U.S. agricultural producers, processors, manufacturers, and distributors buy machinery, equipment, and supplies from international markets in order to produce, process, and distribute agricultural products. The agricultural industry also relies heavily on the importation of petroleum products for operating machinery and equipment.

U.S. agricultural trade in international markets also plays an important part in international diplomacy and foreign relations. Countries that rely on each other for agricultural trade will generally have better relations. Good international relations help to stabilize the world economy, allowing all nations to profit.

Summary

The U.S. agricultural industry involves much more than just production. It includes thousands of agribusinesses that support and benefit from the production of food and fibers. The agricultural industry has a significant impact on the U.S. economy and is a major source of agricultural food and fiber products for the world. The international trade in U.S. agricultural products improves the allocation of resources worldwide and has increased the standard of living for people throughout the world.

Credits

Kohls, R. L. *Marketing of Agricultural Products.* New York: Macmillan Publishing Company, 1990.

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United States Department of Agriculture. *Americans in Agriculture.* Washington, D.C.: Government Printing Office, 1990.

Lesson 2:
Opportunities in Agribusiness Sales, Marketing, and Management

Agriculture has changed dramatically over the past 200 years, from a time when most people were involved in agricultural production to one in which relatively few producers provide food for many people. Improvements in technology continue to allow agricultural producers to produce more on less land, while production requires fewer and fewer people. However, the agricultural industry today involves much more than production. It consists of thousands of agribusinesses that support production by supplying the inputs for production and then processing and marketing the outputs. While agricultural production is employing fewer people, other agribusinesses are beginning a new era of growth. The changes in production have caused major restructuring and a growing need for trained employees in many sectors of agribusiness. The U.S. agricultural industry offers an abundance of choices to those people interested in careers in agriculture.

The History of Agricultural Employment

In the late 1700s and early 1800s, agriculture was very different from today. Nine out of every ten working people worked on a farm. Technology was primitive, with farmers producing crops with some of the same tools that had been used for hundreds of years. Many agricultural producers were involved in subsistence farming, in which farms were self-sustaining units for growing crops and raising livestock primarily for the farm families' needs. Clothing and most of the farm tools were homemade. Little trading of agricultural goods took place because farm families needed much of what they produced to survive.

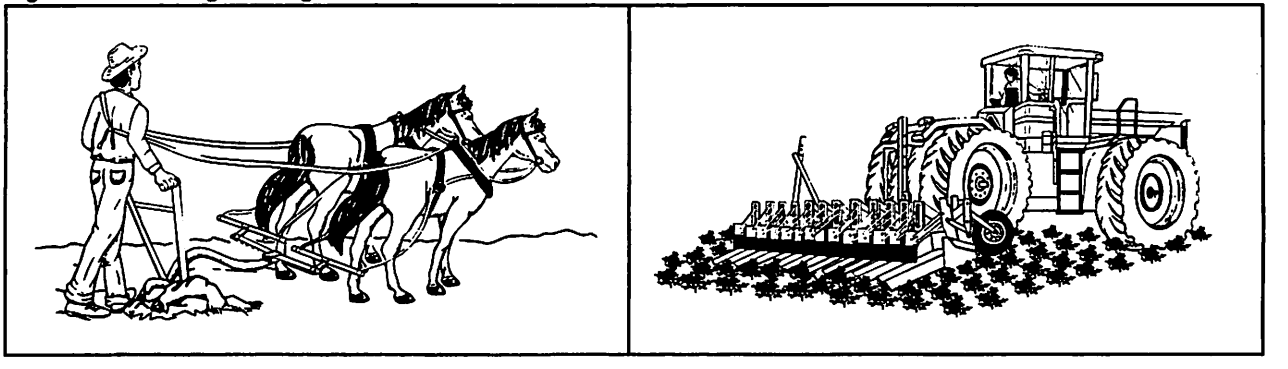
Farm families did carry out limited trading to obtain products that they could not produce. Agribusiness developed from farmers trading excess crops and livestock for such things as salt and sugar. This small amount of agricultural trading provided the basis for what is now the largest agricultural industry in the world.

As the nineteenth century progressed, more advanced methods of farming and improved agricultural technology were developed. For example, new tillage methods made it possible to put more land into production, increasing yields. The use of standardized, manufactured farm tools also increased agricultural yields. Agricultural production took a big leap forward in 1834 when Cyrus McCormick patented and began producing the McCormick reaper. John Deere made his first steel plow out of a circular saw in 1837. Soon John Deere and other companies were manufacturing steel plows. Although these early farm implements seem primitive today, their invention made it possible for many farmers to produce more than they needed for survival.

By the late nineteenth century, the foundation of the modern agricultural industry was in place. With the increased production made possible by new methods and more advanced technology, farmers could feed the growing population of the United States, which was swelling due to large-scale immigration. But, now farmers had to rely on manufacturers and suppliers for inputs for production and on other agribusinesses to process and sell their goods.

The era of the subsistence farmer was almost over by the beginning of the twentieth century. Technology and specialization in production were spreading at a rapid pace, allowing agricultural producers to produce more than ever before and use fewer people to do it. The invention of the

Figure 2.1 - Changes in Agriculture



steam tractor meant that land that had supplied feed for the horses used in production became available for agricultural production. Specialization became a major factor in production as individual producers began to concentrate on producing just a few crops or a particular type of livestock. Agricultural production took another step forward when Ford began marketing the first mass-produced gasoline tractor in 1917. Petroleum products then began to be a major input for the production of agricultural goods.

By mid-century, producers had begun to realize greater benefits from increased agricultural production. In 1947, net income from production climbed to 15.5 billion dollars. This increase in production caused producers to rely on agribusinesses more than ever before, making them a major part of the agricultural industry.

Between 1950 and 1975, U.S. agriculture grew even more, with the United States producing more agricultural goods than any other country in the world. During this period, output from agricultural production increased by 52 percent, with 60 percent fewer hours being used in production. Training future agricultural producers and agribusiness workers to sustain this productivity began to be seen as important for the future of agriculture, so the National FFA Center in Alexandria, Virginia, was dedicated on July 24, 1959. By 1975, the average U.S. producer was feeding 53 people, and only 4 percent of the labor force was involved in agricultural production, compared to 20 percent in 1935 and 90 percent in 1776.

Today the U.S. agricultural industry is a diverse industry consisting of agricultural producers and thousands of agribusinesses and their employees. Two percent of the U.S. population, or 4.8 million people, work in agricultural production. However, more than 15 million people work in agribusinesses in the United States to support that production.

Future Trends for Employment in Agriculture

The 1990s have seen the beginning of another new era for the agricultural industry with even more changes in the production sector. By the year 2000, fewer than 50,000 producers are expected to produce three-fourths of the total agricultural output in the United States. While production is being concentrated in fewer production units, and the overall number of producers is decreasing, the need for trained employees for corporate farms has increased.

Accompanying this shift away from production, changes in the agricultural industry have created a need for increasing numbers of trained employees in manufacturing, processing, and marketing. The demand for workers who support production is greater than ever before. For example, several sectors of the agricultural industry will require employees trained in computer monitoring and control systems. Individuals trained in the management and monitoring of pesticides, groundwater contamination, disposal of animal waste, and many other ecological concerns will be necessary to satisfy the growing concern for a safe and healthy environment. With the changing desires and needs of consumers, employees who have a background in nutrition and food science will be needed to address health issues in the production of food. The change from a production-driven to a highly competitive, customer-driven, and global agribusiness marketplace will continue to create exciting new career opportunities.

Career Opportunities in Agribusiness Sales, Marketing, and Management

Many exciting career opportunities are available in agribusiness sales, marketing, and management. When choosing a career, the first thing to decide is what careers are of most interest. Research into those careers will allow an individual to find out important information about how to reach his or her personal goals. Information on a position's educational requirements, and where to obtain an education, salary, location, availability, and responsibilities will be necessary to decide whether to pursue a particular career.

Agricultural sales careers are a vital component of the agricultural industry. In almost every agribusiness, sales generate income, and without adequate sales the agribusiness will fail. Many different sales positions are available in the agricultural industry. The outlook for employment opportunities is good in retail and wholesale sales, which includes the sale of seeds, fertilizer, pesticides and herbicides, equipment and machinery, and animal medicines. Sales representatives may work at a particular location, such as a farm equipment dealership, or they may travel to cover a network of customers spread over a sales territory. Education and skill requirements vary, with unskilled positions open to individuals with

high school diplomas and other positions requiring university degrees and a great deal of technical knowledge about the product being sold. Entry-level careers in sales, retail or wholesale, may offer the training necessary to obtain positions requiring more technological and professional sales knowledge. Most retail sales employees receive salaries, while those selling wholesale receive commissions or salaries and commissions. A career in sales requires an outgoing personality, initiative, persistence, good communication skills, and a willingness to learn about the product or service being sold to become a better salesperson.

Opportunities for people prepared for careers in agricultural management will increase in coming years. The USDA reported in 1990 that there would be a 10 percent shortage of college graduates in food and agricultural sciences annually through the 1990s. The agricultural industry requires graduates in these areas to fill management positions. Agricultural management positions are available in many businesses, including farm equipment factories, feedlots, corporate farms, and businesses involved in wholesale or retail sales. Many careers in management require college degrees or technical education beyond high school and a varied amount of experience in the selected field. Entry-level positions may offer chances for promotion into management careers with on-the-job training and experience. Besides education or training and experience, careers in agricultural management require the ability to direct, train, and work with people.

More detailed descriptions of some job positions in agribusiness sales, marketing, and management are provided below.

- Retail sales manager - Managers of retail businesses need both interpersonal and business skills. They are responsible for overseeing purchasing, advertising, store layout, finances, price maintenance, store computer systems, personnel, employee and customer relations, employee and management training, and safety and security. They need good business management, communication, and public relations skills.

- Retail salesperson - Retail sales positions may involve a variety of tasks, including customer service, cash register operation, counter and display maintenance, computer price maintenance, and direct selling to customers. Many retail salespersons deal directly with people, making communication and sales skills an important asset.

- Wholesale sales manager - Wholesale businesses obtain goods from manufacturers or producers and sell them to retailers, producers, or other wholesalers. Wholesale sales managers may be responsible for purchasing goods, controlling inventory, and warehousing the products they resell. They also oversee the sales staff. Many managers are responsible for advertising and promotional campaigns, personnel, employee training, and customers and employee relations. They need good business management and communication skills.

- Wholesale salesperson - A wholesale salesperson is responsible for selling products obtained from manufacturers by a wholesale business. Job responsibilities include making sales and taking purchase orders, checking customers' inventories, providing and maintaining displays, and returning outdated or excess inventory from the customer. Sales, communication, and inventory management skills are important for a job in wholesale sales.

- Personnel manager - Personnel managers are also called human resource managers. They generally handle employee matters, which often includes the hiring and training of new employees and overseeing employee benefits. They also conduct interviews and may be involved in employee evaluations. Personnel managers need good communication skills and knowledge of both local and federal employment and benefit laws.

- Plant manager - Managers involved in manufacturing or processing goods may need a variety of both interpersonal and technical skills. An industrial or manufacturer manager must have the technical knowledge to produce the product. Manufacturing or industrial managers may be responsible for overseeing product quality, supplies of raw materials, production schedules, maintenance of equipment, and supervision and training of workers.

- Commodities trader - Cash commodities and futures contracts are traded in commodity markets. A commodities trader must understand the economic factors affecting U.S.

farm commodities in a global market. Commodities traders buy and sell futures contracts and options. They may also advise producers and speculators who want to reduce their price risk. A commodities trader needs training in business and economics. A person entering this field must be able to work under very stressful conditions.

- Corporate farm manager - As corporate farms become more common, people will be needed to manage them. Responsibilities may include supervising feed and feeder livestock purchases, overseeing employees and their training, and overseeing sales and other operations of a production facility. People wishing to enter this field need a strong background in agribusiness management, animal science, and strong communication and problem-solving skills.

International Career Opportunities

In addition to the careers listed above, international career opportunities are growing as the United States imports and exports more agricultural products each year. Many U.S. sales, marketing, processing, and manufacturing companies are involved in international markets. Job opportunities for individuals interested in careers connected to the international agricultural trade will continue to increase in the future.

Among the many new and exciting international sales, marketing, and management areas are agricultural export sales, international marketing, agribusiness management, distribution systems, and international product development and packaging. Most of the positions in these areas require specialized education and training. Many careers in the international market require an educational background that includes the study of a foreign language along with international finance, international trade, international law, or marketing. Entry-level positions are also becoming available that allow individuals with degrees in agriculture to obtain training for other positions in the international market.

One area in which career opportunities are growing is export sales, since more commodities are being exported to other countries as the production of agricultural goods increases. A person entering this field might work directly for a processor or manufacturer of agricultural goods as a salesperson. He or she might also work at an export brokerage firm. Education and training needed for a career in exports include foreign language and customs, international economics, international finance, agribusiness management, and marketing.

Summary

Agricultural production in the United States has changed dramatically over the past 200 years. Changes are still going on, and the U.S. agricultural industry is now at the beginning of a new era. In agriculture, more is being produced each year with fewer people. The changes in production have been accompanied by the creation of new employment opportunities in the thousands of agribusinesses that support production.

Credits

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Lesson 1:
Supply and Demand

Cindy is a cattle buyer from a large midwestern feedlot. Her job is to travel to different auctions in the area and buy certain types of cattle depending on the feedlot's need. How does she know what is a fair price? Why does the price change so much from week to week? Are there things to consider when trying to predict next month's price? She is buying cattle all year long. Therefore, she needs to be able to plan ahead as well as meet the feedlot's present needs.

Demand and Quantity Demanded

Demand for an agricultural commodity like cattle, hogs, or grain is the amount buyers are willing and able to purchase at different prices at a given time and place. Demand is the first component of price. Many people may be willing to buy a new car now, but if they are not able to, they have no effect on demand.

Quantity demanded is how much buyers are willing and able to buy at each specific price. As the price changes, the quantity demanded will change.

Supply and Quantity Supplied

Supply is the amount of product or commodity producers are willing and able to provide at different prices at a given time and place. Supply is the second component of price. Buyers may be very willing and able to buy a product (demand), but if there is a limited supply, the demand may not be met immediately.

Quantity supplied is how much suppliers are willing and able to provide at each specific price. As the price changes, the quantity supplied will change.

Determining Price

Price results from the interaction of the forces of supply and demand. If demand increases without a change in supply, price will go up; if demand decreases, price will fall. If supply increases without a change in demand, price will drop, and if supply decreases without demand changing, price will rise. How does this affect the price of cattle? Consider one step at a time.

If there was a severe drought in a cattle-producing area, what might happen? The price of feed would most likely increase as cattle producers started buying more feed, causing less to be available. If the feed became too high-priced or unavailable, producers would start selling their cattle sooner. Then more cattle would be on the market than the feedlots were willing to buy. If one group tried to sell and the other group was not willing to buy, the price would drop until someone became willing to buy. In this case, an increase in supply would have occurred with no change in demand.

What happens if there is an increase in demand? Cindy's feedlot just sold several tons of meat to Japan to be delivered in a few months. Her company now has a greater need for cattle. She may have to pay more to get the cattle because she is competing with other buyers who also have to satisfy their customers. This may cause the buyers to pay more. An increase in demand without a change in supply will cause an increase in price.

These are just two examples of factors affecting supply and demand. Every day events around the world affect supply and demand at the same time. This interaction determines price.

Law of Demand

The Law of Demand states that when the price of a product increases with no change in factors other than price, less of the product will be purchased. Lower prices mean that more of a product will be purchased. High prices thus result in a lower quantity demanded, and lower prices increase the quantity demanded. The Law of Demand can be depicted by a demand schedule and illustrated by a demand curve.

A demand schedule is a set of prices and the corresponding quantities of an item that would be purchased at each price at a given time and place.

Table 5.1 - Demand Schedule for Hamburger

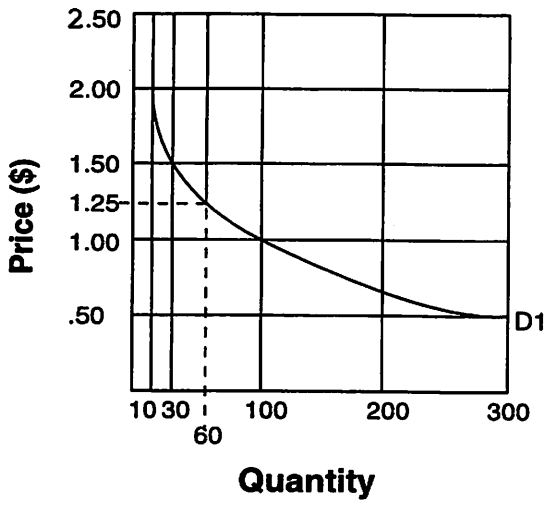
Price/Pound	Pounds Bought
$2.00	10
$1.50	30
$1.00	100
$.50	300

If hamburger were offered for sale at each of the prices listed in Table 1.1, Jerry would be willing to purchase the number of pounds of hamburger that correspond with each price level. This would be his demand schedule for hamburger.

If hamburger were being sold for $1.00 per pound, Jerry would be willing to purchase 100 pounds. However, if the price increased to $1.50 per pound, the quantity of hamburger demanded by Jerry would be reduced to 30 pounds.

The demand schedule can be plotted on a graph as illustrated in Figure 1.1. By plotting the quantity of hamburger demanded by Jerry at each price level and connecting those points in a smooth line, a demand curve can be produced. The demand curve is simply a graphic illustration of a demand schedule. Each point along the demand curve can be used to estimate the quantity of hamburger that Jerry would purchase at each price level. For example, if the price of hamburger were $1.25 per pound, Jerry would purchase 60 pounds of hamburger.

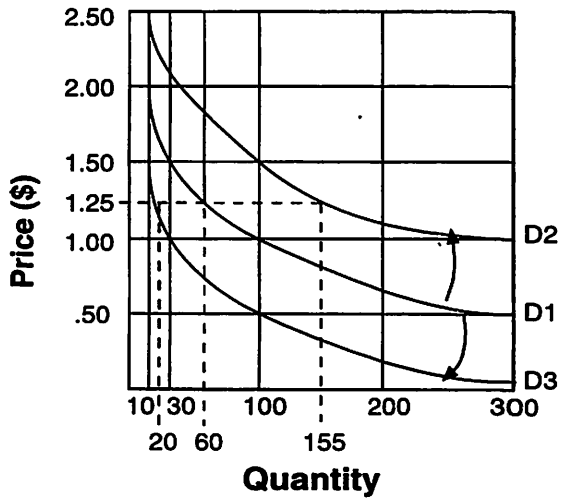
Figure 1.1 - Demand Curve



Demand Shifters

When the prices of goods and services change, the quantities demanded change along demand curves. However, the "demand shifters" described below will cause an entire demand curve to shift in one direction or another (see Figure 1.2). In the case of an increase in demand, the quantities demanded at each price level will increase. Then the entire demand curve will shift upward and to the right (D_2). A decrease in demand would be reflected by a demand curve that shifts downward and to the left (D_3).

Figure 1.2 - Shifts in the Demand Curve



Consumer income - With a change in income per capita, or average income per person, a change in demand is bound to occur. If people have more money to spend, they will usually be more willing to buy an item. With several people buying more of a limited number of the same item, the demand will increase. Because it increases consumer income, inflation will shift the demand curve to the right.

Population - As the number of people trying to buy the same item increases, the demand for that item will also increase.

Individual taste - Some consumers will buy a product because it is needed or because it is a "slight" luxury. Others will buy a product because it fits into their lifestyle; it is the "in" thing to have or to serve. The influence of taste is hard to measure and may change relatively quickly. Still, a sense of it can be a useful tool for predicting the success of a new product or determining how valuable a proven product is.

Competing products - If the price of a competing product is much lower than the standard price for an item, eventually consumers will try the competing product. If they stay with the new product, this will lower the demand for the old product. Manufacturers use lower prices as a tool to build demand for their products. They also offer coupons

and advertise taste improvements and superior quality to gain customers.

Consumer expectations - Expectations play a special role as demand shifts. Because it is hard for producers to predict rapid changes in expectations, it can be difficult to always supply exactly what consumers want. Most consumers buy for only a limited amount of time--a few days or a week or two. Very few consumers buy and store products such as food for much longer than that. If consumers expect a price increase, they are much more likely to stock up. If they expect a price decline, they may hold off making larger purchases. If enough people react the same way at the same time, it can have a direct effect on demand and, thus, on price.

Advertising and promotions/salespeople - Advertising and promotions are ways of trying to increase consumers' awareness and desire to have a certain product. Some advertising methods used are television and radio commercials, magazine ads, and billboards. Promotions include such things as free trial samples and related giveaways.

A salesperson can also become a demand shifter by showing customers that they have a need for a particular product or service. A consumer who has been using one product may change to the salesperson's product if the salesperson convinces him or her that the product meets his or her needs better. For example, a salesperson may convince a producer to plant a different brand of seed that will increase yields for that crop, increasing demand.

Using the original demand curve (D_1) pictured in Figure 1.2, Jerry would have purchased 60 pounds of hamburger per year at a price of $1.25 per pound. If beef promotions, advertising, and Jerry's preference for hamburger (i.e., demand shifters) caused his demand for hamburger to shift to D_2, then he would be willing to increase the quantity of hamburger he purchased in a year to 155 pounds.

Other factors could cause a decrease in Jerry's demand for hamburger. If the Food and Drug Administration (FDA) reported that excessive consumption of red meat contributed to heart disease, then Jerry's demand curve for hamburger might shift to D_3. Then, if the price of hamburger remained at $1.25 per pound, Jerry could reduce his purchases to only 20 pounds per year.

Keep in mind that the factors that influence demand are constantly changing. It is difficult to accurately predict the demand for a product. However, an understanding of the concept of demand and factors that influence it is important in business management and the study of economics.

Law of Supply

The Law of Supply states that when the price of a product is lowered with no change in factors other than price, less of the product will be supplied. Conversely, if the price of a product is increased, a larger quantity of the product will be supplied to the market. The Law of Supply can be depicted on a supply schedule or illustrated by a supply curve.

A supply schedule is a listing of the amount of a product that the industry is willing to offer for sale at different prices.

Table 1.2 - Supply Schedule for Hamburger

Price/Pound	Pounds Offered for Sale
$2.00	300
$1.50	100
$1.00	30
$.50	10

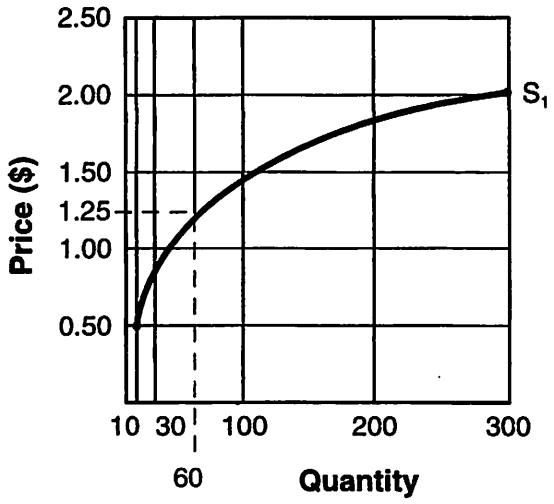
A supply curve is simply a graph illustrating a supply schedule. Notice that the supply curve is plotted in the opposite direction of the demand curve. Similar to a demand curve, a supply curve indicates the quantity of a product that suppliers are willing to provide at various price levels.

Figure 1.3 shows that a supplier would provide 30 pounds of hamburger for sale if the price were $1.00 per pound. If the price were reduced to $.50 per pound, the supplier would only be willing to provide 10 pounds of hamburger. If the price were to increase to $1.50 per pound, the supplier would be willing to increase the quantity supplied to 100 pounds.

Supply Shifters

When the prices of goods and services change, the quantities supplied change along supply curves. However, the "supply shifters" described below will

Figure 1.3 - Supply Curve



cause an entire supply curve to shift in one direction or another (see Figure 1.4). If certain events caused supply to increase, then the supply curve would shift to the right (S_2). At each price level the amount of hamburger each supplier would be willing to provide to the market would increase. A decrease in supply can be illustrated by a supply curve (S_3) that has shifted to the left. The result of a decrease in supply would be that at each price level suppliers would be willing to provide a smaller quantity of hamburger for sale.

Supplier expectations - Suppliers are constantly trying to predict the best strategy for the future. If they expect an increase in price, they will try to increase production.

Natural forces - Nature often causes drastic changes in the supply of agricultural products. Floods can destroy an entire region's crops. Droughts can severely reduce the amount harvested. If natural disasters strike several areas at the same time, the supply curve can shift.

Storage and perishability - These product qualities are also key factors. Currently, a lot of grain is stored at harvest when the price is normally the lowest. After harvest, the price will begin to rise, and some of the stored grain will be sold. This helps maintain price stability. It is much harder to store perishable items, such as fresh fruit and vegetables. Thus, it is much harder to control the supply of perishables, and dramatic price shifts may result.

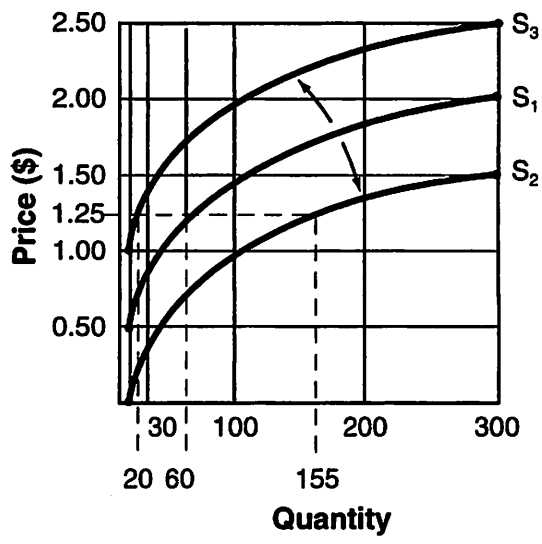
Cost of production - An increase in the cost of production, such as that caused by an increase in the price of an input item, will cause a decrease in the supply of a good. Because it increases the cost of production, inflation shifts the supply curve to the left.

Technology - Another important factor has been advances in technology. Dramatic changes in technique over the past few decades has caused a huge increase in the amount of crops produced from each acre of land.

Government programs - Often the government will develop policies to try to control supply, which, it is hoped, will increase prices of agricultural products.

Using the original supply curve (S_1), Frank would have supplied 60 pounds of hamburger if the price were $1.25 per pound. If a beef shortage occurred in the United States, the supply curve for hamburger would shift to the left (S_3), and Frank would then provide only 20 pounds of hamburger. See Figure 1.4.

Figure 1.4 - Shifts in the Supply Curve



Assume that a new packaging technique extended the shelf life of hamburger. This new technology would shift the supply curve to the right (S_2) and increase the quantity that suppliers were willing to provide the market at each price level. In this example, Frank would be willing to supply 155 pounds of hamburger if the price were $1.25 per pound.

As with demand, remember the factors that influence supply are constantly changing. Understanding the Law of Supply is important in the study of economics and management.

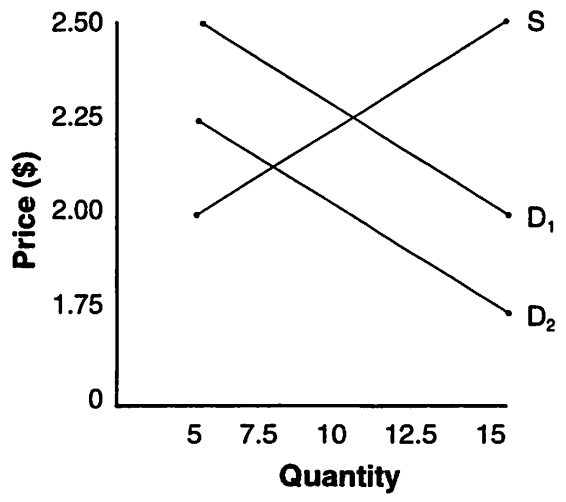
The Equilibrium Point

Supply and demand curves lie in opposite directions. What would happen if these lines were placed on the same graph? Somewhere they would have to cross, and the point at which they did would be the equilibrium point.

At the equilibrium point, a balance exists between the quantity supplied and the quantity demanded. This is how price is determined in the free market. If there is a change in either supply or demand, there will be a new equilibrium point. If the price is too high, the quantity supplied will be greater than the quantity demanded, and a surplus will develop. If the price is too low, a shortage will develop forcing the price to rise to the equilibrium point. In free markets this is how products sell at market-clearing prices; quantity supplied equals quantity demanded.

In Figure 1.5, note that the equilibrium price for D_1 and S is $2.25. At this price, 10 units will be bought. If the price increases to $2.50 without a change in supply or demand, only 5 units will be purchased. If the demand changes to D_2, a new equilibrium point will be reached at 7.5 units.

Figure 1.5 - Equilibrium Price



Goods Demanded by Consumers

Luxury items - These are goods or services that are generally considered nonessential to the survival or well-being of an individual. Driving a fancy sports car or eating steak every day may be enjoyable; however, one will survive without doing so. In good economic times, consumers will spend more on luxury items than they will in hard times.

Necessity items - These are goods or services that are generally considered essential to the survival or well-being of an individual. These items include shelter, food, clothing, and medication.

Elasticity

Elasticity is the measure of how sensitive the market is to changes in price or quantity. Items are elastic to varying degrees, subject to several factors. There are three types of elasticity: inelastic, elastic, and unit elastic.

Inelastic - This is when the change in price is greater than the relative change in quantity. In other words, the price can change drastically, and consumers will still buy nearly the same amount. Items that consumers need for health or well-being tend to be inelastic. An example is insulin for someone who has diabetes.

Elastic - This is when the change in price is less than the relative change in quantity available. With elastic items, a small change in price can have a huge effect on sales. Elastic items tend to be luxury items. A store can often reduce prices by 15 percent and actually make a large profit. Why? Because consumers are willing to respond to a change in price; they are more likely to buy when they feel they are getting a good deal. This will increase quantity sold. The increase in quantity sold offsets the reduced price.

Unit elastic - This is when the change in price is equal to the relative change in quantity available. Unit elasticity only exists under special conditions. If a store has a sale, the reduction in price must be exactly offset by the increase in items sold. If there is an increase in price, the increase must exactly offset the loss due to fewer items sold, or unit elasticity does not apply.

The three types of elasticity are influenced by several factors.

1. Ability of products to substitute for each other
2. Increase or decrease in supply
3. Increase or decrease in demand

4. Income changes in the population that buys the products
5. Price increases or decreases demanded by buyers and sellers

Demand Price Elasticity and Supply Price Elasticity

Price is affected by demand and supply. Elasticity is responsiveness to these factors. After a price change, consumers will change their buying habits. The amount of change is measured by demand price elasticity. The amount suppliers will change their production levels, due to a change or expected change in price, is measured by supply price elasticity.

Demand price elasticity is equal to:

$$\frac{\textit{\% change in quantity demanded}}{\textit{\% change in price}} \quad \textit{or}$$

$$E_d = \frac{(Q_2 - Q_1) \div Q_1}{(P_2 - P_1) \div P_1}$$

E_d = demand price elasticity
Q_1 = original amount demanded
Q_2 = new amount demanded
P_1 = original price charged
P_2 = new price charged

For example, the price of a movie ticket is $4, and the theater decides to lower it to $3. The attendance increases from an average of 20 people per movie to 30 people per movie. Was lowering the price a good management decision? The numbers go into the formula as follows:

$$E_d = \frac{(Q_2 - Q_1) \div Q_1}{(P_2 - P_1) \div P_1} = \frac{(30 - 20) \div 20}{(3 - 4) \div 4} = \frac{10 \div 20}{-1 \div 4}$$

$$= \frac{10}{20} \times \frac{4}{-1} = \frac{40}{-20} = \frac{4}{-2} = -2.0*$$

*Demand price elasticities are always negative.

What does elasticity of 2.0 mean? If the absolute value (or the nonnegative value) of the number is larger than one, it means that there is an elastic demand and total revenue will increase with a cut in price as more people come. If the number is less than one, demand is inelastic, and total revenue will decrease because there will not be enough people to compensate for the difference in price. If it is equal to one, it would be a state of unit elasticity, and a change in price would be exactly offset with no change in total revenue. The supplier can use the same formula for determining the elasticity of supply.

$$\frac{\textit{\% change in quantity supplied}}{\textit{\% change in price}} \quad \textit{or}$$

$$E_s = \frac{(Q_2 - Q_1) \div Q_1}{(P_2 - P_1) \div P_1}$$

E_s = supply price elasticity
Q_1 = original supply
Q_2 = new supply
P_1 = original price
P_2 = new price

In an example, the Jay County elevator buys corn from local producers and resells it as livestock feed. During January, this elevator paid $2.10 per bushel. At this price, producers have been willing to supply 7,200 bushels per day, but this is not enough to meet demand. Therefore, the elevator decides to raise the price to $2.20 per bushel. Producers are now willing to supply 8,500 bushels per day. What is the elasticity of supply?

$$E_s = \frac{(Q_2 - Q_1) \div Q_1}{(P_2 - P_1) \div P_1} = \frac{(8{,}500 - 7{,}200) \div 7{,}200}{(2.20 - 2.10) \div 2.10}$$

$$= \frac{1{,}300 \div 7{,}200}{.10 \div 2.10} = \frac{1{,}300}{7{,}200} \times \frac{2.10}{.10} = 3.79$$

Because 3.79 is greater than one, the supply of corn from storage is elastic. A small change in price will result in a larger change in quantity supplied.

Importance of Demand and Supply Price Elasticity

Demand price elasticity will allow an estimate to be made of how much the quantity demanded will change when the price goes up or down. The supply price elasticity will help in estimating how much production will change as price goes up and down. These two tools show how demand and supply are interacting and trying to reach a new equilibrium point. By using these tools, an agribusiness manager can predict whether a business decision will be profitable.

agribusiness manager can predict whether a business decision will be profitable.

Summary

Supply and demand are the two key concepts in determining how much is produced, what the price is, and how much is stored. Understanding the principles of supply and demand is essential to understanding how the marketplace works. Some items have different reactions to supply and demand. These reactions are measured as elasticity. Luxury goods and necessity goods have different types of elasticity. There are several demand and supply shifters.

Credits

Bacon, Kevin, Nick Boren, and Van Kirkwood. *Agricultural Management and Economics (Student Reference).* University of Missouri-Columbia: Instructional Materials Laboratory, 1988.

Lesson 2:
The Principle of Diminishing Returns

Michelle has just been promoted to the position of supervisor for a large chemical spraying company. The company is expanding, and she has been given a new area of the state as her district. She has been covering the district with only one employee while establishing more customers, but business has been going well, and now she and the employee are having trouble keeping up. She knows she will need to hire more employees and will need to do some calculating to determine how many.

Total Product, Marginal Product, and Average Product

Total product - Total product (TP) is the total output or yield. Michelle must first determine total product to decide how many additional employees she will need. Total product, in Michelle's case, is the number of spraying jobs done each day. With only one worker, Michelle can complete four jobs per day.

Marginal product - Marginal product (MP) is the change in output resulting from each additional unit of input. For Michelle, marginal product would be the change in the number of spraying jobs completed each day (output) because of each additional worker (unit of input) hired.

Average product - Average product (AP) is the total output produced divided by the total number of units of input. In this case, it would be the number of jobs done each day divided by the number of workers.

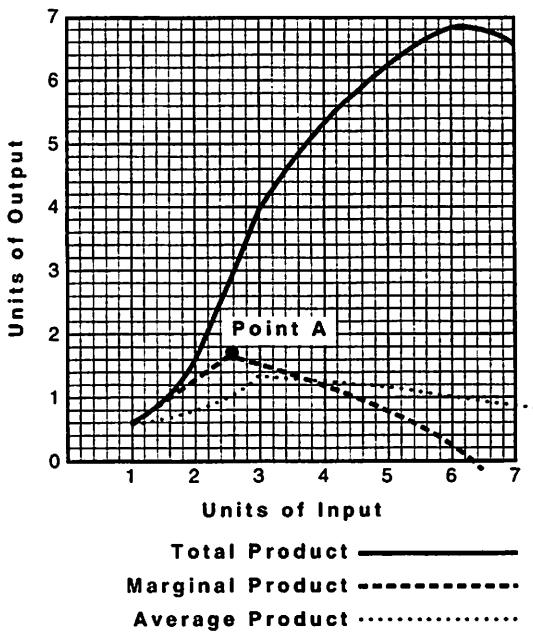
The Relationship of TP, MP, and AP

The relationship between TP, MP, and AP can be illustrated on a graph, as in Figure 2.1. As total product increases at an increasing rate, marginal product and average product also increase, but marginal product increases at a faster rate than average product. While total product continues to increase, first marginal product, then average product begin to decrease. At the point where the lines representing MP and AP cross, the TP begins to increase at a decreasing rate. When marginal product equals zero, and average product is still positive, total product is at its maximum level. When MP becomes negative, TP begins to decrease.

Diminishing Physical Returns

The principle of diminishing physical returns states that at some point in time, marginal product decreases with each additional unit of input, because as additional units are added, they become less efficient. That point in time is represented on the graph in Figure 2.1 as Point A. Michelle knows that she has only a limited amount of equipment and is serving a limited area. She understands that her new district can only become so big. Because of these limits, her total product for her district will also reach a limit. She wants to do a good job, but she knows if she hires too many workers, they will add less to the total product. Her concern is how many workers she should hire.

Figure 2.1 - Relationship of TP, MP, and AP



After hiring one additional worker, her district can do seven jobs per day. The additional worker gives a marginal input of one; marginal input is the difference between the initial amount and the next level of input. The marginal product for her district is the three additional jobs completed. The average product for her district is the total amount of work divided by the number of workers (7 ÷ 2 = 3.5).

What happens when she hires the second additional worker and finishes nine jobs per day? Notice in Table 2.1 that the marginal product is decreasing even though the total product is still rising. As more inputs are added, marginal product will continue to

decrease. Michelle's goal is to use these numbers to determine the best level of operation for her district.

Table 2.1 - Calculating Diminishing Physical Returns

Workers	Jobs/Day (TP)	MI	MP	AP
1	4	XX	XX	4
2	7	1	3	3.5
3	9	1	2	3

Diminishing Economic Returns

The principle of diminishing economic returns states that beyond some point, marginal economic returns, like marginal product, decrease with each additional unit of input. Michelle wants to expand her territory, but she also wants to increase her company's profit. While the number of jobs completed may be increasing, the additional amount of work accomplished by each employee is decreasing because of the limitations of equipment and district size. As her territory nears its most profitable level of operation, the economic returns, or profit, will also decrease as additional levels of input are added.

To determine the most profitable level of operation for Michelle's district, a few more columns must be added to the table.

Total revenue - Total revenue (TR) is the total income from all the jobs. Each job costs the customer $35.

Total cost - Total cost (TC) is the cost of each employee. (Other business costs will be ignored). Each employee receives $80 per day. The cost per day is the number of employees multiplied by $80.

Marginal revenue product - Marginal revenue product (MRP) is the increase in income created by adding an additional input by hiring another employee. In the example, the inputs are increasing at a constant rate, while the outputs are variable.

Marginal input cost - Marginal input cost (MIC) is the increase in total cost with each additional unit of input. In the example, the MIC is the $80 cost divided by the marginal input.

Michelle should continue to hire workers as long as MRP is greater than or equal to MIC (MRP ≥ MIC).

Table 2.2 shows that Michelle should only hire one additional employee because the marginal revenue product is less than the marginal input cost when the second additional worker is hired. Michelle now knows that with her available equipment and district size she only needs two employees.

All of the concepts described above are very important for persons in any business, including agribusiness. These concepts are used to help owners and managers determine the most profitable level of operation. Michelle, like other managers, can use these concepts to help determine what the production level should be for her district.

Maximum Profit

Maximum profit occurs when the net economic returns are at their greatest point, or MIC = MRP. At that level, if any more input is added, it will cost more than the gain realized. If less inputs are used, then the opportunity to increase earnings is being ignored. In Michelle's case, maximum profit would be reached with one additional employee. Marginal revenue product is less than the marginal input cost if a third employee is hired.

Maximum Production and Maximum Profit

Maximum production is when production is at its highest possible level. Maximum profit occurs when net economic returns are at their highest point, or MIC = MRP. Maximum profit always occurs at a level of production that is lower than maximum production.

Table 2.2 - Calculating Diminishing Economic Returns

Workers	Jobs/Day	MI	TP	MP	AP	TR	TC	MRP	MIC
1	4	XX	4	XX	4	$140	$80	XX	XX
2	7	1	7	3	3.5	$245	$160	105	80
3	9	1	9	2	3	$315	$240	70	80

Summary

In any business, production can be increased by adding inputs of land, labor, capital, and management. However, for the business to operate at its maximum profit potential, its manager must be able to determine when marginal input cost becomes equal to marginal revenue product.

Credits

Bacon, Kevin, Nick Boren, and Van Kirkwood. *Agricultural Management and Economics (Student Reference).* University of Missouri-Columbia: Instructional Materials Laboratory, 1988.

Lesson 3:
Fixed and Variable Costs

Modern transportation offers benefits that were unavailable a century ago, but with these benefits come costs. Most families today have more than one car. Some high school students own cars, and if they do not, they generally are allowed to use one of the family cars. Certain costs are associated with owning or using a car. What has to be paid for when operating a car?

Fixed Costs

Fixed costs are incurred regardless of the level of production or use. They are also referred to as ownership costs or overhead costs. Even owning a car involves paying these types of fixed costs. If a student borrowed money to buy a car, then the payments and car license would be fixed costs. These types of costs have to be paid on a regular basis, no matter how little or how much the car is used.

Types of Fixed Costs

Every business incurs five types of fixed costs. They are referred to as the DIRTI Five. They are explained below, again using a car as an example.

Depreciation - Depreciation is the loss of value each year due to wear, age, or obsolescence. Even a car that is never driven will decline in value because new models come out, with innovative features. Most people prefer newer cars, so older ones lose value.

Interest - The cost of using money is called interest. If an individual borrows money, he or she must pay interest; if he or she puts money in a savings account, the bank pays interest. An opportunity cost is also associated with using capital in business, rather than investing the money in an interest-bearing account.

Repairs and Shelter - Repair and shelter costs are incurred to slow wear caused by weather and time. These costs are different from depreciation, because depreciation costs are related to the original investment. Shelter costs are related to housing and maintenance. For example, if a car is stored in a garage when it is not being used, damage caused by the effects of weather such as a hailstorm can be prevented. Repair and shelter costs will occur regardless of how often the car is used.

Not all repair costs are fixed. Repairs associated with the use of an item are variable costs; however, repairs required even though an item has not been used are fixed costs. Maintenance done to prevent costly breakdowns would be a fixed cost.

Taxes - Property taxes are collected on personal items such as cars each year, regardless of whether they have been used.

Insurance - Insurance is a tool to help manage risk. Risk is the uncertainty owners and managers face in doing business. A company pays a premium for insurance, and the insurance company will reimburse the company if a major loss occurs. The insurance premiums on a car are constant.

Variable Costs

Variable costs change in response to the production level or the amount of use. The more an item is used, the more the total variable costs will be. For example, fuel for a car is a variable cost. Total fuel cost varies considerably, depending on whether one drives 50 or 500 miles per week. Variable costs in an agribusiness include labor, supplies, advertising, gasoline, and utilities.

How Variable Costs Become Fixed

Once an item is bought, its cost becomes fixed. The money is already spent; it cannot be spent somewhere else. Suppose a person is on a long trip and has to pay a high price for gas. If a few miles later that person sees a station where gas is cheaper, he or she cannot take advantage of the lower price. The tank is already full, and the gas has already been purchased. The cost of gasoline has therefore gone from a variable to a fixed cost.

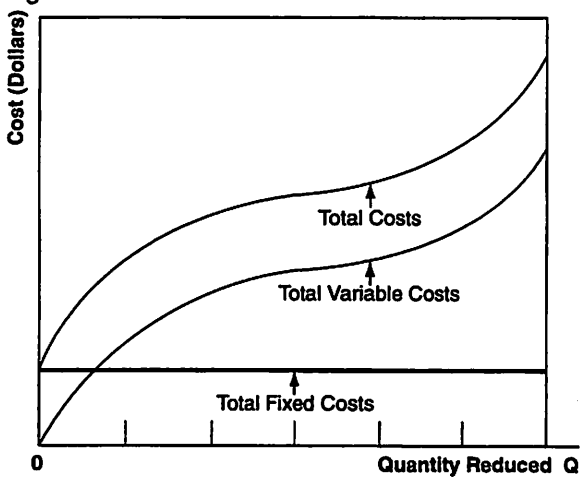
Total Cost

The total cost of producing any product is the sum of the fixed and variable costs. A product can be anything produced and sold or bought and resold. It may also be a service that a business provides.

An agribusiness such as a farm supply store, for example, may have the following total costs. Several fixed costs are involved in starting and running a farm supply store. For one thing, the

owner must take into account the depreciation on the building. He or she will incur the cost of buying or replacing counters and fixtures. Interest must be paid on borrowed money or lost on money that could be invested elsewhere. Weather and time can be quite destructive to buildings, and repairs will have to be made. Property and sales taxes have to be paid. Insurance premiums will probably be due monthly, especially if money is borrowed. If money has not been borrowed, not taking out an insurance policy means risking very high costs later, if the building is damaged or destroyed. In addition to these fixed costs and others, the store will have variable costs, such as utilities, salaries, supplies, advertising, and the many other expenses involved in operating an agribusiness. These variable costs must be added to the fixed costs to determine the total cost.

Figure 3.1 - Total Cost



Total cost is represented in the graph in Figure 3.1. Notice that total fixed costs stay the same at all levels of production. Total variable costs are represented by a curved line because these costs change with different levels of production. Notice also that the distance between the total variable cost curve and the total cost curve is the same at all levels of production. Total cost is equal to variable costs plus fixed costs. Since fixed costs do not change, the distance between the curves is constant.

Average Fixed Cost, Average Variable Cost, and Average Total Cost

In addition to the total fixed cost, total variable cost, and total cost, per-unit costs are also calculated by businesses. Average fixed cost, average variable cost, and average total cost are all per-unit costs.

Average variable cost (AVC) - Average variable cost is the total variable cost (TVC) divided by the quantity (Q). This gives an average per-unit variable cost.

$$AVC = \frac{TVC}{Q}$$

Average fixed cost (AFC) - Average fixed cost is the total fixed cost (TVC) divided by the quantity (Q). It shows the average fixed cost per unit.

$$AFC = \frac{TFC}{Q}$$

Average total cost (ATC) - Average total cost is the total fixed cost (TFC) plus the total variable cost (TVC) divided by the quantity (Q). It gives the average total cost per unit.

$$ATC = \frac{TFC + TVC}{Q} = \frac{TC}{Q}$$

Per-Unit Costs

The concept of per-unit cost can be very helpful in making business decisions. Per-unit costs are used because they reduce values to equal units such as tons, acres, or bushels. The business manager is then able to more easily compare different situations. In general, businesses want a low per-unit cost in relation to the units they are selling.

For example, Dan is the manager of a large feedlot. He is presently buying corn to use in the operation and is paying an average of $2.05 per bushel. His company has the chance to buy 320 acres of land located adjacent to the feedlot that would be ideal for planting corn. Dan has been asked to analyze the fixed and variable costs involved in planting and harvesting corn and determine if it would be feasible for the company to buy the land to supply corn to the feedlot. Dan figures that fixed costs on the land and equipment per year will be $27,200, whether the company plants one acre or all 320 acres. After talking to other producers in the area, Dan decides

that he can anticipate an average of 110 bushels of corn per acre with variable costs of $95.00 per acre.

Dan plugs the figures ($95.00 to plant and harvest one acre or (10 bushels) into the formulas to determine the per-unit costs of planting corn. He calculates the average variable cost:

$$AVC = \frac{TVC}{Q} = \frac{95}{110} = .86$$

The average variable cost would be $0.86 per bushel.

Dan estimates the total fixed cost at $27,200. He begins by calculating the average fixed cost if the company decides to plant all 320 acres ($27,200/320 acres). The total fixed cost per acre is $85.00:

$$AFC = \frac{TFC}{Q} = \frac{85}{110} = .77$$

The average fixed cost is $0.77 per bushel.

If the company planted fewer than 320 acres, the total fixed cost per acre would be higher. For example, total fixed cost for 200 acres ($27,200/200 acres) would be $136.00 per acre. The average fixed cost per bushel would then be $136.00/110 bushels per acre, or $1.24 per bushel.

Finally, Dan figures average total cost for 320 acres:

$$ATC = \frac{(TVC + TFC)}{Q} = \frac{85 + 95}{110} = \frac{180}{110} = 1.64$$

The average total cost is $1.64 per bushel.

Dan now knows that as long as corn prices are higher than $1.64 a bushel, the company will be saving money by buying the 320 acres and planting corn on them. At the present price of $2.05 per bushel, the company will be saving $0.41 per bushel. By looking at the per-unit cost, Dan was able to show the owners of the company how to increase profits by reducing costs.

Short Run and Long Run

The short run is a period during which certain inputs, or resources, are fixed and others are variable. In the short run, only those inputs considered to be variable may be changed. For example, a manager can change the number of workers hired, the amount of gas used, the amount of supplies used, and other variable costs. In order to minimize losses, business should continue in the short run as long as all variable costs are being met.

In the long run, all resources are variable, and there are no fixed costs. The long run encompasses long-range planning for future needs. Should the business expand? Does it need more or less land? What are the equipment and facility needs? These are all questions that can be addressed in the long run. In the long run, returns must exceed total costs for the business to survive.

Summary

When making business decisions, the agribusiness manager should consider two types of costs that make up the total costs of a business. In the short run, costs can be classified as either fixed or variable. Fixed costs include depreciation, interest, repairs and shelter, taxes, and insurance. Variable costs are very important because as long as managers meet these costs, they will continue to operate. In the long run, all costs are variable and will have to be met for the business to succeed. Examining per-unit costs like AVC, AFC, and ATC helps managers when they consider what changes might make a business more profitable.

Credits

Bacon, Kevin, Nick Boren, and Van Kirkwood. *Agricultural Management and Economics (Student Reference).* University of Missouri-Columbia: Instructional Materials Laboratory, 1988.

Lesson 4:
Substitution of Inputs

In the first lesson, the principle of diminishing returns was used to help determine the best level at which to operate an agribusiness. The second lesson dealt with fixed and variable costs and showed that understanding the relationship between these costs is important to any business manager. This lesson explains how to determine the best combination of inputs that can be used in a business without changing the level of production or increasing costs.

Substitution

Substitution is replacing one input with another in an attempt to maximize profit. It is illustrated in Figure 4.1. People have been using substitution throughout history. Animals replaced people for heavy work like plowing and hauling. Many centuries later, tractors and trucks replaced the oxen, horses, and wagons. In both cases, as years went by and time and labor became more critical, the substitutions made work faster and easier.

Substitution may also be used to lower costs, as when cheaper feed ingredients replace costly ones to form a good ration price or machines replace people in certain jobs.

Determining Maximum Profit

A manager wants to organize a business with the best combination of inputs, so that inputs cannot be added to or subtracted from the business without decreasing profit. This condition exists at the best level of input substitution.

Determining maximum profit by substitution is related to the principle of diminishing returns, in which inputs can only be added up to a certain level without decreasing profit.

Methods of Substitution

Constant substitution - Constant substitution is when one resource can be substituted for another at the same rate for each additional unit of input. For example, many swine producers feel that milo can be substituted for corn in a hog ration on a pound-for-pound basis. If this is true, a farmer would want to compare unit prices and use whichever grain is cheapest.

Variable substitution - Variable substitution is when one resource can be substituted for part of another at a different rate for each additional unit of input. For example, a business decides to replace some workers with machines. They predict the following results (Table 4.1).

Figure 4.1 - Substitution

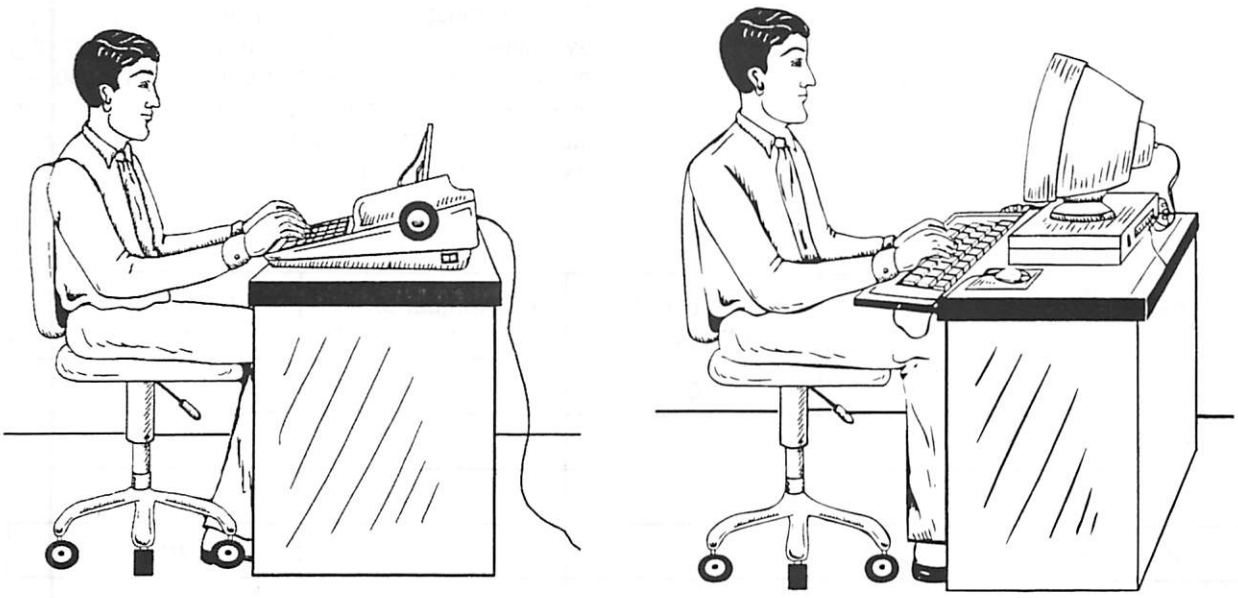


Table 4.1 - Variable Substitution

Number of Workers	Workers Replaced	Number of Machines	Machines Added
25		0	
18	7	1	1
13	5	2	1
10	3	3	1
8	2	4	1

The first machine replaced seven workers, but the second machine only replaced five, and the third machine only replaced three workers. The fourth machine only replaced two workers.

Calculating the Best Rate of Substitution

Calculating the best rate of substitution is a matter of finding out how much may be gained and how much may have to be given up with each level of substitution. The first step is to determine the marginal rate of substitution (MRS) at each level.

$$MRS = \frac{\textit{number of units replaced}}{\textit{number of units added}}$$

Now the business firm can determine its marginal rate of substitution. The marginal rate of substitution for the business in the example above is shown in Table 4.2.

The next step is to determine the price ratio (PR) of the added and replaced inputs. The price ratio is

$$PR = \frac{\textit{price of added unit}}{\textit{price of the replaced unit}}$$

If the cost of a worker is $250 a week and the cost of owning and operating the machine is $1,000 a week, what is the price ratio?

$$PR = \frac{\$1{,}000}{\$250} = 4$$

To determine the best rate of substitution, the marginal rate of substitution (MRS) must be compared to the price ratio (PR). The best rate occurs where the marginal rate of substitution equals the price ratio. This is the most profitable combination of inputs to use.

How many machines should the firm in the example substitute? Compare the marginal rate of substitution in Table 4.2 with the price ratio of 4. The company should only substitute two machines because if they use more, the marginal rate of substitution will be less than the price ratio. MRS should always be greater than or equal to PR ($MRS \geq PR$).

The firm must be sure that it has enough capital available for the purchase and operation of the machines. Forecasts indicate that purchasing the machines will be made possible by the reduction in labor costs for the firm, which amount to more than the cost of the machines.

Table 4.2 - Marginal Rate of Substitution

Number of Workers	Number of Workers Replaced	Number of Machines	Number of Machines Added	Marginal Rate of Substitution
25		0		
18	7	1	1	7/1 = 7
13	5	2	1	5/1 = 5
10	3	3	1	3/1 = 3
8	2	4	1	2/1 = 2

What happens if prices change, causing the price ratio to change? Labor prices and inflation, along with other factors, might cause a change in the price ratio. If that happens, the new price ratio will have to be compared with the marginal rate of substitution to find the new best level of substitution.

Summary

An efficient manager may be able to increase a firm's profits through substitution. The level of substitution is determined by comparing the marginal rate of substitution (MRS) with the price ratio (PR) and substituting when MRS > PR. The best rate of substitution is when MRS = PR.

Credits

Bacon, Kevin, Nick Boren, and Van Kirkwood. *Agricultural Management and Economics (Student Reference).* University of Missouri-Columbia: Instructional Materials Laboratory, 1988.

Lesson 5:
Opportunity Cost

It is Wednesday night, and Kent has made a date with Katie. Unfortunately, Friday night is the only time Katie is available. Kent was supposed to work Friday night at the grocery store from 5 p.m. until 11 p.m. He makes $5 per hour. A friend is willing to work Kent's hours for the money, so he has that part worked out. But Kent now has to add the $30 he is giving up to the other costs of the date, such as gas and his share of the evening's expenses.

Opportunity Cost

Opportunity is the potential for increasing income or the chance for betterment. Cost is the value paid for an item or the amount given up for the use of something. Opportunity cost is the return on the best alternative not selected. In the previous example, Kent had a chance to date Katie; however, to go on the date, he had to not only pay for the date but also give up the opportunity to work and earn money.

Opportunity cost for a business is determined in the same way. A business is often faced with two alternatives for investing its money. A bank may be willing to pay 6 percent interest; a certain stock may pay 9 percent. If the business places its money in the bank, the opportunity cost is the 9 percent that it could earn on the stock. Because money is not actually lost, opportunity cost is considered a noncash cost.

If Kent has five 100-dollar bills to invest to achieve the following returns, where should he invest his money? He has to invest in the first increment before he can invest in the second. What will be the opportunity cost of putting all the money in the bank?

As shown in Table 5.1, if all the money is put in the bank, there would be a return of $530. If Kent invests the money where it will be the most profitable, he will invest the first three units in livestock. He will then move to the lawn service because the first unit of the lawn service returns more than the fourth unit of livestock.

In this example, all five units can be invested for more than the bank would return. The most profitable return will yield (115 + 120 + 121) + (110 + 125) = 591. The opportunity cost of investing all the money in the bank would be $591.

Net opportunity cost is used by some people to compare two alternatives. Net opportunity cost is defined as the difference between what is invested in and the best alternative that is not chosen. In the above example, the net opportunity cost of putting all the money in the bank would be the difference between $591 (from the most profitable investment) and $530 from the bank, or $61.

Effects of Opportunity Cost on Business Decisions

All business decisions involve limited resources: land, labor, and capital. Each business must be able to achieve the proper mixture of these resources to earn a profit.

Resources are limited because of opportunity cost. More of a resource may be available to a company, but economically, it may not be in the company's best interest to add that resource. Investing money, labor, or land in another enterprise may prove more profitable.

For example, a manager may have the time and labor to paint the business' building every year, but the company's capital might be better spent on advertising and publicity. That use of the money

Table 5.1 - Investment Opportunities

Unit of Money	Lawn Service	Livestock	Bank
1	110	115	106
2	125	120	106
3	112	121	106
4	105	105	106
5	98	95	106

may enhance sales, something a paint job is less likely to accomplish.

Another reason why resources are limited is that several businesses are competing for them. Only a limited amount of suitable land is available. Labor can become limiting as businesses borrow money, causing rising interest rates, which make it less profitable to borrow money.

The manager's job is to find the combination of resources that best suits the business's needs.

Failure to Consider Opportunity Cost

Times do change, and successful managers change with them. What was considered practical and economical just 20 years ago may end in failure today. The real question today is, how can the manager stay in control of the situation?

If a manager fails to consider the opportunity cost of a decision, the opportunity to make a greater profit may be missed. By staying aware of opportunity cost, the manager hopes to avoid costly mistakes that cut into profit.

Measures Used to Represent Opportunity Cost

Since nearly all resources become limited at some time, managers need some way to represent opportunity cost of separate investments.

When the opportunities available require different amounts of investment, they are measured by looking at the rate of return on investment (ROI). ROI can be used to compare investments because it expresses the measure of return as a percentage. For example, if investment A returns $700 for a $600-dollar investment, there would be a gain of $100. If investment B returns $1,100 for $1,000 invested, it would also have a return of $100. Which is the best investment? They both return $100. However, because investment A has a return of 100/600, or 16.7 percent, and investment B only returns 100/1,000, or 10 percent, investment A is the best choice (16.7% > 10%).

When different opportunities require the same amount of investment, net returns are often used. Recall Table 5.1 presented earlier in the lesson. Net returns were used with each level of investment to determine the most profitable mix of investments. Because all investments are made in equal units, converting to ROI is not necessary to determine which investments are most profitable.

Summary

All decisions have some costs associated with them, and the opportunity cost incurred need to be considered. Opportunity cost is the return on the best alternative not selected. The rate of return on investment is a good indicator of which alterative is the best choice. All decisions that involve the use of scarce resources are affected by opportunity cost.

Credits

Bacon, Kevin, Nick Boren, and Van Kirkwood. *Agricultural Management and Economics (Student Reference).* University of Missouri-Columbia: Instructional Materials Laboratory, 1988.

Lesson 6:
Major Markets For Price Discovery in Agribusiness

Many agribusinesses are affected by the trading that takes place in the commodities market or stock market. Commodities exchanges are markets in which agricultural goods like grains and livestock and contracts for their future delivery are bought and sold. Stock exchanges are markets for the purchase and sale of shares of stock.

Major Markets for Price Discovery

The major market for price discovery for agricultural products in the United States is the commodities market, where cash commodities and contracts for future delivery are traded. The oldest commodities exchange in the United States is the Chicago Board of Trade. Other large exchanges are located in New York, Kansas City, and other cities across the country.

In the agricultural price discovery system, prices are constantly being rediscovered. Price discovery is the process by which buyers and sellers arrive at a specific price for a given lot of produce at a given location. Price discovery provides an estimate of supply and demand and of the market clearing price. It is different from price determination in that the price is not based on the general principles of supply and demand. Instead, the equilibrium price target must be discovered for each transaction in the marketplace based on the bargaining power of the buyers and sellers and what they believe the supply, demand, and price will be tomorrow and months into the future. The price that is discovered will not necessarily equal the market clearing price that is determined by supply and demand.

The commodities market allows the price discovery system to function by providing an organized marketplace for buyers and sellers of agricultural goods. The exchanges also provide uniform rules for trading, delivery, and payment, and they collect and distribute price information to the public. The commodities market thus provides the means for price discovery to take place.

How Agribusinesses Utilize Commodity Markets

Producers and agribusinesses use the commodities market to protect themselves against price changes. Agribusinesses such as grain elevators that warehouse storable commodities use the commodity markets to protect against price decreases that may occur during the time that the grain is being stored. Agricultural producers use the commodities market to protect the price they will get in the future while their crops are still in the fields or livestock are still in the pastures or feedlots. Agribusiness manufacturers and processors that purchase raw agricultural products use the commodities market to purchase the raw materials they need at the lowest possible price.

Another major participant in the commodities market is the speculator. A speculator is someone who is not directly involved in agribusiness and is not interested in buying or selling the actual agricultural products themselves, about which he or she generally knows little or nothing. The speculator is concerned only with selling those products at a higher price than that at which they were purchased. A trader is speculating when he or she holds a market position in anticipation of a favorable price movement that will generate profits. At times speculators do up to 90 percent of the trading that goes on in the commodities market. The addition of speculators to the commodities market creates a very competitive (extremely active) market.

Speculators affect agribusiness because they aid in discovering the price of agricultural products. If speculators believe that crops will be poor and a shortage will occur, prices for futures contracts will go up. If speculators believe that crops will be good and a surplus will be produced, prices for futures contracts will go down. Speculators' expectations of supply and demand therefore affect price.

Producers, agribusinesses, and speculators trade contracts for the purchase and sale of agricultural commodities for future delivery. A futures contract is a legally binding agreement made on a futures exchange to buy or sell a commodity. The contract specifies the quantity, quality, time of delivery, and price of a commodity. To understand how futures contracts function, certain terms must be understood.

Hedging - Hedging is a means of managing price or market risk by taking a position in the futures market that is the opposite of that held in the cash market. If a trader purchases a contract to buy, taking an opposite position would involve purchasing a contract to sell--the opposite of the initial or opening position. Taking an opposite position is also

Figure 6.1 - Futures Contract

DATE	CASH	FUTURES	BASIS
December	Expected hedge purchase price = $63.10/cwt.	Buy March 1 feeder cattle futures @ $65.60/cwt.	Expected basis = -$2.50/cwt.

referred to as offsetting a position. If a trader does offset his or her position, he or she is out of the futures market. All of this trading activity generally occurs without traders actually having any of the commodity in their possession.

Imagine that you are a trader and you purchase a contract to buy 5,000 bushels of corn at $2.35 a bushel. The next month the price of corn goes up to $2.50, and you decide to get out of the market, since you never really wanted the corn. So you buy a contract to sell the corn at $2.50, taking an opposite position. You make money on the difference in price, and never actually have any corn in your possession.

Basis - The basis is the difference between the local cash price and the price of the expiring futures contract. Since the local basis reflects the supply and demand conditions of that area, the basis may vary from one locality to another; it may also vary from day to day at a given location. The basis is derived from how far the commodity will have to be shipped to market. For example, suppose a futures contract is made in the Chicago exchange for a price of $70.00. The commodity must be shipped from Iowa at an estimated cost of $2.50. The cash price in Iowa will be $67.50. The basis is the $2.50 difference. The basis for grains can be expected to narrow (decrease) during the market year.

Long - Buying a futures contract without closing out one's position through an offsetting sale or by taking delivery.

Short - Selling a futures contract without closing out one's position through an offsetting purchase or by making delivery.

Long Hedge - A term referring to buying a futures contract to offset the risk of a price increase on an upcoming cash commodity purchase.

Short Hedge - A term referring to selling a futures contract to offset the risk of a decline in prices on an upcoming cash commodity sale.

This terminology may be somewhat confusing to people who are unfamiliar with the operation of the commodities market. An example of a long hedge is provided below to help illustrate the concept.

EXAMPLE: Mark is the manager of a livestock feedlot. He is concerned that the price of feeder cattle may rise and decides to purchase a futures contract in December to determine the maximum price he will have to pay for feeder cattle in March. Once he purchases the futures contract, Mark will not be able to purchase feeder cattle at a lower price if prices decline. Instead, he will have to pay the cash market price plus or minus the basis at the time he actually buys the livestock in the cash market and offsets the futures contract. Mark buys a March contract with the terms described in Figure 6.1.

When it is time to purchase the feeder cattle in March, futures are trading at $71.00/cwt. The local

Figure 6.2 - Futures Contract with a Rise in Prices

DATE	CASH	FUTURES	BASIS
March	Cash purchase price = $68.00/cwt.	Feeder cattle futures sell March 1 @ $71.00/cwt.	Realized basis = -$3.00/cwt
		Gain = $5.40	Basis improvement = -$0.50

CASH PURCHASE PRICE - FUTURES GAIN = REALIZED HEDGE PRICE
$68.00 - $5.40 = $62.60/cwt

Figure 6.3 - Futures Contract with a Decrease in Prices

DATE	CASH	FUTURES	BASIS
December	Expected hedge purchase price = $63.10/cwt.	Buy March 1 feeder cattle futures @ $65.60/cwt.	Expected basis = -$2.50/cwt
March	Cash purchase price = $61.00/cwt.	Feeder cattle futures sell March 1 @ $63.00/cwt.	Realized basis = -$2.00/cwt
		Loss = $2.60	Basis narrowed = +$0.50

CASH PRICE + FUTURES LOSS = REALIZED HEDGE PRICE
$61.00 + $2.60 = $63.60/CWT

cash market is at $68.00/cwt. When Mark offsets the hedge by buying a futures contract to sell and purchasing the feeder cattle in the cash market, he obtains the information oultined in Figure 6.2.

Mark was right in believing that cattle prices might rise, and by hedging he protected himself against the rising prices. He purchased the cattle at the higher price of $68.00/cwt but gained $5.40 by hedging in the futures market. Mark's realized hedge price is $62.60/cwt., which is 50 cents better than he expected because of the improvement in the basis.

Mark did not buy the cattle on the futures contract but at the local cash price. The futures contract was used only to protect him from rising prices. He bought the cattle and then offset his position in the futures market by selling the contract. Mark thus bought long and sold short and gained a realized hedge price of $62.60.

What would have happened if cattle prices had dropped? Suppose the futures are trading at $63.00/cwt. and local cash price is at $61.00/cwt. How will this change the realized purchase price?

Mark would have done better not buying a futures contract, even though his realized price was only 50 cents more than he expected.

Another way to protect against price changes in the future is by using agricultural options. Options are contracts that can provide insurance and marketing flexibility for producers and agribusinesses. An option is used only if prices are in the business's favor. It gives the owner the right, but not the obligation, to buy or sell a futures contract at a certain price for a certain period of time. The price that must be paid for these options is termed the premium. The premium is determined by what the buyer and seller believe the commodity is worth. The person or persons who sell the option are willing to take the risk of a change in the price of a commodity for the amount of the premium.

The guaranteed price at which the futures contract can be bought or sold is called the strike price. A call option conveys the right to purchase a futures contract at a designated strike price. A put option conveys the right to sell a futures contract at a specific strike price.

The buyer of a futures option has three choices: (1) exercise the option, by taking a buying or selling position in the futures market; (2) allow the option to expire without using it and lose only the premium; or (3) offset the original purchase by selling the option. Like the futures contracts, options are traded through commodity exchanges. An example of options trading is provided below.

EXAMPLE: Suppose Beth, a feedlot manager, thinks that corn prices are going to rise and wants to protect herself from price changes without hedging in the futures market. She purchases a call option for 5,000 bushels of corn at a guaranteed price of $3.50 per bushel within two months of the purchase of the option. Beth pays a premium of 5 cents per bushel, $250.00 (5,000 x .05). When Beth needs to purchase corn, the price of corn is $3.60. She purchases the corn at the local cash price and then exercises her option. The option is now worth 10 cents per bushel ($3.60 - $3.50 = .10). Beth has saved five cents per bushel by purchasing the option as shown in Figure 6.4.

Figure 6.4 - Returns on an Option

CASH PRICE - OPTION PREMIUM + OPTION GAIN = REALIZED PRICE
$3.60 - .05 + .10 = $3.65

If the futures price were less than $3.50, Beth could have allowed the options contract to expire and purchased the corn at the lower cash price. Her only loss would have been the $250 originally paid for the option.

Every trader in the commodities market should recognize the opportunities for gain and the possibilities of loss. For every dollar that someone gains in the commodity market, someone must also lose a dollar. Total gains in the commodities market are equal to total losses.

The Stock Market's Role in Agribusiness

While the commodities market deals directly with agricultural products, agribusinesses may also operate in the stock market. The stock market plays an important role in raising capital for agribusiness corporations. Selling shares of stocks through the stock exchange provides the means for corporations to raise money for starting and expanding their operations. The exchanges also provide places for investors to sell their shares to other individuals if the need arises.

Individuals or other companies that purchase stock are called shareholders or stockholders. They receive certificates called shares that indicate the number of units of stock that they have purchased. The shares of stock entitle stockholders to a share of the profits of the corporation. The amount that is paid to a shareholder is called a dividend. Dividends are based on the profits of the corporation. The value of the stock may go up or down, depending on the corporation's profits or expected profits.

The two main categories of stock sold by businesses are common and preferred. Preferred stock takes precedence over common stock in payment of dividends. Financial losses can therefore be greater with common stock than with preferred. Dividends for preferred stock are guaranteed in many cases.

Summary

Price discovery for U.S. agricultural goods takes place primarily in the commodities market. Producers and other agribusinesses use these markets to protect themselves against changes in the price of a commodities by purchasing and selling futures contracts and options. Agribusinesses also utilize the stock market by selling shares to raise funds for starting or expanding their businesses.

Credits

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Lesson 7:
Government and the Economics of Agriculture

Throughout U.S. history, the economics of agriculture and the economy of the United States have been closely connected. The government recognizes that agriculture strongly affects the overall economic condition of the United States, and the agricultural industry knows that government policies affect the economics of agriculture. The government has controlled prices, created policies to limit production, and used agriculture to stabilize the economy of the United States. Some policies have been very controversial, while others have been widely accepted as vital to maintaining a safe and adequate food supply in the United States.

Government Involvement in Agriculture

The reasons for government involvement in agriculture have changed over time, depending on the particular political, social, and economic environment of the nation. For example, one reason the government has found it necessary to become involved in agriculture is to oversee the safety of the food supply. It has intervened to ensure food safety due to increasing public concern in recent years over such things as sanitation, additives, and nutritional values of foods.

Another reason the government has intervened in agriculture is to ensure an adequate food supply. The government has aimed at expanding production. Projects funded by the government for irrigation, drainage, research, and agricultural extension education have increased productivity. Since the 1970s, the government has been increasingly concerned with protecting the environment to ensure the capacity of agriculture to produce in the future. Programs and special funds supported by the government have been developed to conserve the soil and ensure its productivity for future use. The U.S. government has also supported and funded programs for conserving water and preserving prime farm land.

The government has expanded its involvement in the export of food since the 1970s. One of its goals has been to increase export earnings. It has also used the exportation of food and fiber as a tool of foreign policy. Beyond supplying food to other nations, agricultural exports are used to maintain good foreign relations and as bargaining chips in international diplomacy.

One of the most costly reasons the government became involved in agriculture was to regulate prices and support farm income. The government formed storage programs in the 1970s to remove surplus commodities from the market to stabilize prices. It has used land set aside programs and direct payments to producers to support farm income.

Government Impact on Agriculture

In developing programs to meet all these different concerns, the government has had a huge impact on the agricultural industry. The industry has had to adapt itself to this intervention, which has not always been to its benefit.

The government's attempts to ensure the safety of the food supply have had both a positive and a negative effect on the agricultural industry. The banning of certain herbicides and insecticides has decreased production through the loss of crops to uncontrolled weeds and insects. The government has regulated processing facilities to ensure sanitation and to eliminate the dumping of waste. These regulations have improved food safety but have also increased production costs and the cost of agricultural commodities. They have had the side effect of forcing many small producers out of certain areas of agricultural production.

Government policies to expand the food supply have increased productivity. Government-funded research has resulted in better farming methods, such as terracing and no-till farming, that have increased production per acre. Irrigation projects in the western United States, particularly in California and along the Colorado River, have made once unproductive land fertile.

Government conservation programs have had a positive impact on the environment. Soil and water conservation is one of the largest areas of government involvement in agriculture. The government required producers to file a conservation plan to participate in federal programs like the set-aside program, in which producers agreed not to plant crops on a certain portion of their land. The Conservation Reserve Program (CRP) pays producers not to grow crops on land entered into the program. Soil conservation measures have

made it possible to save the productive topsoil and increase yields.

The increased productivity caused by government involvement has increased exports, generating more profits for the agricultural industry. Agricultural producers can provide more food and fiber products than are needed to meet domestic demands. The agricultural industry produces commodities at prices that make them very competitive in international markets.

Storage programs to control the price of agricultural products helped agricultural producers during times of high production. They also encouraged agricultural producers to depend on government intervention to correct the market rather than make changes themselves to meet the demands of competition. If an automobile manufacturer produces too many cars, the government does not buy the excess cars to create a shortage and raise the price. The manufacturer is forced to lower the price to clear out the excess inventory. If a manufacturer is unable to sell the product and make a profit, the company will go out of business, and other manufacturers of automobiles that can compete successfully will benefit. As the government reduces agricultural support programs, producers will face the task of making a profit in a competitive market, and some will be unable to survive.

Agricultural Prices and the Government

Price is a primary tool for rationing in a market economy like that of the United States. When meat or bread prices rise, consumers see the purchasing power of income decline. Some consumers are forced to make do with less. The extent to which citizens of the United States are affected when food prices fluctuate gives the government justification to make food production a concern of public policy. In the past, the government has used four methods to control the price of food directly.

The federal government has instituted price controls in times of military conflict and under peacetime conditions of high inflation and declining wages. For example, during and after World War II, shortages made it necessary to ration goods. Price controls were used during the shortages to prevent inflation and windfall profits by producers. President Nixon also used price controls in 1971 in a program designed to deal with inflation and unemployment. It consisted of a 90-day freeze on most prices and wages. Retail food prices were also frozen, but farm commodity prices were not, and they increased. Because commodity prices had been so low, food prices stabilized during the freeze. After Nixon lifted the freeze and concentrated on controlling profit margins in 1972, food prices went up. However, food prices went up only 4.3 percent, while commodity prices had gone up 30 percent. The prices received by agricultural producers gave them a profit margin comparable to that of wholesalers and retailers.

Export controls, like price controls, have been used by the government as a solution to economic problems. The government has restricted export shipments to control the food supply and domestic prices in times of world food shortages. Restricting exports increases the food supply and lowers prices. Export controls have only been used in the short run until production could meet demand.

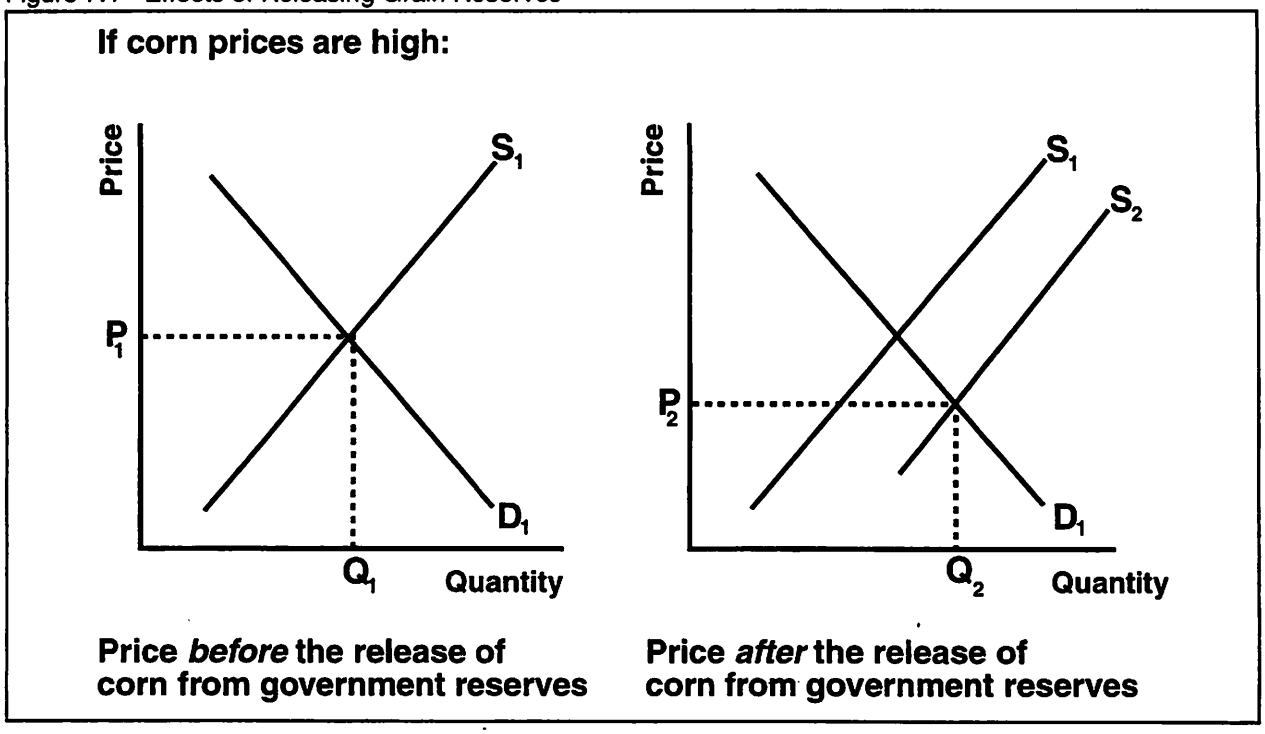
The government has also controlled price by reducing import restrictions. Reducing import restrictions and allowing more products to be imported increases supply and lowers prices. This action is good for consumers, retailers, and wholesalers because they have to pay less. Agricultural producers do not support this alternative because it lowers their incentive to produce and makes it difficult to decide what to produce to meet the demands of changing markets.

The government has strongly supported maintaining grain reserves because of their importance in controlling prices. Grain reserves can be used as an inflation-fighting tool. If grain prices rise too high, the government releases some of the reserves, which increases supply and lowers the price. If the prices drop too low, the government increases the price by increasing reserves. The timing of grain releases is an important part of using this tool effectively, because releasing grain can severely depress the price (Figure 7.1). Grain reserves provide the only means by which the government can control grain prices without influencing future production decisions.

Summary

In the past, the government has been involved in agriculture for various reason, including insuring an adequate food supply and regulating agricultural prices. Four methods have been used by the government to control the price of food: instituting

Figure 7.1 - Effects of Releasing Grain Reserves



price controls, restricting exports, reducing import restrictions, and controlling grain reserves.

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Lesson 1:
Managing Financial Resources

Planning for the future requires more than setting educational or career goals. A complete financial plan takes into consideration these goals and needs and includes a plan for paying for them. A financial plan can help an individual manage his or her money so that personal and financial goals can be reached.

The Importance of Financial Planning

Financial planning is the process of defining goals and developing and implementing a plan to finance them. Putting together a financial plan is important because it reveals how much money is received and enables the planner to monitor spending. This information can then be used to manage money to allow an individual to achieve his or her goals. Meeting goals involves managing money for personal needs, such as food, clothing, and housing. Using a financial plan to manage money also permits an individual to plan in order to obtain those things he or she desires, such as an expensive car, or a special vacation.

The Importance of Goals and Objectives

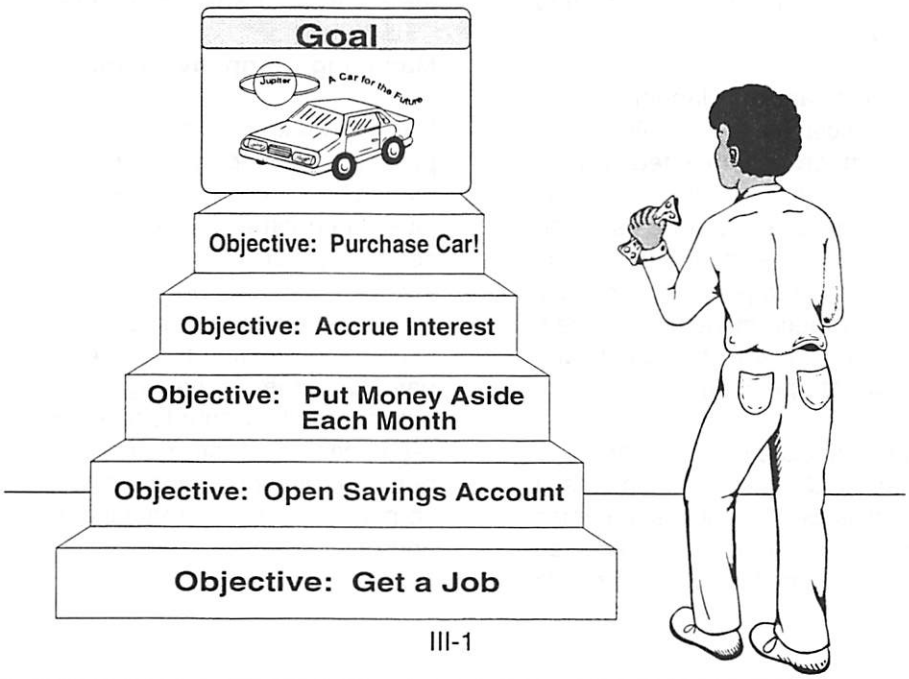
A goal is a statement of what an individual wants to accomplish both personally and financially. Goals give direction to the use of financial resources. Goals are an important part of the financial plan, because they indicate where finances will be needed. A person might have the goal of saving enough to make a down payment on a car or buy breeding stock to start an agricultural production business. Achieving these goals will give the individual great satisfaction and likely stimulate more goal setting and more financial planning.

Objectives are the steps necessary to achieve a goal (Figure 1.1). They outline the details that will make a goal a reality. The value of objectives in a financial plan is that they allow the individual to plan the use of financial resources and measure his or her progress toward a goal.

Steps in the Financial Planning Process

The first step in financial planning is recording a projection of how much money will be received. Income from jobs may be paid weekly, biweekly, or monthly, while other income may be received only once or twice a year. A record should be kept showing when money will be received and the source and amount of the money. Any financial plan must take into account the difference between net income and gross income. Net income is the actual amount of money that will be received after any deductions (e.g., income tax, Social Security).

Figure 1.1 - Goals and Objectives



The second step in the financial planning process is making a list of wants and needs and using it to determine goals and set objectives. When making a financial plan, needs, things necessary for survival, form the basis of the plan and should be considered first; wants, or those things that are desired to make life more comfortable, are secondary in importance.

The third step in a financial plan is to compare the amount of money received with the expenses associated with wants and needs. In this step, a distinction should be made between short-, intermediate-, and long-term financial goals; the amount of money received will help to determine the time frame for achieving the goal. A short-term goal focuses on immediate satisfaction of wants and needs, with objectives to be satisfied in a one- to four-week time frame. An example of a short-term goal is to set enough money aside, after meeting personal needs, for taking a weekend trip or going out for dinner and a movie. An intermediate goal focuses on a somewhat longer period: two to twelve months. Some intermediate goals would be saving to purchase a new appliance, piece of furniture, or stereo. A long-term goal focuses on delayed gratification, with objectives taking a year or more to satisfy. Long-term goals may include financial planning to purchase a car or setting aside money for educational needs. Short-, intermediate-, and long-term goals are based on income, and income is limited to the money received. A financial plan can help an individual to balance income and spending so financial obligations and personal goals can be met.

The fourth step in financial planning is to implement the financial plan. With the information that has been accumulated, a plan can be developed that shows how the money received is to be spent to achieve goals. The plan should also monitor how money is actually spent. The person putting together the financial plan should record how much money is received, indicate how much money is to be spent, and then track the amount of spending.

The final step in the financial planning process is to monitor the plan and make adjustments if necessary. No plan is perfect, and sometimes adjustments must be made. Unexpected expenses may make it necessary to rethink decisions about wants and needs. Since meeting needs is the basis of the plan, adjustments may only be made to wants. Making adjustments does not necessarily eliminate important goals, but it may change the time frame in which they are accomplished. The ability to adjust the plan should only increase an individual's confidence in making decisions and taking action.

Education, Experience, and the Financial Plan

A financial plan is based on income, and education and experience affect earning potential. Obtaining an education and gaining experience in one's chosen field are therefore important to consider in financial planning. Both are investments made to increase future income.

Education is an important factor in financial planning. Since a college or trade school education may be quite expensive, education requires financial planning. However, the knowledge gained is an asset that often allows an individual to earn more income than he or she would without it, and these earnings are usually greater than the expense of the education. A larger income permits greater freedom in financial planning because more money is available to satisfy wants.

Experience also affects financial planning. The skills obtained through experience on the job can have a dramatic effect on earning potential. Generally, the more experience an individual has, the more he or she can be expected to earn.

Managing Company Resources

Like individuals, companies engage in financial planning. Employees may play a role in managing the company's resources by monitoring job-related expenses that will be paid for by the company. For example, transportation expenses involved with the business may be paid, or a company car may be given to the employee to be used for job-related travel. A company may also pay for other traveling expenses, such as lodging, food, or entertainment for clients. These resources must be managed separately from personal finances, since they are a part of the company's plan for reaching its business goals and objectives.

Managing company resources well will help the company reach its goals for profit, and a profitable business may offer benefits to its employees. For example, they are more likely to experience job stability. Employees also benefit due to greater opportunities for advancement and increased earnings.

Summary

Financial planning involves recording money received and spent and using this information to plan how to meet personal and financial goals and objectives. The financial planning process involves five steps: listing the money received, listing wants and needs and developing goals and objectives, comparing the amount of money received to the costs of wants and needs, implementing a financial plan to control spending, and monitoring the plan to make adjustments if necessary. The entire plan is affected by education and experience, both of which may increase earning power. On the job, employees may have to manage money as well, since company resources paid to employees for business expenses reflect a part of the company's financial plan given to employees to manage.

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Lesson 2:
Developing a Budget

A budget can be a great planning tool that enables an individual to monitor his or her financial status. It can help a person take control of his or her future because it shows the amount of money available for purchases. A budget can also be an aid in learning to live within one's income.

The Importance of a Budget

A budget consists of two parts. The first part shows the expected income for the period, and the second part shows the planned expenditure of that income. In this way, a budget becomes a forecast of income and expenditures for a specific period of time.

As a record of expected income and expenditures, a budget can be used to monitor spending. At the end of the budgeting period, the plans made for spending income can be compared to actual spending. This information allows an individual to make changes in the amount or type of spending if necessary.

As a planning document, a budget enables individuals, households, businesses, and even governments to set priorities and monitor progress toward certain goals. For example, an individual may budget to set aside income for educational needs or a down payment on a new car. Businesses use budgets to ensure that outlay is less than income so that a profit is realized that can then be used for such things as expanding the business or paying dividends to stockholders. The most complicated budgetary process is that of the government, which plans the collection and expenditure of the monies needed to carry out the social, military, and economic policies of an administration.

Finally, a budget can help an individual to meet unexpected expenses when they occur. In preparing a budget, setting aside savings is important not only for meeting budget objectives but also for providing a surplus of money to meet unplanned expenses. If sufficient money is available, the planned budget can still be carried out in spite of those expenses, but if not, changes must be made in the budget based on needs and wants. Delaying the purchase of items that are desired rather than needed, like a new stereo or car, will be necessary. Knowing how to distinguish between needs and wants and being able to adjust a personal budget makes it possible to continue to achieve financial objectives and goals, even if they may be delayed by unexpected expenses.

Credit and Personal Finances

When planning a budget, a person should remember to include his or her use of credit. Credit is the transfer of money on the promise of repayment at some future date. Credit cards and bank loans are two types of credit.

Credit must be taken into consideration in short-, intermediate-, and long-term financial management, because money must be paid back to the creditor out of future income. Paying back the money borrowed may take months or years. Therefore, an individual should be cautious when using credit to make a purchase. Making many purchases on credit can create a huge financial burden for the future.

Interest is the money paid on money that is invested or borrowed. It is usually a percentage of the amount borrowed when using credit. The cost of interest should be included when calculating the total cost of an item. If it is possible to pay cash for that item, credit should not be used. Avoiding interest charges saves money, and saving money makes more money available to meet other objectives and goals.

If managed properly, however, credit can be of great benefit. Purchasing on credit allows people to obtain things that are needed immediately even when cash is not available and then use them while paying for them over a period of time. Credit also makes it possible to buy very expensive items, like a house, for which it would be difficult to save enough money.

The Financial Implications of Debt

Because credit is often easy to obtain, the temptation to use credit to "buy now and pay later" may be difficult to resist. However, payments on credit may become a liability. Poor use of credit can lead to months or even years of burdensome debts. Going into debt can have a number of negative consequences.

Accumulating large debts may hamper future credit purchases. Credit card companies and banks are not willing to lend money to those people who have

shown themselves to be unable to pay off their debts. When buying something on credit, plans should be made to make payments in a timely manner.

Debt may make it difficult to pay for those things needed for survival. Assuming too many financial obligations at once can lead to monthly payments so large that not enough financial resources are left to meet essential living expenses. If making purchases on credit makes it hard to buy necessities, using credit should be avoided.

Failure to meet financial obligations can lead to other problems. Credit collectors may contact employers if payment is not received. The debtor's wages may then be garnisheed. Garnishment is the legal practice of taking a specified amount of money from earnings in order to repay a creditor. A debtor who cannot repay the money borrowed may be forced to declare bankruptcy. His or her personal assets will be seized and sold to repay creditors.

Debt is not always a bad thing, however, if credit is managed properly. For example, many students have to borrow large amounts of money to finance their education after high school. This use of credit creates the potential for a larger income in the future. Most student loans do not have to be paid back until the student has graduated and found a job, and payments can be made over a period of time. In almost all cases the return on the investment is far greater than the amount of debt. In addition to paying for further education, the use of credit allows individuals to establish that they can handle credit responsibly. Being in debt and showing that they can make the necessary payments can make it easier for them to obtain credit later.

Some guidelines for using credit are given below.

Credit should be used in some situations:

- To help purchase items that are needed to establish a household, such as a refrigerator or furniture.
- When a true emergency arises and cash is not available.
- If money is needed for education. Borrowing money for an education usually pays off in increased income for the borrower.
- When the price of a necessity is increasing quickly and money can be saved by using credit

Credit should not be used in the following instances:

- When buying something on impulse because the payment terms seem so easy that they will not be a problem.
- When buying something just to boost morale or increase status.
- In expectation of future salary increases.
- When purchases strain cash reserves and wreck a budget because payments are too high.
- For daily living expenses.
- When what is bought will wear out before the last payment is made.
- Anytime that no reasonable prospect for repaying the amount exists.

Guidelines for Budgeting

Certain guidelines can be followed when setting up a budget. These guidelines indicate how much of an individual's monthly income should be spent on various expenses. Different standards may be applied when determining what percentage of monthly income should be spent on a particular expense, but some possibilities are listed below. If spending exceeds these percentages, individuals should examine their budgets to make sure their expenditures are appropriate.

- Housing - 20 to 30 percent
- Utilities - 5 percent
- Transportation - 5 to 15 percent
- Food - 10 to 20 percent
- Savings - 10 percent
- Clothing - 5 to 10 percent
- Entertainment - 5 percent
- Installment debt - 5 percent and up

Summary

A budget is an important tool for financial planning because it provides a forecast of income and expenditures for a specific period of time, allows spending to be monitored, enables a person or group to set goals for spending, and helps meet unexpected expenses. When planning a budget, monitoring the use of credit is important. If managed properly, credit can benefit an individual by allowing him or her to purchase and use an item

even if cash is unavailable. However, excessive credit purchases and high interest payments may create debts that hamper future business purchases, make it difficult to pay for necessities, and even lead to the garnishment of wages and bankruptcy.

Credit

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Lesson 3: Credit

Over a lifetime, an individual will use credit to buy many items. Establishing the foundation for receiving credit through the proper management of finances is therefore very important. Understanding the types and sources of credit available will allow a person to make the appropriate choices when he or she wants to purchase something using credit.

Credit History

An individual's credit history is a record of how he or she has managed finances in the past. The individual's ability to obtain credit is influenced by his or her credit history. A good reputation for managing finances can build a good credit history and make more credit available, which, if used wisely, will build an even stronger credit history. However, a record that shows poor management of finances can prevent a person from getting credit, and it can take many years to rebuild a credit history. If an individual manages his or her finances so that spending does not exceed income, a financial institution will be more confident that he or she will be able to make the necessary payments and will be more likely to grant credit.

Establishing a Credit History

An individual establishes a good credit history by showing that he or she is dependable and responsible and can manage finances. This foundation demonstrates to a lender that an individual can be trusted to pay back money that is borrowed.

A good start to establishing a credit history is to set up a checking or savings account as soon as possible. Once a savings account is set up, it should be managed so that it earns interest on money that is not needed for short-term expenses. The balance of a checking account should be kept above the minimum so that no service charges are issued for writing checks. A well-managed account indicates financial responsibility and is a stepping stone to establishing a good credit history.

Establishing a good credit history can be done by simply paying the bills for everyday living expenses on time. Paying rent and utility bills promptly shows that an individual is financially responsible. Using credit cards wisely and with caution can also help establish a good credit history. Credit cards on which the balance is paid off monthly can help to show lenders that an individual is responsible.

Another way to establish a credit history is through small loans. Responsible repayment of small loans provides a good opportunity to establish a solid credit rating. A teenager can build a credit history by having an adult who has already built a good credit history, such as a parent, co-sign for a loan. The teenager then has the chance to show a lender that he or she is responsible. If the loan is paid back promptly, he or she establishes a good reputation with the lender as well as a credit history to show future lenders that his or her finances were properly managed in the past. It can help an individual obtain the credit needed to borrow money to buy those items with which to set up a household.

The same things that can build a good credit history can create a poor credit history if managed badly and may cause an individual to be denied credit. Writing checks when an account has insufficient funds shows poor financial management. Failing to make payments on a co-signed loan can ruin an individual's credit history, as well as that of the person who co-signed. Maintaining balances on credit cards from month to month shows poor financial management.

Kinds and Sources of Credit

Few individuals have enough cash to buy all the things they need, so they must borrow money. They must know the kinds of credit that are available and the sources of credit to choose the correct type for their needs. An individual should always consider all the options before making a decision about credit.

Credit can be categorized into two basic types based on the length of time the money is needed. Generally, the intended use of the loan will help determine which type is chosen.

Current credit is money borrowed for a term of less than a year. Examples of this short-term credit include purchases made with credit cards, loans for medical bills, and emergency loans for auto or home repairs. The loan is generally paid back in monthly installments.

Noncurrent credit is money borrowed for more than one year. This long-term credit may be used to purchase a car, buy furniture or appliances, or pay for educational expenses. It can also be used to

buy a home or land or to purchase or start a business. The loan is usually paid back in monthly installments.

Some loans require security. A secured loan is a loan in which an asset--either the item being purchased or something else owned by the borrower--is put up for collateral. The collateral is pledged or mortgaged by the borrower to ensure repayment of the money. If the money is not repaid, the asset may be seized and sold to pay the loan. Examples of collateral include a car used to secure the loan needed to purchase it and a home used as collateral to obtain the money needed for remodeling. In contrast to a secured loan, an unsecured loan, which is sometimes called a signature loan, does not require collateral and is based on a good credit history. Secured loans usually have lower interest rates than unsecured loans.

Repayment schedules vary, depending on the type of credit used. Some types may require a single payment that includes the principal and interest in one lump sum. For instance, lump sum payments are made on credit cards that require the balance to be paid on a monthly basis. A loan that requires a lump sum payment may be taken out by individuals or businesses if they know that larger amounts of income will be received at a particular time of the year. An agricultural producer, for example, may borrow money to produce crops and pay the entire sum back when crops are harvested. The most widely used method for repaying loans, however, is with a repayment schedule in which principal and interest are to be paid back on a periodic basis. This schedule may be set up on a monthly, semi-annual, or even yearly basis.

An individual may borrow money from a number of different sources. The amount, loan period, purpose for which the money is borrowed, repayment method, and type of collateral necessary to secure the loan will vary with each source.

Commercial banks - Commercial banks offer short- and long-term loans that require a single payment or periodic payments of interest and principal. Commercial banks will loan money to individuals and businesses for almost any use, including the purchase of real estate and other business and personal uses.

Credit unions - Credit unions are cooperative associations that accept savings deposits and make small loans to their members. The loans are for short- and long-term credit.

Savings and loans - Savings and loans were originally set up to provide long-term credit used to buy homes. They lend money for real estate.

Small Business Administration - The SBA primarily guarantees short- and long-term credit for small businesses.

Manufacturers and dealers - Manufacturers and dealers primarily offer short- and long-term credit to customers to buy the cars, furniture, or other products that they are selling.

Bank credit cards - Credit cards are issued by banks and allow customers to borrow money to buy goods or services. Most involve short-term credit, with payments being made on a monthly basis.

Simple Interest

When credit is used, interest is charged on the amount of money borrowed. Simple interest is interest that is paid only on the sum of money loaned, or principal. Simple interest is calculated by multiplying the principal (p) borrowed by the rate of interest charged (r) and the amount of time (t). The formula is:

$$i = prt$$

If a loan for $1,000 was taken out at 8 percent interest, the simple interest after six months would be $40.

$$i = prt$$

$$i = (\$1{,}000)(.08)(.5)$$

$$i = \$40$$

Compound Interest

When interest is calculated not only on the principal but also on the accrued interest payments, it is referred to as compound interest. The formula for figuring compound interest is as follows:

$$A = p\left(1 + \frac{r}{x}\right)^{yx}$$

In the formula, *A* is the amount of principal and interest, *p* is the principal, and *r* is the yearly rate of

interest. The number of years is *y*, and *x* is the number of times the interest is compounded yearly.

Amortized Loans

Amortized loans are payed off in installments over time, with each payment covering the current interest and part of the principal. In an equal-payment plan, each payment is the same amount of money. Early payments include more interest and less capital. Interest payments decrease in later years as the outstanding principal decreases. More of the payment then goes to pay off the principal.

Lending institutions usually calculate payments on amortized loans using software designed for financial management. Amortization tables, such as the one pictured in Figure 3.1, can also be used as a quick reference for figuring payments. Suppose that $10,000 is borrowed at 10 percent interest for five years. What would the annual payments be? Look at Table 3.1. For five years and 10 percent interest, it shows a value of .2637. The annual payments would be $10,000 × .2637, or $2,637.

Summary

Building a good credit history is an important part of financial planning. Establishing a good credit history can help a person reach goals and objectives by enabling him or her to obtain more credit. Knowing the different types and sources of credit available is also important because it allows an individual to make the best choices for his or her needs.

Credits

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Figure 3.1 - Annual Payment per $1 of Loan at Given Interest Rates and Maturities (Amortization Table)

YEAR	4%	5%	6%	7%	8%	9%	10%	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%
1	1.0400	1.0500	1.0600	1.0700	1.0800	1.0900	1.1000	1.1100	1.1200	1.1300	1.1400	1.1500	1.1600	1.1700	1.1800	1.1900	1.2000
2	.5301	.5378	.5454	.5530	.5607	.5684	.5761	.5839	.5916	.5994	.6072	.6151	.6229	6308	.6387	.6466	.6545
3	.3603	.3672	.3741	.3810	.3880	.3950	.4021	.4092	.4163	.4235	.4307	.4379	.4452	.4525	.4599	.4673	.4747
4	.2754	.2820	.2885	.2952	.3019	.3086	.3154	.3223	.3292	.3361	.3432	.3502	.3573	.3645	.3717	.3789	.3862
5	.2246	.2309	.2373	.2438	.2504	.2570	.2637	.2705	.2774	.2843	.2912	.2983	.3054	.3125	.3197	.3270	.3343
6	.1907	.1970	.2033	.2097	.2163	.2229	.2296	.2363	.2432	2501	.2571	.2642	.2713	.2786	.2859	.2932	.3007
7	.1666	.1728	.1791	.1855	.1920	.1986	.2054	.2122	.2191	.2261	.2331	.2403	.2476	.2549	.2623	.2698	.2774
8	.1485	.1547	.1610	.1674	.1740	.1806	.1874	.1943	.2013	.2083	.2155	.2228	.2302	.2376	.2452	.2528	.2606
9	.1344	.1406	.1470	.1534	.1600	.1667	.1736	.1806	.1876	.1948	.2021	.2095	.2170	.2246	.2323	.2401	.2480
10	.1232	.1295	.1358	.1423	.1490	.1558	.1627	.1698	.1769	.1842	.1917	.1992	.2069	.2146	.2225	.2304	.2385
11	.1141	.1203	.1267	.1333	.1400	.1469	.1539	.1611	.1684	.1758	.1833	.1910	.1988	.2067	.2147	.2228	.2311
12	.1065	.1128	.1192	.1259	.1326	.1396	.1467	.1540	.1614	.1689	.1766	.1844	.1924	.2004	.2086	.2168	.2252
13	.1001	.1064	.1129	.1196	.1265	.1335	.1407	.1481	.1556	.1633	.1711	.1791	.1871	.1953	.2036	.2121	.2206
14	.0946	.1010	.1075	.1143	.1212	.1284	.1357	.1432	.1508	.1586	.1666	.1746	.1828	.1912	.1996	.2082	.2168
15	.0899	.0963	.1029	.1097	.1168	.1240	.1314	.1390	.1468	.1547	.1628	.1710	.1793	.1878	.1964	.2050	.2138
16	.0858	.0922	.0989	.1058	.1129	.1203	.1278	.1355	.1433	.1514	.1596	.1679	.1964	.1850	.1937	.2025	.2114
17	.0821	.0886	.0954	.1024	.1096	.1170	.1246	.1324	.1404	.1486	.1569	.1653	.1739	.1826	.1914	.2004	.2094
18	.0789	.0855	.0923	.0994	.1067	.1142	.1219	.1298	.1379	.1462	.1546	.1631	.1718	.1807	.1896	.1986	.2078
19	.0761	.0827	.0896	.0967	.1041	.1117	.1195	.1275	.1357	.1441	.1526	.1613	.1701	.1790	.1881	.1972	.2064
20	.0735	.0802	.0871	.0943	.1018	.1095	.1174	.1255	.1338	.1423	.1509	.1597	.1686	.1776	.1862	.1960	.2053
25	.0640	.0709	.0782	.0858	.0936	.1018	.1101	1187	.1275	.1364	.1454	.1546	.1640	.1734	1829	.1924	.2021
30	.0578	.0650	.0726	.0805	.0888	.0973	.1060	.1150	.1241	.1334	.1428	.1523	.1618	.1715	.1812	.1910	.2008
35	.0535	.0610	.0689	.0772	.0858	.0946	.1036	.1129	.1223	.1318	.1414	.1511	.1608	.1707	.1805	.1904	.2003
40	.0505	.0505	.0664	.0750	.0838	.0929	.1022	.1117	.1213	.1309	.1407	.1505	.1604	.1703	.1802	.1901	.2001

Lesson 4:
Developing a Savings and Investment Plan

Developing a savings and investment plan is an important part of a financial plan. Saving money not only maintains a pool of available funds but actually increases the amount of money earned by providing additional income through interest payments. Investing money is generally riskier because investments can provide greater financial losses as well as rewards.

The Time Value of Money

The time value of money is based on the relationship of money, interest, and time. Simply said, a dollar received today is not equal to a dollar that is received in the future, because today's dollar can be put to work to produce returns in excess of the value of the original dollar. Returns accumulate due to interest, which is the payment an individual receives for letting someone else use his or her money. Over time, interest increases the value of the money originally invested. The longer the period of time the money is invested or the higher the interest rate, the more the money will earn.

Two types of interest may be paid on an investment. Simple interest is interest that is paid only on the sum of money invested. When interest is paid on not only that amount but also on the accrued interest payments, it is referred to as compound interest.

To find the value of money over time, being able to calculate the value of money in the future is necessary. The formula for calculating the future value of money is

$$FV = p(1+i)^n$$

where FV = future value, p = principle, i = rate of interest, and n = number of years. This formula enables an individual to determine the value of savings or investments in interest-bearing accounts after they have been compounded with interest for a specific period of time.

As an example, suppose Annie has $100 and is planning on investing it at 7 percent interest. She wants to know the future value of that money in 2 years.

$$FV = p(1+i)^n$$

$$\text{Future value} = \$100\ (1 + .07)^2$$

$$\text{Future value} = \$100\ (1.07)^2$$

$$\text{Future value} = \$100\ (1.1449)$$

$$\text{Future value} = \$114.49$$

The value of Annie's investment in two years will be $114.49.

Tables can also be used to determine the future value of money with compound interest. Suppose that $100 is placed in the bank at 7 percent interest for five years. What would the future value be? Look at Table 4.1. For five years and 7 percent interest, it gives a value of 1.4025. The original investment is multiplied by this number to find the future value of the money. The future value of $100 compounded at 7 percent for five years is $140.25 (100 x 1.4025).

The Rule of 72

The Rule of 72 is a simple formula that provides an estimate of the number of years it would take for an investment to double in value based on the interest rate. In the formula, *i* equals the rate of interest and *y* equals the number of years to double the investment.

$$\frac{72}{i} = y$$

Suppose that Garrett made an investment at 6 percent interest. He wants to figure out how long it will take for his investment to double.

$$\frac{72}{i} = y$$

$$\frac{72}{6} = y$$

$$12 = y$$

Garrett's investment will double in 12 years.

The Importance of Saving Money

Savings are a very important part of an individual's financial plan. The amount in savings can be a significant factor in allowing a person to achieve

Figure 4.1 - Future Value at Compound Interest (Compounded Annually)

YEAR	4%	5%	6%	7%	8%	9%	10%	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%
1	1.0400	1.0500	1.0600	1.0700	1.0800	1.0900	1.1000	1.1100	1.1200	1.1300	1.1400	1.1500	1.1600	1.1700	1.1800	1.1900	1.2000
2	1.0816	1.1025	1.1236	1.1449	1.1664	1.1881	1.2100	1.2321	1.2544	1.2769	1.2996	1.3225	1.3456	1.3689	1.3924	1.4161	1.4400
3	1.1248	1.1576	1.1910	1.2250	1.2597	1.2950	1.3310	1.3676	1.4049	1.4428	1.4815	1.5208	1.5608	1.6016	1.6430	1.6851	1.7280
4	1.1698	1.2155	1.2624	1.3107	1.3604	1.4115	1.4641	1.5180	1.5735	1.6304	1.6889	1.7490	1.8106	1.8738	1.9387	2.0053	2.0736
5	1.2166	1.2762	1.3382	1.4025	1.4693	1.5386	1.6105	1.6850	1.7623	1.8424	1.9254	2.0113	2.1003	2.1924	2.2877	2.3863	2.4483
6	1.2653	1.3400	1.4185	1.5007	1.5868	1.6771	1.7715	1.8704	1.9738	2.0819	2.1949	2.3130	2.4363	2.5651	2.6995	2.8397	2.9859
7	1.3159	1.4071	1.5036	1.6058	1.7138	1.8280	1.9487	2.0761	2.2106	2.3526	2.5022	2.6600	2.8262	3.0012	3.1854	3.3793	3.5831
8	1.3685	1.4774	1.5938	1.7181	1.8509	1.9925	2.1435	2.3045	2.4759	2.6584	2.8525	3.0590	3.2784	3.5114	3.7588	4.0213	4.2998
9	1.4233	1.5513	1.6894	1.8384	1.9990	2.1718	2.3579	2.5580	2.7730	3.0040	3.2519	3.5178	3.8029	4.1084	4.4354	4.7854	5.1597
10	1.4802	1.6288	1.7908	1.9671	2.1589	2.3673	2.5937	2.8394	3.1058	3.3945	3.7072	4.0455	4.4114	4.8068	5.2338	5.6946	6.1917
11	1.5394	1.7103	1.8982	2.1048	2.3316	2.5804	2.8531	3.1517	3.4785	3.8358	4.2262	4.6523	5.1172	5.6239	6.1759	6.7766	7.4300
12	1.6010	1.7958	2.0121	2.2521	2.5181	2.8126	3.1384	3.4984	3.8959	4.3345	4.8179	5.3502	5.9360	6.5800	7.2875	8.0642	8.9161
13	1.6650	1.8856	2.1329	2.4098	2.7196	3.0658	3.4522	3.8832	4.3634	4.8980	5.4924	6.1527	6.8857	7.6986	8.5993	9.5964	10.6993
14	1.7316	1.9799	2.2609	2.5785	2.9371	3.3417	3.7974	4.3104	4.8871	5.5347	6.2613	7.0757	7.9875	9.0074	10.1472	11.4197	12.8391
15	1.8009	2.0789	2.3965	2.7590	3.1721	3.6424	4.1772	4.7845	5.4735	6.2542	7.1379	8.1370	9.2655	10.5387	11.9737	13.5895	15.4070
16	1.8729	2.1828	2.5403	2.9521	3.4259	3.9703	4.5949	5.3108	6.1303	7.0673	8.1372	9.3576	10.7480	12.3303	14.1290	16.1715	18.4884
17	1.9479	2.2920	2.6927	3.1588	3.7000	4.3276	5.0544	5.8950	6.8660	7.9860	9.2764	10.7612	12.4676	14.4264	16.6722	19.2441	22.1861
18	2.0258	2.4066	2.8543	3.3799	3.9960	4.7171	5.5599	6.5435	7.6899	9.0242	10.5751	12.3754	14.4625	16.8789	19.6732	22.9005	26.6233
19	2.1068	2.5269	3.0255	3.6165	4.3157	5.1416	6.1159	7.2633	8.6127	10.1974	12.0556	14.2317	16.7765	19.7483	23.2144	27.2516	31.9479
20	2.1911	2.6532	3.2071	3.8696	4.6609	5.6044	6.7274	8.0623	9.6462	11.5230	13.7434	16.3665	19.4607	23.1055	27.3930	32.4294	38.3375
25	2.6658	3.3863	4.2918	5.4274	6.8484	8.6230	10.8347	13.5854	17.0000	21.2305	26.4619	32.9189	40.8742	50.6578	62.6686	77.3880	95.3962
30	3.2433	4.3219	5.7434	7.6122	10.0626	13.2676	17.4494	22.8922	29.9599	39.1158	50.9501	66.2117	85.8498	111.0646	143.3706	184.6752	237.3762
35	3.9460	5.5160	7.6860	10.6765	14.7853	20.4139	28.1024	38.5748	52.7996	72.0685	98.1001	133.1755	180.3140	243.5034	327.9972	440.7005	590.6681
40	4.8010	7.0399	10.2857	14.9744	21.7245	31.4094	45.2592	65.0008	93.0509	132.7815	188.8834	267.8635	378.7211	533.8686	750.3782	1051.6674	1469.7713

goals and objectives, because saving allocates money for the future that will allow a person to obtain both wants and needs. For example, money saved may be used to purchase real estate, pay for an education, or provide money for retirement.

Saving money for emergencies can strengthen a financial plan. Saving can make money available for unexpected expenses, such as car repairs and medical expenses, or for periods when no income is received. Being able to pay for emergencies with savings, instead of rearranging a budget or borrowing money and paying interest, allows a financial plan to continue uninterrupted. A good rule of thumb is to try to have enough money saved for emergencies to cover three months of normal spending.

The most important reason for saving money is to earn interest. In savings, the money is not only being allocated for the future but is also earning interest and growing. As more money is saved, more money becomes available through interest to be used to reach financial goals.

Saving needs to be done on a regular basis, no matter how small the amount set aside. Money received from allowances or a part time job can be placed in a savings account. Forming a habit of saving money can make more money available for investing on a larger scale. It is very important to be consistent. The amount placed in a savings account each time a deposit is made is not nearly as important as establishing a habit of saving. If possible, a good amount to set aside is 10 percent of net income.

Methods of Saving and Investing Money

A variety of different methods of saving and investing money exist. They vary by the amount of risk associated with each one. Saving money can be done by putting money in an insured savings account, buying certificates of deposit, or investing in annuities or U.S. savings bonds; little or no risk is associated with these options. More risk is associated with investing money in bonds, mutual funds, or stock.

Insured savings account - Insured saving accounts are available through banks, savings and loans, credit unions, and other financial institutions. An insured savings account can be started with a small amount of money, which earns interest and is readily available if needed for an emergency or other investments. Interest rates are lower than with other methods of saving and investing, but deposits under $100,000 are insured by the government.

Certificates of deposit - Certificates of deposit (CDs) are available through banks and some other financial institutions. They are issued for different amounts (the minimum is generally $500 or $1,000) and for different lengths of time. Money invested in certificates of deposit is not as readily available as money invested in saving accounts, since penalties are assessed for early withdrawal of the money. However, CDs earn higher rates of interest: the longer the period of time until a CD's maturity, the higher its interest rate. Certificates of deposit are insured by the government.

Annuities - An annuity is very similar to a certificate of deposit, but it is issued by an insurance company rather than a bank. They almost always pay higher interest than CDs. A penalty is assessed for early withdrawl of the money invested.

U.S. savings bonds - Savings bonds are available through most financial institutions; many companies also offer payroll deduction plans for purchasing them. The bond is purchased at an amount less than face value and grows to the face value at the maturity date specified on the bond. Interest rates are lower than those of other bonds, but the money is guaranteed by the government. Purchasing U.S. saving bonds is a good method of supporting the government.

Treasury bonds - Treasury bonds are issued by the U.S. Treasury Department. They are available in amounts from $1,000 to $1 million and mature after periods of 30 days up to 5 years. Treasury bonds are riskier than savings bonds because they fluctuate in value depending on interest rates if sold before they reach maturity. Bonds issued by the treasury generally have better interest rates than either savings accounts or savings bonds. Again, the longer the time to maturity, the greater the interest rate.

Bonds - Bonds are issued through corporations (corporate bonds) and local governments (municipal bonds). Bonds are certificates of debt that promise payment of interest on specified dates and payment of the original investment upon maturity. Interest rates are higher than those for savings accounts or savings bonds, but bonds involve more risk, because their value depends upon the financial well-being of the corporation or agency issuing the bond.

Mutual funds - Mutual funds are diversified investments that are managed professionally. Mutual funds involve investments in several different companies. They allow individual investors to pool their money to meet various investment objectives. Mutual funds are listed in many newspapers, where the price listed is the cost of one share of the fund. The amount that the share increases or decreases from the original purchase price is the amount gained or lost on the investment. While the potential for large returns exists, earnings are not guaranteed.

Futures - Futures contracts are contracts for the purchase and sale of commodities for future delivery. They are traded on the commodities exchanges. Speculating on the futures market by buying and selling contracts is risky. Speculators may not make a profit and may even lose their original investment.

Stock - Stocks represent a share of ownership in a company. The price of the share may increase or decrease, depending on the success of the company, and the amount of change is equal to the amount of profit or loss. Stock prices may be found in newspapers. Stocks are traded on the New York Stock Exchange and the American Stock Exchange. Buying stock is a risky investment, and while careful management of stocks can have financial rewards, losses may be just as large.

As indicated above, the level of interest or returns on investments depends on the type of savings plan or investment. The higher the risk is, the greater the potential return. While investing money in an insured savings account has no risk, the interest paid is low compared to the returns from other options. In contrast, stock is very risky, with no guarantee of receiving a return or even getting back the original investment; however, rewards are also potentially much greater.

Developing a Savings and Investment Program

Like the rest of the financial plan, choosing how to save and invest money requires careful thought and planning. Most plans consist of gradually building an investment program. A good start would be to open an insured savings account and then consistently deposit money in the account to earn interest.

As the amount of money in a savings account increases, the next step is to diversify. Diversification is the reduction of risk through the spreading of dollars among several different types of savings and investments, such as savings accounts, certificates of deposit, and stocks or bonds. The first step in diversification might be to purchase a certificate of deposit or a savings bond, which have greater rates of return than a savings account. As they mature, this money could be used to purchase stocks in hopes of generating even higher returns. A diversified savings and investment plan brings in additional profits while leaving some money readily available in savings for emergencies or unexpected expenses.

Diversification can also be done by purchasing mutual funds. Because mutual funds are by nature diversified investments, they provide many alternatives for investors and many different opportunities for profit. Dividends are usually automatically reinvested in the fund to generate more returns. A ready market for selling mutual funds exists if the money is needed for emergencies or unexpected expenses.

Summary

The time value of money is an important concept to remember when developing a savings and investment plan. A dollar received today is not equal in value to a dollar received in the future, because today's dollar can produce returns that are worth more than the original dollar. Saving money is important not only because additional money can be earned through interest payments but also because money will be needed to meet future goals and objectives and may be needed for emergencies. Many different methods of saving and investing money may be used to generate additional income, but a good savings and investment plan starts with placing money in an insured savings account and builds gradually into a diversified investment program.

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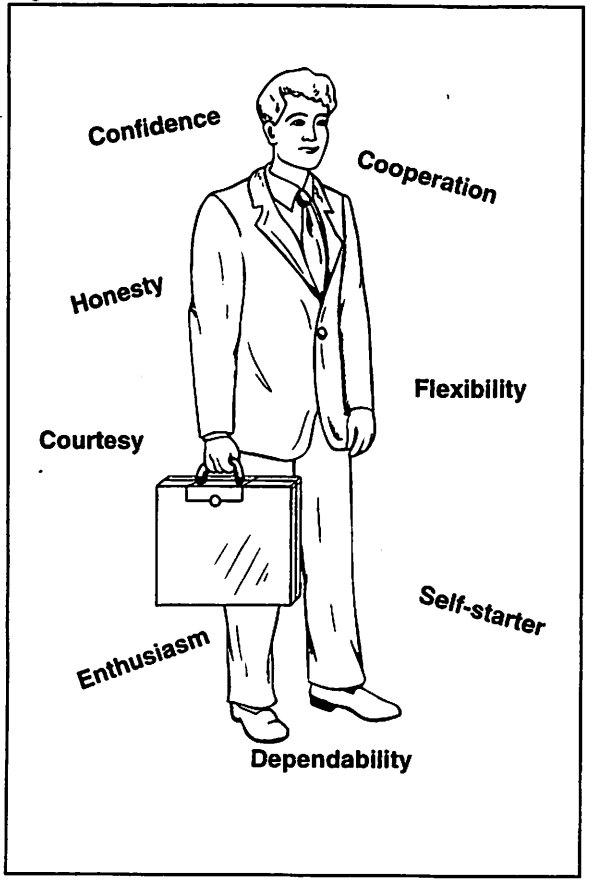
Lesson 1:
Developing a Positive Work Attitude

In order to succeed on the job, an individual must have the right attitude. An employee who displays a poor attitude toward the job and his or her coworkers is not likely to advance in a career. People often lose their jobs not because they are unable to do the work required, but because they have a negative attitude. Therefore, all employees should work on developing a positive work attitude.

Positive Work Attitude

Whether or not an individual has a positive work attitude can be determined by examining the behavior he or she displays in the workplace. A positive attitude is revealed through a combination of many traits (Figure 1.1). An employee must work on developing these traits until a positive attitude becomes a state of mind.

Figure 1.1 - Traits of a Positive Work Attitude



- Confidence - People with a positive attitude believe in their ability to do the job well. This self-confidence leads them to try to do their best in the workplace. They also have confidence in the abilities of coworkers and encourage them to do their best as well.

- Self-starter - Self-starters display initiative by doing things without being told. Self-starters learn to work well with a minimum of supervision. They use all available opportunities to learn more about assigned responsibilities and are always willing to take on additional ones. Accepting more responsibility indicates that an individual feels positive about the work that he or she is doing.

- Cooperation - The ability to cooperate with others allows an employee to get along with bosses and coworkers. Cooperation includes following the rules and procedures established by a business. A cooperative person is willing to consider the ideas of others and to help them whenever possible.

- Courtesy - Like cooperation, courtesy improves relationships with other people in the workplace. Being polite to others, showing respect for them, speaking to them in a pleasant voice, and expressing appreciation for their time and effort are all behaviors that mark a positive work attitude.

- Dependability - Following instructions, being punctual and consistent in attendance, and completing tasks on time demonstrate that a person is dependable.

- Honesty - Being truthful when giving information, keeping promises, handling company money wisely, and not wasting time on the job are all traits of an honest person.

- Flexibility - Technology and competition have made it necessary for many businesses to make changes in the way they do business. Employees who have a positive attitude are willing to learn new procedures and information and cheerfully accept change. They know that changes bring new opportunities for growth, both for themselves and the company.

- Enthusiasm - Enthusiasm is the sum of all the other aspects of a positive attitude. It is expressed through an obvious enjoyment in

being at work. Sharing an enthusiasm for work with others can spread feelings of fellowship and pride throughout a business organization.

The Importance of a Positive Work Attitude

A positive work attitude is important to be successful in a career. Being confident, a self-starter, cooperative, courteous, dependable, honest, flexible, and enthusiastic creates the opportunity for advancement. If a person examines and constantly works to improve his or her attitude toward a job, he or she will be able to appreciate the job more. A sincere appreciation for the work will encourage that individual to add to his or her knowledge and skills and become a greater asset to the business. An employee who is a valuable asset is more likely to be promoted. Companies promote employees who display a positive attitude toward their jobs not only because they are always trying to improve their performance, but also because these employees spread their positive attitude to others in the company.

Developing a Positive Work Attitude

Obviously, developing a positive work attitude is necessary for success. Choosing the right career is closely connected to a positive attitude. While an individual should always display a positive attitude toward any job, being positive is easier when a career is satisfying. If a job is not fulfilling, it is that much harder to build and maintain a positive attitude.

An employee can work to improve his or her attitude. To develop a positive attitude, find people in the workplace who display the traits discussed in this lesson. Spend some time observing their behavior, and try to imitate it. Also, try to build self-confidence; have faith in your ability to do well on the job. Finally, work on improving the traits and behaviors associated with a positive work attitude. If you do not see yourself as a self-starter, for example, take the initiative and learn more about the job. Whenever mistakes are made, treat them as an opportunity to learn and become a better worker.

Perhaps the most important aspect of a positive attitude to develop is enthusiasm, because it is so contagious. Enthusiasm shown by one worker can spread through an entire organization, but a lack of enthusiasm can spread just as rapidly. Feeling and displaying enthusiasm about a job every minute of every day is a hard, if not impossible, task. Take every opportunity to smile and look for positive things that can turn a bad day into a good one. Go out to a favorite place for lunch, or find someone else who is having a bad day and try to improve his or her attitude. Efforts to increase another person's enthusiasm often have a positive effect on both people involved.

Developing a positive work attitude is far from an easy task. It takes commitment to develop it fully. However, a positive work attitude brings rewards that make it worthwhile--not only success on the job, but also a feeling of self-satisfaction.

Summary

A positive work attitude is necessary to be successful in a career. Being confident, a self-starter, cooperative, courteous, dependable, honest, flexible, and enthusiastic are all part of a positive attitude. On the job, employees must cultivate a positive attitude as a state of mind.

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Lesson 2:
Positive Workplace Relationships

Part of developing a positive workplace attitude is learning to cooperate with others in the business organization. Cooperation involves being able to work with everyone, including superiors and coworkers with diverse backgrounds, attitudes, and opinions. Following an old but still meaningful guideline for behavior--"Do unto others as you would have them do unto you"--can help people work together effectively. If positive relationships are maintained, working as a team to reach the goals of the business is possible.

Positive Relationships with Bosses

In maintaining a positive relationship with the boss, it helps to remember that his or her function is to help others complete the tasks of the organization. In the final analysis, nobody ever really works for anyone else. Instead, everyone does his or her individual part to complete the overall task. If one person does not complete his or her part of a team effort, the product or service cannot be provided. The boss's task is to help all the people of the organization work better. The boss is the worker who links together all the individual tasks and workers necessary to produce the final product. He or she solves problems that may stop or slow down the process of producing a product or offering a service to the customer. The boss helps people work more efficiently, so that the entire organization benefits.

An employee must realize that an orderly system must exist within the organization in order to bring all the tasks of a business together. A positive relationship with the boss includes respecting and following the lines of authority or chain of command. These terms refer to the order in which different positions are ranked within an organization by level of authority. If a problem exists or he or she needs guidance to complete a task, an employee should follow the lines of authority by communicating first with immediate supervisors. An employee can display respect for superiors by following rules and regulations, showing up for work on time, and working to make changes take place smoothly. He or she should also concentrate on completing tasks correctly. Finally, an employee should solve problems rather than create them. Following these guidelines will maintain order within the business and help everyone, including the boss, complete individual tasks and the overall task of the organization.

Communicating properly with the boss when problems that require his or her attention arise will help build a positive relationship. An employee should discuss problems in terms that can be measured or observed rather than in terms of personal attitudes or feelings. Employees should also discuss desired outcomes instead of simply complaining about problems. An employee should not simply complain that a problem exists and dwell on his or her feelings about the situation. Instead, he or she should state that a problem exists and give reasons for the problem that can be addressed by the boss. Giving the boss honest and complete information about problems will also help maintain a positive relationship.

Positive Relationships With Coworkers

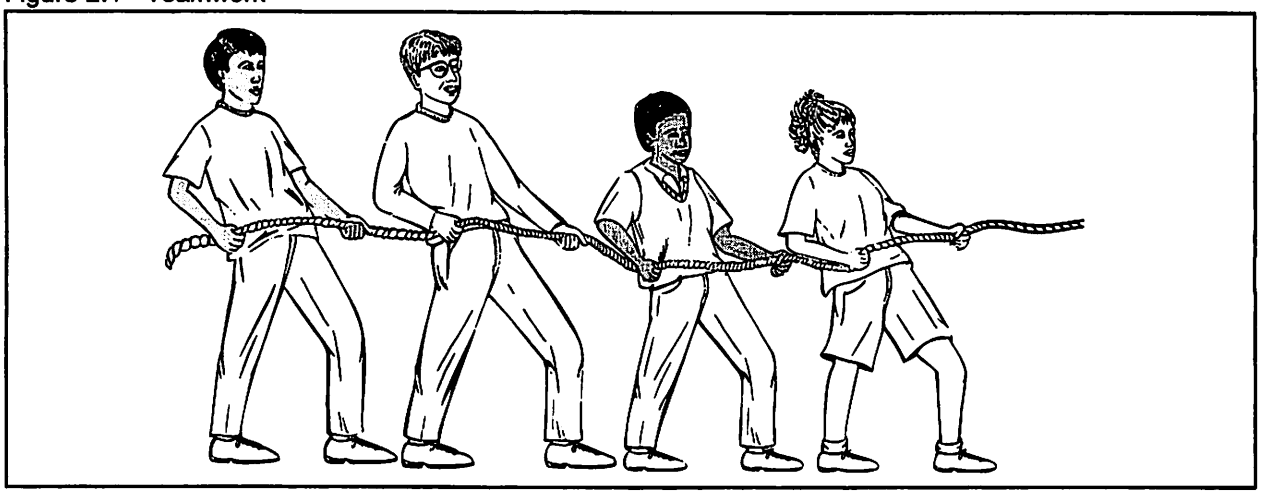
One way for an individual to maintain a positive relationship with coworkers is to do his or her share of the work. Most people are willing to help out if one of their coworkers needs some extra help getting the job done every once in awhile. However, they will become angry if they are constantly having to do someone else's work as well as their own.

Treating others considerately is also important in maintaining positive relationships. Employees need to respect the fact that coworkers will have different personalities, behavior, beliefs, and opinions. They need to tolerate these differences. Even if they do not always agree with coworkers, they must try to understand and accept other perspectives when disagreements occur. Showing consideration for others also involves making compromises to resolve disagreements.

Working as a Team Member

The word team can refer to different combinations of people and even animals, but the concept of a team is always the same--a group working together to accomplish some task. Sports provide many good examples of group effort and teamwork. On a softball team, for instance, the individual effort of one member of a team may produce a base hit, but once the player is on first base he or she needs others to make hits to advance to score a run. The player also needs a coach to help him or her hit, field, or run the bases better. The player's individual

Figure 2.1 - Teamwork



effort is useless without the help of the coach and the other players needed to complete the task.

Teamwork is needed on the job so that workers can combine their individual efforts together to achieve a common goal. A worker needs to understand that even though other workers have differences, it is necessary for them to be unified as a team. Even if a person puts forth his or her best individual effort, that effort is useless without the efforts of the other members of the team. The final result is more important than the separate tasks involved in making a product or offering a service.

Successful team members share several important traits.

- They work hard to do their part to contribute to the success of the team. They strive for excellence even when a task seems unpleasant.
- They share their ideas with others if they believe that they will help the team to be successful.
- They concentrate on finding solutions to problems facing the team rather than on the problems themselves. Focusing on the problem may simply contribute to it.
- They accept the decisions made by others, whether the decision is made by the team as a whole or by a manager.
- They take interest in what the other members of the team are doing. They provide encouragement and praise for their efforts.
- When the team succeeds, they take personal pride in that success. When the team is not successful, good team members are willing to take responsibility for their actions if they have contributed to the problem.

It is important to remember that in some cases not everyone on a team has a positive work attitude or team spirit. Good team members understand that some people may not put forth a winning effort for the team. Since they see everyone on the team as a potential winner, team players do not accept defeat. They work even harder to make everyone a winner!

Summary

Teamwork is important for the success of a business organization. A team member understands that he or she works for himself or herself as well as the business and that individual efforts must be combined with the efforts of others to offer a product or service. Maintaining positive relationships with bosses and coworkers is important in completing the goal of the entire organization.

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Lesson 3: Criticism

Criticism, if given and taken correctly, can be a valuable tool for workers and managers. A person who cannot give constructive criticism limits his or her abilities to instruct others. A person who does not take criticism well is limited to his or her own ideas and insights.

Types of Criticism

Only two types of criticism exist--criticism that is constructive and criticism that is not. People who do not successfully learn the skill of giving and taking constructive criticism severely limit their ability to instruct and learn. The difference between constructive and nonconstructive criticism is whether or not an explanation of the corrective action required is included. Nonconstructive criticism only identifies the problem; it does not suggest a solution. Constructive criticism identifies the problem and gives instructions for solving it.

For example, suppose Bill has volunteered to be an assistant coach of a local Little League team. At practice, he asks a pitcher to throw him a curve ball. The pitcher did not throw the ball correctly. Bill could respond with nonconstructive criticism: "Are you sleeping out there? I asked for a curve ball, and that wasn't it. Now throw me a ball that curves." This type of criticism does not attempt to determine the cause of the problem or explain how to fix it. It is simply a demand for improvement. If the pitcher does not know how to improve, however, the quality of the pitch is not going to change, and he may resent Bill's unreasonable demands. The pitcher may become angry or just give up trying to improve if the nonconstructive criticism continues.

If Bill uses constructive criticism, he is much more likely to achieve a positive result. Suppose that instead of simply offering criticism, he gives instructions and a demonstration of how to do the pitch properly. Saying, "To pitch a curve ball, you need to spread your fingers over the seams of the ball, like this," Bill demonstrates the proper positioning and watches as the pitcher attempts to imitate him, ready to offer suggestions if needed. Bill takes the pitcher through the rest of the pitch and gives further instructions to improve his delivery. Although the pitcher still needs practice, he at least has the basics down due to Bill's use of constructive criticism.

Understanding the Value of Constructive Criticism

Nonconstructive criticism rarely corrects a problem. It often ends up hurting the person being criticized. In a work environment, the bad feelings created by nonconstructive criticism can have a negative impact on a business. In contrast, constructive criticism is a valuable tool that can be used positively to improve the way a business operates. Understanding the value of constructive criticism is crucial for both employees and management because criticism serves several vital functions.

Using constructive criticism effectively allows a business to meet the goals of operating productively and efficiently. Because no one is perfect, at some time or another everyone will make mistakes on the job. If those mistakes are not corrected, the employee will most likely make them time and time again. This situation could damage the productivity of the business. When criticism is given and taken correctly, however, it can improve the business's productivity, because problems are resolved much more easily.

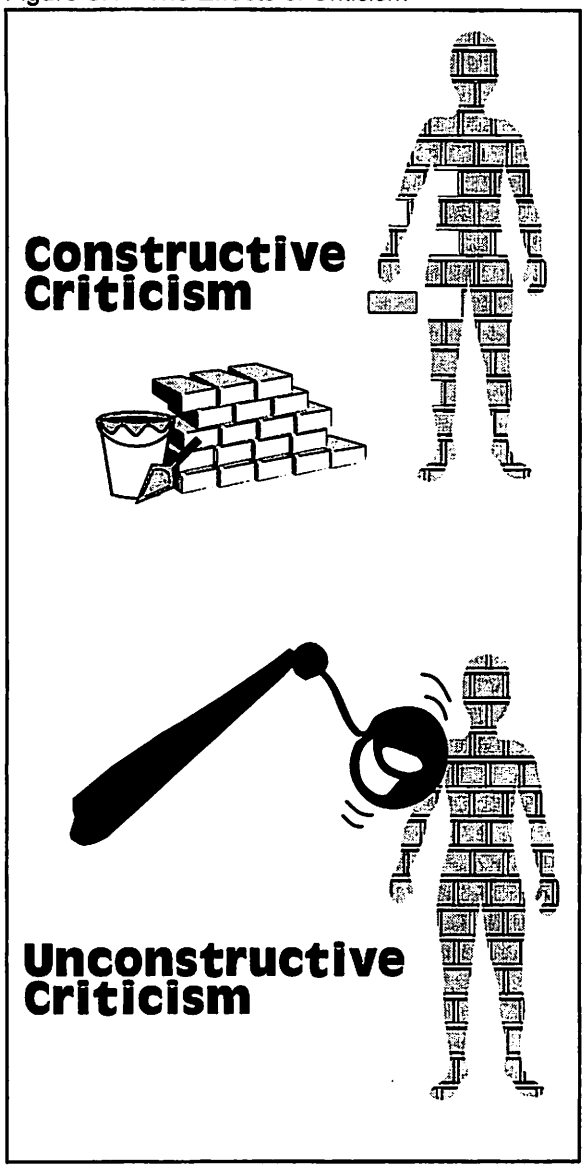
Constructive criticism can help an employee improve his or her job performance. It can be a valuable tool in helping employees become more productive, competent, and valuable. Constructive criticism, which includes giving instructions, allows them to learn more about their jobs. Employees need to remember that criticism is not a personal attack but a way for them to become better at doing their jobs.

A proper use of criticism can improve employee morale. Constructive criticism allows the person being criticized to maintain a more positive attitude about the situation, because he or she is addressed with respect. Instead of simply receiving negative comments about his or her performance, the employee is approached as if he or she can improve, and a means for improvement is offered through instructions and demonstrations. Constructive criticism is supportive rather than destructive. It builds up instead of tearing down.

Receiving Criticism

Everyone can expect criticism on the job. No one is perfect, and mistakes will be made. Handling

Figure 3.1 - The Effects of Criticism



criticism positively when it is received is therefore very important.

Maintaining control over his or her reaction is very important in helping an employee who is being criticized to handle criticism effectively. Criticism is often given in the spirit of helpfulness, and an employee should keep this in mind and listen carefully to the message being given in the criticism. Part of a boss's responsibility is to point out the mistakes an employee makes and to conduct a periodic review of an employee's strengths and weaknesses. In either of these situations, an employee should always show respect for the boss. He or she should listen closely in order to understand the problem and instructions for correcting the problem. Making excuses and being offended by criticism will not solve the problem but will instead limit an employee's ability to implement a solution. Only when the problem is identified can plans be made to correct the situation, which is the final step in receiving criticism effectively.

Since constructive criticism includes giving instructions, employees must know how to take instruction. Listening closely to instructions is necessary so that each step of the whole task is understood. Asking questions can help employees clarify any part of the task that they do not understand. After instructions are given, an employee must follow the instructions and finish the task correctly. If the task cannot be completed correctly for some reason, a person should never be afraid to ask for help. Asking for help can prevent a major mistake (and additional criticism) from being made.

Unfortunately, not all criticism is constructive, but no matter how the criticism is delivered, it can be valuable. Remember that first fall when learning to ride a bike? Riding the bicycle might cause some pain, but most people do not blame the bicycle. Instead, they get back up on the bicycle and try to do better so that it does not happen again. The pain of nonconstructive criticism needs to be dealt with in the same way.

In spite of how criticism is given, employees should think about the message behind the criticism rather than defending themselves. Employees can turn nonconstructive criticism into constructive criticism by meeting it with a positive attitude. They should assure the person giving the criticism that they regret what has happened and are committed to doing better. Then they should ask questions about how to resolve the problem. For example, if a boss tells an employee that he or she needs to become a better team player but offers no instructions about how to put this suggestion into practice, the employee has to ask for specifics. If for some reason no instructions are given, even in response to questions, employees have to find out for themselves what needs to be done to resolve the problem.

Giving Criticism

Many people have special skills. Someone may be able to throw a baseball, cook a meal, drive a car, or complete a task on the job better than others.

Because of this difference in skills, just as everyone can expect to be criticized, everyone is likely to do the criticizing at some point. When criticizing someone else, keep in mind that the way criticism is given can affect how the other person accepts it. Constructive criticism is always tactfully given and is designed to be helpful to the listener. Criticism that is not constructive is sometimes malicious and often causes pain.

Criticism is a two-way street. Criticism is much easier to receive if it is given with the proper attitude. When the person giving the criticism is calm, courteous, and fair, the person taking the criticism finds it easier to listen, respect the person doing the criticizing, and value the criticism being given.

The following guidelines should be taken into consideration when criticizing others.

- Mention only those aspects of the problem that can be corrected by that person.
- Be clear about what is to be corrected.
- Emphasize how the person receiving the criticism will benefit from it. Most people want to know what they will gain from making the changes requested before they alter their behavior.
- Pick the right setting and time to give criticism. Criticizing someone in front of others can be very embarrassing for the person being criticized and can do more harm than good. Try to avoid giving criticism when the person being criticized is not prepared to listen or accept it--in the middle of a very stressful day, for example.
- Criticize the problem and not the person. Rather than attacking the employee directly (by saying that he or she is incompetent or lazy, for example), focus on the aspect of his or her performance that needs to be changed.
- Whenever possible, mention things that the person does correctly, in addition to the criticism.
- Speak in a positive tone.
- Demonstrate confidence in the person's ability to correct the problem. Allowing him or her another opportunity to do a task correctly is a good way to demonstrate confidence. Simply saying "I believe in you" can also demonstrate faith in the ability of others to do well.
- Look for signs that the listener is responding positively to the criticism. His or her body language, facial expressions, and eye contact can indicate whether or not the person being criticized is responding well. Look for signals that he or she understands the problem and feels supported in solving it.

Criticism without instruction is just a statement of the problem; it does not suggest how the problem can be resolved. To be able to criticize others constructively, a person must know how to give instructions. Understanding the problem and being able to visualize the steps that must be followed to correct it is necessary. The corrective procedure needs to be summarized as a step-by-step process, with each step being explained clearly. If certain steps are hard to understand, the steps should be repeated or demonstrated. After the steps are clearly explained, the listener should be asked if he or she had any questions. Questions must be answered clearly and directly. Reviewing the procedure by allowing the listener talk through or demonstrate the steps can test the results of the instructions.

Constructive criticism is an important tool that can help workers become better at what they do. However, employees should never perceive their boss as someone who is always looking to catch others doing something wrong. Although correcting problems as they happen is important, taking the time to *catch someone doing something right* is just as important. Praise lets people know that their efforts are appreciated and encourages them to continue. A little praise for something done well helps an employee feel good about his or her job.

Summary

Nonconstructive criticism can be damaging. Constructive criticism, however, is a valuable tool, since it can lead to improvements in productivity, employee performance, and morale. Dealing with criticism, whether it is constructive or nonconstructive, is an important part of improving on the job and becoming a better employee. People criticizing others should always be careful to be constructive in their criticism. Respect is important; people being criticized always need to show respect

for the speaker, and people giving criticism need to respect the person they are criticizing.

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Lesson 4:
Ethical Behavior in the Workplace

Ethical behavior in the workplace is a very important part of personal development. A business is not likely to survive if employees do not act ethically.

Work Ethics

In general, ethics are a set of values that establish a standard for judging right and wrong. Ethical considerations govern the way people interact in society. Most people agree, for example, that taking something that belongs to another person is wrong. These shared values make living together in a civilized society possible.

Work ethics are principles of right conduct as accepted by a profession or by the business world in general. Some ethical behaviors are of concern in any area of business, such as fulfilling the terms of contracts. Others are of concern to a particular profession, such as the medical profession. Ethical standards serve two main functions: to communicate the ideals of the profession and to serve as a general guide for professional conduct.

An individual business may have a formal written code of ethics that establishes certain rules and practices to govern day-to-day operations. Managers and employees can apply this code if they are unsure whether some act is ethical. In order for a code to be effective, it must apply to all members of an organization and be put into practice on a daily basis. The business must also enforce its code of ethics by punishing violations. If guidelines are met, however, a code of ethics can provide a foundation for ethical behavior for everyone employed by the business.

Work ethics serve an important function for the business world. They make it possible for businesses to prosper, because consumers are more likely to do business with organizations they trust and respect. In the short run, disregarding ethical standards can benefit a business. It may profit as long as no one discovers the unethical practices, but if such practices become common knowledge or if consumers even suspect that they are occurring, public distrust can ruin the business. If you suspected that a business was misleading or defrauding customers or endangering its employees or the public, would you purchase its product or service?

Ethical Behavior

What is ethical behavior? While everyone has personal ethical standards that are reflected in his or her actions, decisions, and values, individual codes of ethics can conflict. Some areas of public debate arise out of these conflicting values. Personal ethical codes also may not help an individual determine what ethical behavior in the workplace is, because the code of ethics he or she has developed may not seem adequate to deal with the complexities of business. In either case, what is ethical is often not clear; ethical versus unethical may not be black and white. Ethical dilemmas arise from these gray areas.

Obviously, if a business has a written code of ethics or clearly follows unwritten standards of professional conduct, an employee should base his or her behavior on them. If it does not, however, he or she should try to determine what is ethical by following certain guidelines.

- Ethical behavior is legal. If an action is legal, it conforms to a set of written laws. However, ethics go beyond written laws to set moral standards for behavior. For instance, the law can outline what constitutes truth (and deceit) in advertising, but it cannot make lying itself illegal. People accept that lying is generally wrong because of ethical codes. The law, therefore, provides the minimum standard for determining ethical behavior. An action that is illegal is also unethical, but unethical actions may not always be illegal.

- Conduct is ethical if it enhances self-respect. When making an ethical decision, it may help to consider whether a certain course of action would be followed by a person of good character. If not, that action is not likely to be ethical. Ethical behavior triggers self-respect, a feeling that an individual is a "good person." An inability to face oneself is an indicator that an action is wrong.

- Ethical behavior develops personal integrity. It enhances personal growth by conforming to moral rules. Even if they do not follow them, most people know the moral standards that are generally accepted by society. Moral rules prohibit murder, theft, cheating, and lying,

among many other actions. If an act violates one of these moral rules, it is unethical.

- Ethical conduct involves taking the needs of other people into consideration. An activity that is harmful to others is usually unethical. When faced with an ethical dilemma, a member of a business organization should attempt to look beyond his or her own or the business's interests and consider the interests of those people who will be affected by his or her decision--coworkers, consumers, other businesses, or society as a whole.

- Conduct that is ethical builds confidence in others. In the workplace, when all workers follow principles of right conduct, everyone can work together with a feeling of security. They know what behavior they can expect from others, which improves the relationships between coworkers. Ethical conduct also builds confidence in the general public. In sales, for example, ethical behavior forms a basis for long-term customer relationships.

When attempting to decide whether an action is ethical, thinking about the problem is important. Ethical dilemmas generally cannot be resolved both quickly and well. If an ethical decision must be made rapidly, keep in mind that a choice is probably unethical if it seems wrong or is likely to be criticized by others.

Ethical Behavior and Job Performance

If a person is caught acting unethically, his or her career can be damaged. In very serious offenses, unethical behavior can result in the offender being fired, facing legal charges, and enduring public disgrace. An unethical individual might have sanctions imposed on him or her by the business itself for less serious offenses. Some unethical actions (like betraying the trust of coworkers) might never be overtly acknowledged within the business but may keep an employee from being singled out for special recognition or promotion. Finally, once a person gains a reputation for acting unethically, regaining the trust of others may be difficult or even impossible.

Ethical behavior may not always be rewarded, but it is an essential part of good job performance and creates the potential for advancement. Organizations promote employees who are assets to the organization, because managers want their behavior to spread to others. Most businesses want managers to have especially high standards of ethics, since the management guides overall business activities and sets the standard for other employees to emulate. Employees who are upright in character and respect themselves enough to act ethically inspire respect in others. Ethical employees build good relationships with customers and within the organization itself. Businesses value workers with these qualities.

Summary

Work ethics are principles of right conduct as accepted by a profession or by the business world in general. Making ethical choices is not always easy; what is ethical may not be clear. If a business has a written code of ethics, employees should follow it. If not, individuals can determine whether conduct is ethical by looking at whether it is legal, enhances self-respect, develops personal integrity, takes the needs of others into consideration, and builds confidence in others. While behavior that is unethical may not always be punished, ethical behavior is a part of good job performance and creates opportunities for advancement.

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Lesson 5:
Managing Time Effectively

Managing time effectively is a valuable skill. To achieve all the tasks associated with a job, employees often have to be able to manage their own use of time. Otherwise, the job may not be finished or may be done poorly.

The Purpose of Goal Setting

A goal is an outcome toward which a person directs his or her efforts. Goals are reached through objectives, which are the steps that are followed to achieve the goal.

Goal-setting fulfills several purposes. Goals are important in time-management because it is impossible to make choices about the best use of time if activities have no focus. Goals also give life purpose, preventing an individual from drifting aimlessly from one activity to the next.

Setting up a goal allows an employee to divide a project into manageable parts in order to manage time effectively. The objectives allow time and energy to be focused on a particular step that needs to be accomplished. The objectives can then be used to evaluate the progress that is being made toward reaching the desired goal. This evaluation may cause a person to change the objectives that will be needed to reach a goal.

Developing Goals

The process of setting goals is not difficult, although careful consideration needs to be given to exactly what the goals and objectives should be. The process is outlined below.

1. The first step in developing goals is making sure that the goal is truly what is desired. A goal is more likely to be achieved when a person is committed to reaching it.

2. The next step is to make a short statement describing the goal. The statement should include what is to be accomplished, what may have already been accomplished, and resources that may be needed to help reach the goal. For example, a goal for a retail agribusiness might be to achieve a ten percent increase in sales for the upcoming month. The statement might be "I plan on achieving a ten percent increase in sales by increasing advertising by two percent and extending the hours that the business is open."

3. Carefully consider the steps necessary to achieve the goal.

4. Develop a plan of action. This plan is a detailed outline of the short-range objectives necessary to complete the goal. For example, to reach the stated goal of increasing sales by increasing advertising by two percent, an objective might be to run a special ad to promote sale items. The plan is not completed until the goal is reached.

5. Put the plan into action.

6. The plan needs to be reread periodically to measure the progress that has been made. Rereading the plan will also help an individual determine if his or her present performance will meet the goal.

When setting up a plan of action, goals may be either short-range or long-range goals. In some cases, short-range goals need to be linked to long-range goals. The objective that an individual is trying to accomplish right now may be connected to the goals for the day, week, month, and year, until all short- and long-range goals are linked together to form a lifetime goal. Career planning provides an example of an area in which short-range goals (doing well on an important test) might be linked to long-range goals (graduating from a good technical school) to achieve the lifetime goal of success in a particular career. The short-range goals need to be completed in order to complete the long-range goals.

A well-developed goal has several important characteristics. It should always be clearly stated, which is part of the reason why it should be written down. The goal has to be achievable, and a way to measure achievement needs to be written into the goal. Therefore, when possible, it should be written in quantifiable terms (a *10 percent* increase in sales, for example). A goal must also have a realistic deadline for its completion. Finally, a goal must be flexible enough to take into account changing circumstances.

Prioritizing Goals

Since an individual is likely to be trying to achieve several goals at the same time, prioritizing goals becomes necessary. Several factors need to be considered when prioritizing goals.

Workers are hired to solve problems. They may be employed to produce, promote, or sell a product or service. Some problems are solved by simply pushing the right button, running the right advertisement, or calling the right person, but others take planning to reach the goal of solving the problem. The goals of the entire organization need to be considered first, since personal work goals should be based on responsibility and accountability. A worker needs to understand his or her responsibilities and coordinate his or her goals with the supervisor's and organization's goals. An employee prioritizes goals by taking into account the kind of work that needs to be done to achieve the company's goals. In sales, for example, a company may place a priority on making sure all current customers are taken care of before new accounts are developed. The salesperson's personal work goals may be to call on all the established customers during the first three weeks of the month and then call on possible new accounts during the last week of the month. The goals of the organization must be considered before the salesperson develops additional goals.

Goal setting involves stating what one would like to happen. A problem exists with a goal when what is actually happening is not what is desired. If a problem occurs, it may be necessary to consider prioritizing goals. If a student's semester goal was to get an "A" in algebra, but today's test grade turns out to be a "B", the student's objectives need to be prioritized to reach the desired results. A new objective to reach the desired goal of an "A" may be to cut back on hours spent watching television, playing sports, or working at a part-time job to allow more time to study algebra.

In many cases, goals are prioritized by a natural chain of events. If a career is being planned, a person may need to achieve goals for completing algebra, a term paper, and other high school course work before the goal of graduating from high school. Graduating from high school comes before going to college or trade school, and completing college or trade school comes before preparing a resume and applying for jobs.

When prioritizing goals on a daily basis, one thing to consider is the importance or urgency of the activity involved. Urgent tasks are things that have to be done immediately. They may or may not be important. Important tasks are ones that have long-range consequences. Goals can be prioritized by looking at their relative urgency and importance. For example, if something is both important and urgent, it should take priority over another activity that is also important, but not urgent.

Time Management

Time management is an important factor in accomplishing goals. It can take very little time to get big results if goals and objectives are set, evaluated, and adjusted. The goal of getting an "A" in algebra can be accomplished by planning time during the school term to study every chapter, time to study for a test, and time to get help when information is not understood. Waiting until the night before the final to study is not managing time effectively.

While putting together a weekly time management plan is beneficial, daily time management planning is essential to make the best possible use of time. When setting up a time management system, list and prioritize current goals. Make a list of the objectives that must be completed to reach each goal, and prioritize them. Relate the tasks for the day to the objectives, and then prioritize the tasks on the basis of the goals and objectives. Set up a schedule for completing the tasks, focusing on the ones with the highest priority. Priority tasks should be scheduled for personal peak energy periods--the times that an individual has the most energy. When allotting time for a task, plan using the minimum time necessary to complete a task. The best time for daily planning is at the end of the previous day.

Completing a project or solving a problem without a plan is possible, but it becomes much more difficult to know whether progress is being made. Setting goals helps people to focus on managing their time to achieve a desired end.

Tools for Time Management

Employers today are looking for people who can act effectively to meet goals. Individuals who learn to manage time are able to meet their goals more efficiently than people who do not. Different tools are available to assist in time management.

The simplest of these tools is a list, which is used to set priorities and rank projects or objectives by their importance. The list should include everything that needs to be accomplished, prioritized from the most important to the least important. Each day new items will be added as others are completed and taken off the list; the list must be revised daily to account for these new activities and priorities.

A personal planner is a more specialized time management tool. The planner acts as a type of "action plan" that organizes objectives and goals to be completed. Personal planners contain information on daily, weekly, and monthly agendas, priorities, and finances. They also may contain important personal and business telephone numbers and addresses. Planners can help an individual make time work for them by helping him or her focus on what is important.

The National FFA Organization has a personal planner designed just for high school students. It has a calendar for recording assignments and due dates as well as other important activities. The planner also contains information about FFA, goal-setting and time management tips, and a study guide section.

Summary

To manage time effectively, an employee of a business needs to set up a plan. The most important part of a time management plan is developing goals. Goals are simply an outcome toward which a person directs his or her efforts. Clear and measurable objectives that outline the necessary steps to achieve these goals also need to be set up. Goals may be prioritized according to a natural chain of events, to target problem areas, to satisfy organizational goals, or by relative urgency and importance.

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Lesson 6:
Developing Stress Management Techniques

Sometimes the fast pace of life takes its toll by causing various degrees of stress. Stress can serve a useful purpose by stimulating people's efforts and pushing them to set high standards. However, excessive stress can lead to the development of mental or physical stress disorders. Unless certain preventive measures are taken, stress can accumulate to cause mental or physical breakdowns. People experiencing stress can utilize several techniques to help them manage stress.

Indicators of Excessive Stress

Life inevitably brings problems. Sources of stress include school, work, sports activities, and parents, bosses, or other sources of authority. The way that people feel mentally or emotionally can sometimes affect the way their bodies function. They can feel just as unwell from mental or emotional problems as from physical causes.

In some cases, stress is self-perpetuating. An individual's values and way of looking at things may cause him or her more stress than another person might experience under the same circumstances. A person who suffers from stress is likely to take things more seriously than people who do not. Receiving a "B" on an algebra test may be a very stressful situation to a student who expects perfection.

Stress is sometimes linked to feelings of anxiety, fear distress, guilt, or shame. Excessive stress may be indicated by the following signs.

1. Insomnia
2. Dysfunctional eating habits, including eating too much or a lack of appetite
3. Panic attacks
4. Hyperventilation
5. Increased smoking or alcohol consumption
6. Abuse of prescription or nonprescription drugs
7. Headaches
8. Muscle spasms and soreness
9. Jaw problems caused by clenching or grinding the teeth
10. Cold and canker sores
11. Skin disorders, including itchy or painful rashes and outbreaks of acne
12. Digestive tract problems, the most serious of which are ulcers
13. Chest pain
14. High blood pressure (hypertension), which can be worsened by stress and cause damage to the kidneys or, in serious cases, strokes
15. "Blahs" or "blues" ("blahs" refers to a lack of interest in life, while "blues" refers to a sense of sadness
16. Depression

One of the more serious reactions to stress is depression. Recognizing stressful conditions is generally not hard, but recognizing depression may not be easy. Just as there are many degrees of stress, many degrees of depression also exist. The degree of depression may depend on whether the depression is recognized and how it is handled. Some signs of depression are listed below.

1. Loss of interest in school, work, friends, or activities, which may include not wanting to talk to friends on the phone or, in some cases, isolating oneself and avoiding encounters with friends entirely
2. Difficulty sleeping, interrupted sleep, or sleeping more than usual
3. Loss of interest in food, personal care, and grooming
4. Unplanned gain or loss of weight in a short period of time
5. A feeling of unhappiness that lasts longer than six weeks
6. Suicidal thoughts
7. Pattern of increased carelessness that may cause accidents while walking or driving
8. Poor self image and feelings of worthlessness
9. Blowing up frequently and easily over minor matters that never really were a bother before
10. Loss of energy, sometimes causing an inability to make decisions
11. Feelings of confusion and an inability to concentrate

Many people feel "down" from time to time, but the "blahs" or "blues" are usually passing phases. Identifying where these feelings end and serious depression begins is sometimes very hard. Knowing the signs of depression is important, because it is not a simple condition. Skilled medical and psychological help as well as support from family and friends may be needed to treat it.

Causes of Stress in the Workplace

Many factors can cause stress in the workplace. A job that is undemanding or boring can be just as stressful as one that involves too much responsibility. Most on-the-job stress comes from the gap between the demands of the work and what can reasonably be achieved. Another source of stress is the difference between an individual's desires or expectations for advancement and recognition and what he or she achieves or receives as a reward. A third cause of stress is personality conflicts with other employees or supervisors. Stress may also be the result of a physical illness or problems outside the workplace that make it difficult to concentrate on the job.

Stress Management

One thing that can help individuals deal with stress is being more flexible in their approach to life. No one can eliminate stress entirely, but some stressors (factors that create stress) can be avoided. For instance, if a person's schedule is already full, he or she must learn to say "no" when asked to take an additional task. If stressful situations cannot be avoided, altering one's attitude toward them may be possible. Bend rather than break when confronted by stressors. The stress felt by the student mentioned in the example on the preceding page might have been alleviated if he or she tried to accept that perfection might not always be possible.

In many cases of stress, the circumstances involved are such that preventing stress may not be possible, so stress needs to be managed. Attention should be concentrated on coping with stress at the lowest possible cost to one's health. A variety of techniques can be used to manage stress.

One way of dealing with stress is through some sort of physical relaxation technique, such as deep-breathing exercises or muscle relaxation. In deep-breathing exercises, concentrate on taking slow, deep breaths, which have a calming effect. Stress can also be alleviated by alternately tensing and releasing muscle groups, since forcing muscles to contract automatically triggers their relaxation, allowing muscles that have been unconsciously tightened due to stress to relax. Even simply dropping a clenched jaw and relaxing tensed facial muscles can have a positive effect, but for more complete relaxation, this technique can be practiced on the muscle groups of the entire body from forehead to feet.

Mental relaxation techniques like meditation and visualization can be used as well. Meditation involves clearing the mind of stressful thoughts. Instead of dwelling on those things that might cause stress, focus on one relaxing thought or word for a significant length of time--at least twenty minutes. If meditation seems too difficult, one alternative is visualization. Visualization involves using imagination to focus thoughts in a particular direction. When using visualization, imagine a pleasant scene, one that is associated with peace or comfort. Then place yourself in that scene, imagining what you would be thinking or feeling. Let the scene gradually fade away while retaining the feelings that it triggers.

Efficient time management, which was discussed in Lesson 5, can be another way to reduce stress. Since stress is often caused by feeling weighed down by demands, eliminating those things that waste time can significantly relieve stress. To see if your time may be spent more effectively, review your activities, including how long they take, how stressful they are, and how valuable they are. Eliminate activities that cost more in terms of time and stress than they are worth. Also, concentrate on one day at a time, focusing on what needs to be done that day rather than what lies ahead.

Stress can be managed by focusing on other areas in life. Part of managing stress is engaging in diverse activities and interests, especially leisure activities, and living a balanced lifestyle that includes both work and play. People who keep all their eggs in one basket are much more at risk than those whose lives contain many interests. When stress becomes excessive, manage it by engaging in some sort of leisure activity. Reducing stress may mean taking a walk in the park, or a drive in the country, watching a good movie, being with a good friend, or whatever else helps an individual relieve stress. After relaxing, a person can generally return to a stressful situation with a new attitude.

If people are able to talk about their problems out with parents, teachers, friends, or partners, their stress level is often decreased. Support from family and friends can be especially important in alleviating stress. Make sure to keep these relationships strong so that emotional support will be available if needed.

Humor can be used to reduce stress. Even the simple act of smiling seems to have a beneficial effect, while laughter has been linked to a reduction

in body chemicals associated with stress. To alleviate stress, try to find the humor in everyday situations and problems. Take the time to seek out those things that make you laugh--watch a funny movie or television show, for example.

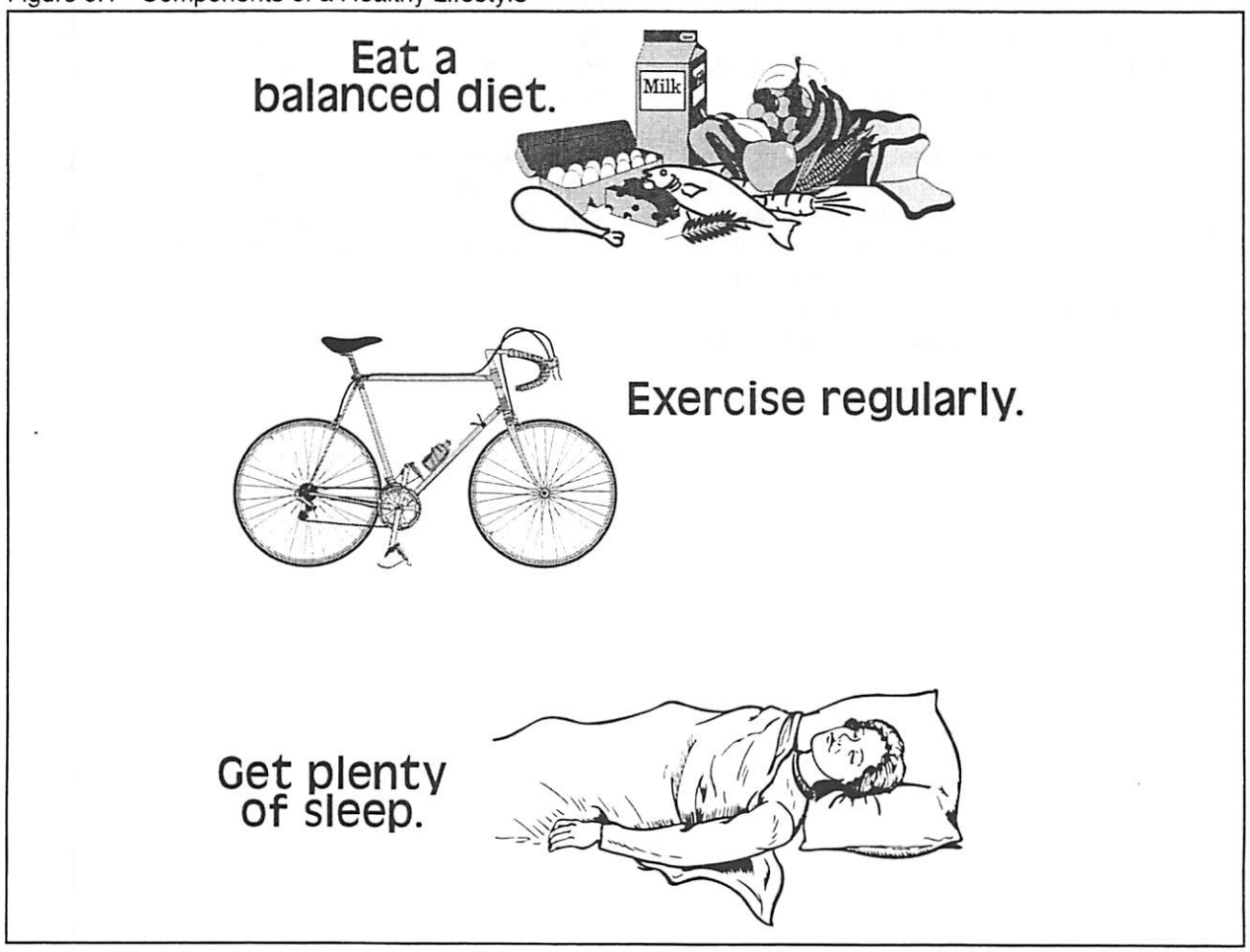
When an individual experiences repeated bouts of stress or depression, he or she should get professional help from a therapist or support group rather than simply trying to cope with it. People go to a doctor to help relieve the symptoms and pain of a physical illness. The same should be true for severe emotional or mental illness. People are not weak or at fault if they experience this type of illness; generally, nothing can be done to stop it from happening. Severe emotional or mental illness needs to be treated like any other illness or disease.

Maintaining a Healthy Lifestyle

While the techniques mentioned in the previous section can alleviate stress, eating properly, exercising, and getting enough sleep can not only reduce the effects of stress but also improve a person's health. If a person does not follow these recommendations for diet, exercise, and sleep, stress can take a greater toll on his or her system.

A balanced diet high in complex carbohydrates and low in fats is important for health, especially since stress can aggravate problems such as high blood pressure that can be affected by diet. Daily nutritional recommendations from the USDA call for six to eleven servings of bread, cereals, rice, and pasta; three to five servings of vegetables; two to four servings of fruit; two to three servings of meat, poultry, fish, dry beans, eggs, and nuts; two to three servings of milk, yogurt, and cheese; and sparing use of fats, oils, and sweets. A diet high in complex carbohydrates (grains, potatoes, breads, rice) is beneficial because they release long-term energy. Foods that contain a lot of refined sugar can give a quick energy boost, but the resulting energy level will drop just as rapidly. Fats should be limited because they increase blood cholesterol levels linked to heart disease.

Figure 6.1 - Components of a Healthy Lifestyle



When meals are eaten also has an effect on health. Eating breakfast is very important. It provides energy for the body to operate in the morning when energy levels are depleted. Skipping any meal can lead to fatigue, headaches, and an inability to concentrate that can affect performance.

Exercise is another important part of a healthy lifestyle. Not only does exercise have obvious physical benefits, such as strengthening muscles (including the heart) and burning calories, but is also lowers anxiety levels, gives an increased feeling of personal control, and reduces the levels of hormones related to stress, all of which are important in countering the effects of stress. Everyone should perform some sort of aerobic (requiring a continuous supply of oxygen) exercise for 30 minutes three times a week, with proper warm-up and cool-down periods to reduce the chance of injury. Aerobic exercise includes such activities as running, swimming, dancing, and cycling; walking is a very effective form of aerobic exercise. If exercising for thirty minutes is not possible due to poor fitness, start by exercising for a shorter period and work up. The key to a good exercise program is moderation. Too much exercise can be as harmful as too little, since frequent exercise increases the risk of injury.

Getting enough sleep is the final component of a healthy lifestyle. If a person is suffering from a lack of sleep, he or she will display irritability, an inability to concentrate, and a diminished memory, all of which affect performance. While the amount of sleep required varies from person to person, most people need at least seven hours of sleep a night for the body to replenish itself. People under stress need even more sleep, since their bodies have more demands made on them.

Summary

Stress can be harmful because the way people feel mentally and emotionally can sometimes affect them physically. An individual may experience tension headaches, digestive disorders, high blood pressure, skin diseases, or other physical problems that are brought on by stress. Many techniques can be used to help alleviate the effects of stress. Proper diet, exercise, and sleep are important not only because they counteract the effects of stress, but also because they are essential to a healthy lifestyle.

Credits

Eliot, Robert S., M.D. *From Stress to Strength: How to Lighten Your Load and Save Your Life.* New York: Bantam, 1994.

Leatz, Christine A., M.S.W. *Career Success/Personal Stress: How to Stay Healthy in a High-Stress Environment.* New York: McGraw-Hill, 1993.

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Lesson 7:
Finding a Job

Determining which career to pursue and finding a job are two very different processes. Individuals must decide what career interests them. They must look into career opportunities and characteristics of different careers. After an individual has selected a career, he or she needs to find a job in that area.

Steps in Choosing a Career

Consider interests, abilities, and other characteristics. What are your hobbies and interests? Do you enjoy showing cattle, riding horses, or walking in the forest? What talents do you have? If you are artistic or enjoy public speaking, consider careers in which you could use these skills. What careers appeal to you? Think about friends or family members who work at jobs that seem interesting. In what courses in school did you do well? In what areas do you have experience or knowledge? Which of your physical characteristics may influence your decision? Some characteristics may limit career choices. If a person has poor eyesight, he or she is unlikely to become a professional umpire. If he or she has slow reflexes, being a jet fighter pilot would be difficult. Being a tree surgeon requires good arm strength to climb trees. An individual with many allergies may not want to work as a landscaper or gardener.

Take career interest or vocational aptitude tests. Most counselors or placement directors have access to these tests. The scores from these tests may indicate which skill areas are strong or weak. The Armed Services Vocational Aptitude Battery (ASVAB) is a commonly-used vocational aptitude test.

Narrow the field of career choices. When trying to choose a career, consider the following questions. Do you like to work with people or things? Do you like to work alone or with others? Do you want to work indoors or outdoors? Would you rather work with your hands or with ideas? What type of salary do you want? Do you want to live in a rural or urban location?

Study the characteristics of career choices. Compare the education or training required, work environment, salary range, expectations and duties of the job, and opportunities for advancement for different careers. The library, school counselor, or career center should have information about careers. Another good place to learn about careers is from people in that occupation. They are excellent sources of information that books may not provide.

Choose a career that matches personal interests. Based on the information gathered in the preceding steps, select careers that match personal interests. If a person enjoys working with animals, becoming an accountant would probably not be a good choice. If he or she likes working with numbers, being a veterinary technician probably would not be enjoyable. People are more likely to be successful in careers that they find interesting.

Plan for alternative occupations. Allow some room for choices in a career. Look at careers in related areas. If being a green keeper seems appealing, look at related areas such as grounds keeper, golf course superintendent, or a lawn service manager. Also, look at careers that require similar skills. For example, a tractor mechanic, welder, and computer repair technician all require good mechanical skills, but the career areas are quite different.

Plan for career preparation. Preparing for a career is important. The next section of this lesson will discuss career preparation in more detail.

Career Preparation

Career preparation can include the courses taken in high school, work experience, and any additional education. In high school, take courses that are interesting and explore a variety of subjects. The best time to look at career alternatives is in high school.

High school students can use several different strategies to gain work experience. The agriculture program provides excellent opportunities for real job experience through Supervised Agricultural Experience (SAE) programs. Another way students can gain experience is to take summer jobs in career areas that interest them. Students can also obtain experience through work-study programs and through unpaid observations. Unpaid observations may include accompanying a veterinarian or extension agent to observe the responsibilities of the job. Students should try to explore a variety of career opportunities while in high school.

When preparing for a career, students should plan for additional education or training beyond high school, if required. They can obtain training from vocational-technical schools, two- and four-year colleges and universities, or private technical schools.

Ways to Find Out About Available Jobs

Once an individual has prepared for a career, he or she is ready to find a job in that career area. Information about possible jobs can be found through many sources. The most obvious place may be the classified advertisement section of newspapers, which lists some of the job openings in the community. Both local newspapers and newspapers from surrounding cities or states can provide useful information about jobs. Magazines covering an area of interest may also contain classified advertisements for job openings. Magazines about the fruit production industry, for example, will have advertisements for orchard managers and other positions.

Personal contact with friends, family, teachers, etc., is an excellent way to find out about available jobs. They may know of job vacancies before the information is released to the public. Unless they are asked, however, personal contacts may not consider revealing job openings, so asking direct questions is important. Also, when talking with friends and family, practice active listening (listening closely and trying to understand completely what is being said). Even before the job search begins, friendly conversation may reveal a good opportunity for a job.

Job openings can be discovered by contacting private and public employment agencies and the businesses themselves. Private and public employment agencies will have information about jobs that are available. Some companies work exclusively through employment agencies. Also, check with businesses directly to find out about openings; ask about opportunities or just look at a placement bulletin board.

Either as a student or after graduation, check with the school placement office. Telling the placement person what types of jobs are of interest is important when visiting the office. He or she may know about job opportunities but may not mention them unless an interest is shown. Look on the placement board for current job listings as well. Some businesses simply post job information on the board. Meeting with recruiters who occasionally come through the office may be beneficial if a person has an interest in further education or the military.

A source of information about job openings across the nation is the Internet. Job search resources that allow an individual to search a database for a particular job title can be used as an aid in finding a job. People searching for jobs can also join an electronic bulletin board service to access its postings for employment. These services may be free or they may require users to pay a fee.

Applying for a Job

Certain steps are generally followed when applying for a job. First, the job applicant should prepare a resume to submit when applying and interviewing for jobs. The second step is to contact the employer about job opportunities. An individual may have many leads on possible jobs, but without contacting the business, he or she cannot know which jobs are still open. The next step is to fill out a job application. If the application passes inspection, the applicant may then get the opportunity to interview with the business. Finally, he or she should be sure to show a real interest in the job by following up after the interview rather than leaving the responsibility for making contact to the interviewer.

Job Inquiries

Once possible job openings have been identified, contact businesses about available jobs. Direct contact with the potential employer, telephone contact, or letters of inquiry can be used to inquire about jobs. The method used will vary depending upon the size of the community, the location of the business, and the position.

When pursuing a job in a small town, contacting the manager directly may be best. Direct contact involves going to the business and talking with the manager or personnel director about job opportunities. If the job is in a large metropolitan area with many businesses, speed up the process by inquiring by phone. If jobs are available, set up an appointment to meet with the managers. Calling for an appointment can be more convenient for the employer than the walk-in inquiry. Often, a letter of inquiry (see Figure 7.1) is appropriate. If the job opportunity would require long-distance travel, write to make sure a job is available before visiting in person. Sending a letter of inquiry may be more

Figure 7.1 - Letter of Inquiry

349 Monrovia Street
Littleton, Missouri 10005
May 5, 19--

Mark Eads
Service Manager
Jackson's Implements
220 Old Hwy. 47
Bigton, Missouri 66555

Dear Mr. Eads:

At the suggestion of my agricultural education instructor at Littleton High School, Mr. Tom Adams, I am writing to you regarding employment with your service department.

On June 4, I will graduate with a strong emphasis in agricultural mechanics. I have completed small engine repair, farm implement repair, welding, and electricity classes with a B+ average. In addition, I completed a computer course that covered spreadsheets, databases, and word processing. I also worked part-time at a small engine repair shop this past year, which enabled me to improve both my mechanical and people skills.

My resume with additional information is enclosed with this letter. Since I am planning a career in the agricultural mechanics field, I am eager to work for an implement dealer with a reputation like yours.

Please send application materials in the enclosed envelope for any positions for which I might be considered. I look forward to hearing from you.

Sincerely,

Janet Stewart

Enc: resume, envelope

appropriate when trying to obtain a supervisory or upper-level position.

Summary

Before beginning a job search, select a career area. Consider interests and abilities when selecting a career. After preparation for a job has been obtained, apply for a job. Job inquiries can be made over the phone, through the mail, or by direct contact. Then apply for the position using a cover letter, resume, and/or job application. A follow-up letter may be useful after making contact with a potential employer.

Credits

Harris, Clark Richard. *Leadership and Personal Development.* University of Missouri-Columbia: Instructional Materials Laboratory, 1991.

Lesson 8:
Resumes and Applications

A resume is a written summary of an individual's qualifications for employment. It is a very helpful tool when searching for a job. Resumes are given to prospective employers and may also be used as a source of information when completing applications for jobs, scholarships, awards, etc. The ability to complete an application properly is very important as well. Frequently, prospective employers will review an application when the applicant is not present. Therefore, it must be accurate and clearly written. A poorly written, sloppy application will be the first one thrown into the trash can.

Resumes

Although resumes may be set up differently, they should contain the same basic information. The information is usually presented as outlined below. Sample resumes are shown in Figure 8.1 and 8.2. The placement of information within the different sections of the resume may vary slightly. For example, the National FFA organization has a specific format for resumes that differs somewhat from the examples shown.

Personal information - This information should be listed first on a resume. It includes the individual's name, current address, and telephone number. If his or her current address is different from the permanent address (i.e., parents' address), then the second address should also be listed. The reason for including a permanent address is that many potential employers will keep resumes on file for job openings that appear later.

Employment objective - After the personal information, a brief statement of the employment objective, which indicates the type of job being sought, should be included. For example, an individual might have to find work as a wholesale salesperson. The objective should be specific to each job, which means that it will be changed each time a person applies for a different job. A specific objective lets an employer know that the applicant is interested in a particular job.

Educational background - In this section, list the most recent education first. Include dates, places, and degrees earned, as appropriate. If a degree has been earned from a college or technical school, high school information may be omitted. Any information about earning a certain degree should be listed here. For example, if a person earned a college degree financed completely (100%) or partially (70%) through scholarships and work experience, he or she should note this fact below the information about the degree to show an employer that the applicant is willing to work hard and take responsibility.

Work experience - List the most recent work experience with starting and ending dates first. If an individual is currently working, he or she should include the start date for the job followed by the words "to present." Include the company's name and address. If the job has a title, it should be listed, along with a brief but detailed description of the duties and responsibilities associated with it. This information will be used before the interview to make the initial decision about the applicant's qualifications for the job.

Other information - Headings such as "Activities," "Honors," "Awards," and "Skills," or a combination of these (e.g., "Honors and Activities") are appropriate. They should be organized with the most important items first. If the list is long, select only the most important. This list may vary for different jobs because some information may be more appropriate for one job than another.

References - At the end of the resume, type the heading "References" followed by either the references themselves or the phrase "Available upon request" if the resume does not have enought space to include them. If the resume says that references are available, make sure to have a typed list of references ready to give to the employer if he or she asks for them.

The reference list should have the word "References" centered at the top of the page and include the names, job titles, addresses, and telephone numbers of at least three people who have direct knowledge of the skills, work experience, and/or character of the person putting together the resume. People used as references should not be relatives of the applicant. Teachers can be good references, since they know about an individual's class work and sense of commitment and responsibility.

Professional and personal references should be listed separately. Professional references are given

Figure 8.1 - Resume (High School)

Tim Johnson
2288 South High Street
Anytown, MO 66444
(573) 555-1396

CAREER OBJECTIVE: To obtain employment in the field of horticulture.

EDUCATION:

Anytown High School, Anytown, MO
Projected graduation date: May, 1998
Grade point average: 3.4/4.0
Science and Horticulture emphasis

EXPERIENCE:

Anytown High School Anytown, MO Greenhouse Worker
Part-time greenhouse worker; assisted with daily plant care and transplanting.
9/96 to present

Kay's Landscaping Anytown, MO Landscaping Assistant
Part-time landscaping assistant; assisted with installation of trees, shrubs, perennials, and turfgrasses.
6/96 to 8/96

HONORS and ACTIVITIES:

Nursery/Landscaping contest team; secretary, FFA; honor roll, 2 years; 4-H member, 6 years; high school choir member

REFERENCES:

Gayle Smith	Kay Weber	Tom Richards
Agriculture Instructor	Owner	Principal
Anytown High School	Kay's Landscaping	Anytown High School
Anytown, MO 66444	Anytown, MO 66444	Anytown, MO 66444
(573) 555-1234	(573) 555-4444	(573) 555-1234

Figure 8.2 - Resume (College)

ELISA RIERA

PRESENT ADDRESS
1911 E. Walnut
Anytown, MO 66444
(573) 555-1233

PERMANENT ADDRESS
R.R. 3, Box 156
Othertown, MO 63437
(573) 555-1357

CAREER OBJECTIVE:

To obtain a position as a field manager for the Swine Products Department with Cargill, Inc. - Nutrena Feed division.

EDUCATION:

State University
Bachelor of Science in Agriculture, May 1996
Major: Agricultural Economics — Minor: Animal Science
GPA: 3.2/4.0 — Major GPA: 3.5/4.0
Financed 100% through scholarships and work experience.

EXPERIENCE:

Riera Custom Baling — Othertown, MO — Owner and Operator
Owner and operator of custom baling service producing 10,000 bales a year for various employers. This includes preparing, operating, and repairing the baler, and managing all present and future aspects of the enterprise. The tractor and baler are leased, and the annual maintenance expenses are shared. This operation has financed a major portion of my education expenses.
1993-Present

Riera Farms — Othertown, MO — Assistant Manager
Farm consists of 430 acres of grain and pasture production, a 250-sow farrow-to-finish operation, and a 280-ewe feeder lamb operation. Responsibilities include assisting with the planting and harvesting of the crops and management of the livestock. Personally involved in the daily decision-making process and management of the farm operations.
1990-Present

Bijou Restaurant — Othertown, MO — Server
Responsible for serving patrons of the establishment.
March 1992-June 1992

HONORS AND ACTIVITIES:

Little Sisters of the Pearls and Rubies-Secretary
National Agricultural Marketing Association
Alpha Zeta Academic Fraternity
College of Agriculture Scholarship
Andrew Benton Memorial Scholarship
Veronica Orris Scholarship
Daniel and Caroline Thornton Scholarship
MFA Foundation Scholarship
Diane Dent Scholarship
Department of Agricultural Economics Award for Scholastic Excellence
State University Dean's List

REFERENCES: Available upon request.

by people who have worked for or with the job applicant and can vouch for his or her abilities. Personal references are given by people who have known the applicant for an extended time and can vouch for his or her character. If possible, a separate reference page should be used for each type of reference.

Before using someone as a reference, contact that person and gain his or her permission. If possible, let the person know what the job is. Be selective when asking people to serve as references; make sure that they are able and willing to give a good reference. Asking a potential reference if he or she feels prepared to provide a good recommendation gives him or her a chance to consider that matter.

Resumes should be one or two pages in length. Try to keep a resume as short as possible; only include the most important information. For entry-level jobs, one page is enough. A resume should be longer than one page only if the amount of experience the individual has requires two pages. A resume should be neatly typed and sharp, clean copies should be made on good quality copy paper, perhaps colored and with a slight texture. Avoid extreme colors. Poor copies make a poor impression on potential employers.

Completing Job or Scholarship Applications

When completing a job or scholarship application, be as neat as possible. Type the application, or write neatly in black ink if the application must be completed at the site. Do not leave any blanks. If the application is not completed, the people reading it may wonder whether you did not understand the question, did not want to reply, or thought the question was not applicable. For questions that do not apply, fill in the blanks with "N/A" (not applicable).

The form should be completed accurately. Spell all words correctly; misspelled or scratched-out words quickly detract from the quality of the application. Follow the directions on the application. Read ahead before filling in the blanks. Do not assume that all forms are set up the same way. For example, assuming that the state and zip code are placed after the city in the personal information section would be a mistake if these items were to be included on a different line. Another common mistake is placing a first name in a blank asking for a last name.

Two strategies may help when filling out applications. If the application may be taken home, make a photocopy of the form and prepare a working copy. Then accurately transfer the information to the application that will be given to the company. A person searching for a job should also prepare a file that contains job application information, such as resumes, references, or any additional information that he or she may need, and carry when contacting any potential employer in person so that the information will be readily available to fill out applications. Such preparation expresses to the potential employer that the person is truly interested in a job and is an organized individual.

Applying for a Job

Once information about an opening has been obtained and a resume has been completed, begin the job application process. If possible, visit the business to obtain an application; fill out the application and send it to the company with a resume and cover letter. If a job application cannot be obtained, go ahead and send the cover letter and resume. Figure 8.3 shows an example of a cover letter.

The cover letter is a tool used to gain the interest of the potential employer. It should inform him or her of the qualities and skills that a person has that qualify him or her for the job. The letter should include several paragraphs that discuss where information about the job was obtained, why it is of interest, and what qualifies the applicant for the job. The applicant should also use the cover letter to request a job interview (or at least a personal call).

The initial paragraph of a letter of application should indicate the reason for writing, the specific position or type of work for which the writer is applying, and how he or she learned of the opening. The writer should refer to any previous conversation or correspondence.

In the second paragraph, the writer should mention why he or she is interested in the position, the organization, and its products or services. Above all, it should indicate what the applicant can do for the employer. A recent graduate might explain how his or her academic background qualifies him or her for the position. If he or she has had some practical work experience, the writer could point out specific achievements or unique qualifications. The letter

Figure 8.3 - Cover Letter

111 Deer Park
Any City, Missouri 10002
April 1, 19--

Andrew Smith
Personnel Director
Green Seed Company
222 Cunningham Road
Any City, Missouri 10001

Dear Mr. Smith:

This letter concerns the sales position that you have available in the Southwest Missouri territory. I discovered the opening through my school placement office.

The sales position is in my area of interest. Last summer I worked as an intern with Gail Ray, a sales representative for Dayton Seed. In this position, I found myself to be well qualified to be a sales representative in your field. I have also had extensive experience working with many people during my education, as president of my FFA Chapter and vice president of my senior class. These experiences helped me to develop leadership, organization, negotiation, and people skills.

Enclosed are my resume and a completed application. I believe that you will find my credentials qualify me for this sales position.

If possible, I would like to meet with you so that we can discuss the position available and my qualifications. I will contact you on April 10 to see if a personal meeting can be arranged. If you have any conflicts or questions, please contact me at (715) 555-6886.

Thank you for your consideration.

Sincerely,

Tim Jones

Enc: resume, application

should not repeat the information the reader will find in the resume.

In the third paragraph of a letter of application, the applicant should refer the reader to the enclosed resume or application that summarizes his or her qualifications, training, and experience. The writer may also make the employer aware that his or her credentials can be obtained from a College Placement Office. If both paragraphs are very short, the third paragraph of the letter can be combined with the second.

The closing paragraph should indicate a desire for a personal meeting. The applicant may want to suggest alternative dates and times or simply advise the other person that he or she is flexible regarding the time and place for an appointment. The writer should include his or her phone number in the letter and offer any assistance to help obtain a speedy response (such as calling on a certain date to set up the meeting). A sentence should be included asking if the contact person desires additional information or references.

The writer should use short but complete sentences and avoid unnecessary words throughout the letter. None of the paragraphs in the letter should exceed five sentences. The writer should avoid overusing the word "I." Many sentences can be reworded with a little effort. The letter will then sound more businesslike and flow more smoothly.

Summary

Resumes and applications represent the people completing them and must therefore be of good quality. Employers may decide to interview or hire a person based on the strength of a resume and an application. Scholarships often are awarded based on an application alone. By following the simple guidelines in this lesson, an individual can prepare good resumes and applications.

Credits

Harris, Richard Clark. *Leadership and Personal Development.* University of Missouri-Columbia: Instructional Materials Laboratory, 1991.

Lesson 9:
Interviewing for a Job

Applying and interviewing for jobs are very important skills. Once possible job openings have been identified, an applicant must sell himself or herself to the interviewer. The selling process begins with the resume and job application. They must be neat and make the interviewer want to talk to the job applicant. Giving the best interview possible is then vital. Frequently, the interview is an individual's only opportunity to impress a potential employer with his or her abilities.

Dressing for the Job Interview

When interviewing, appropriate attire is important. A suit is often worn for an interview, but the applicant should be familiar with the type of clothing worn on the job and wear at least what is expected for employees. If a person is applying for a job as an administrative assistant, shorts and a top would not be appropriate attire. On the other hand, wearing a suit to an interview as a grain elevator worker may not give the correct impression to the employer. Never wear clothes with holes, tears, or stains. Remember that a job applicant has only one chance to impress the interviewer and can always dress down later if the job requires more casual clothing.

Dress conservatively. A more conventional interviewer may not appreciate flashy or trendy clothes. One example of conservative dress is a plain white shirt or blouse, rather than a shirt or blouse that is flowered or has bold checks. Wear simple jewelry, if any, and a minimum of makeup. Bold jewelry or excessive makeup is distracting.

Wear polished shoes. Some interviewers will take note of shoes as an example of an applicant's normal appearance and attire.

Be neat and clean. An individual interviewing for a job should always look his or her best. Avoid stopping for gas on the day of the interview because of the lingering odor from the fuel. Also, avoid eating messy foods before or during the interview. Interviewing in stained clothing would be very embarrassing.

Hair should be neat and of an appropriate length. Loose, long hair may be unsafe for jobs around machinery. Men should be clean-shaven or have well-trimmed facial hair. A scraggly beard just makes an applicant look scruffier, not older.

Before Arriving for an Interview

One of the first things that a person should do before interviewing is to research the company. He or she might talk with friends who work there, call the business for information, or look up information at the library. It would not make a good impression to ask what type of work is done at a business. If a job applicant does not know what the company does, why would he or she want to work there?

Know what type of job is available. Knowledge of the specific job title is not necessary, but a general knowledge of the opening (whether the job is in sales, service, or management, for example) is important. When asked what position is desired, "Any job that is available" is not a good answer.

Knowing the interviewer's name and the correct way to pronounce it is also important. This information can easily be learned by calling the receptionist. Addressing the interviewer by the wrong name or mispronouncing his or her name is not a good way to start the interview.

Practice interviewing before going in for an interview. One opportunity for practice is a mock interview with a teacher or administrator. Expect constructive criticism. The whole reason for practicing is to improve interviewing skills. If the job applicant knows a businessperson, asking him or her to give a practice interview may be helpful.

Consider videotaping a practice interview. The interviewer should ask tough questions to aid in preparing good responses for the real interview. The video can provide insight into problems with voice, posture, appearance, and quality of responses. Engaging in several practice interviews would be even more beneficial, because watching the video between practices to look for areas that need improvement would be possible.

Bring a resume to the interview. It will be useful if the interviewer does not have his or her copy handy. The resume can also be a reminder for information such as dates of employment.

Bring a black ink pen to fill out additional forms and to take notes. They are recommended because

many businesses request that forms be completed in black ink.

Go to the interview alone. If friends come along, the job applicant does not appear to be serious about working. If another person drives the applicant to the interview, he or she should wait outside.

Arrive ten to fifteen minutes early in order to be relaxed for the interview. If the prospective employee is late for the interview, the interviewer may take it as an indication that he or she may be late on the job. If delays cannot be avoided, call the interviewer.

When driving to an interview, make sure the vehicle is clean inside and outside. Often, employers use the job applicant's vehicle as a measure of his or her personality. Drive carefully and within the speed limit on the way to the interview.

Being aware of major current events is helpful. The interviewer may talk about something that is happening locally or nationally. If the person being interviewed can contribute to the conversation, his or her knowledge creates an image of a well-rounded individual.

Pointers for the Interview

The first thing to remember is to make a good first impression. An interviewer will find it hard to overlook a poor impression. Remember that the first impression may be made as the job applicant drives up to the business or influenced by the way he or she acts in the lobby or halls while waiting for the interview. Since the interviewee may not always know who the interviewer is, he or she should always be careful to act appropriately.

Be prepared. Proper preparation includes doing research, practicing for the interview, and dressing appropriately. Preparation can be extremely important for a successful interview.

When greeting the interviewer, make sure to shake his or her hand. Give a firm handshake; do not grasp the interviewer's hand too tightly or too limply. A firm grip shows confidence.

Be polite, using good manners. Being courteous does not just apply to the interviewer, but to all the employees of the company. The receptionist, for example, may be asked what he or she thinks of the applicant.

Listen closely to what the interviewer is saying and respond when appropriate. Answer the interviewer's questions completely without talking too much. Knowing when enough has been said is important. A job applicant can sometimes talk himself or herself out of the job by giving too many details.

Be positive during the entire interview. Do not talk negatively about previous jobs or school. The interviewer will probably not hire a person who displays a negative attitude.

Maintain eye contact with the interviewer. Do not stare, but look at the interviewer when he or she is speaking. Making eye contact signals that a person is paying attention and is interested in what is being said.

Do not smoke or chew gum or tobacco before or during the interview. If a job applicant smokes on the way to an interview, his or her clothes may carry a lingering tobacco odor, which may be offensive to the interviewer.

The interviewer will usually ask if the person being interviewed has any questions, which is a good opportunity to ask a few questions. Make sure that the interviewer has not already addressed the questions.

Observe cues that the interview is ending, such as the interviewer straightening papers on the desk, asking for other questions, and pushing back his or her chair. As the interview draws to a close, give a short, positive closing statement. In making this statement, the applicant should be sincere about why he or she would like to work for the company or how he or she would fit into the company. This last statement may be what the interviewer remembers, and it may make the difference. Thank the interviewer for his or her time and shake hands before leaving.

Questions Asked During a Job Interview

Interviewers ask many different types of questions during job interviews. Planning the answers to some tough questions ahead of time is worthwhile.

"What qualities do you have that will help you in this job?" A possible answer would be, "I get along well with other people." However, since this is a value statement, it would be better to say, "I enjoy working with others." Giving examples of committees, teams, etc. would help elaborate on this answer.

"What are some of your faults?" Do not give a long list of shortcomings but focus on one or two areas for improvement. An appropriate response would be, "With my limited experience, I have a lot to learn."

"What are three adjectives that describe you?" Plan for this question by having a list of four or five adjectives prepared. Good responses include industrious, responsible, cooperative, efficient, loyal, and trustworthy. Be truthful because the interviewer may ask for a couple of examples that back up the adjectives used in the description.

"What do you want to be doing in five years?" Be careful when answering this question. If the person being interviewed says he or she wants to move up a step or two in the company, the person at that step may be doing the interviewing. If he or she expresses an interest in doing something else, the interviewer may give him or her that opportunity now. It is appropriate to express a desire to expand responsibilities and learn new skills to improve job performance.

"What have you done that makes you qualified for this job?" Do not be too boastful, but give some examples of past successes that demonstrate qualifications. Examples that reveal hard work and discipline are always appropriate.

"Why are you interested in working for our company?" This question helps interviewers decide if they want the interviewee to work for the company. It also tells the interviewer the applicant's reasons for wanting to work there. The prospective employee might point out that a friend or family member has the same job and it sounds very interesting or that he or she became interested in the career area when it was discussed in agriculture classes.

"What have you done that shows you can work with other people?" The job applicant might discuss activities that show how well he or she has worked with others. FFA provides numerous opportunities to demonstrate an ability to cooperate with others, such as committees, contest teams, leadership activities, etc. It is also helpful to include non-FFA examples such as sports, student council, 4-H, church youth group, or fair board. Do not get too carried away with the list of accomplishments, or it will seem like bragging. Include only the most significant achievements.

These questions may be difficult to answer without preparation, but they are all appropriate questions. Sometimes interviewers may ask questions that are inappropriate and illegal, however. Because of anti-discrimination laws, interviewers cannot ask questions about age, ethnic background, nationality, religion, disabilities, marital status, sexual orientation, political affiliation, and arrest record. The person conducting the interview may not know that the question is illegal. The job applicant may refuse to answer, or he or she may try to address the issue that prompted the question. For example, a question about marital status may arise from a concern about the applicant's ability to travel extensively. The prospective employee can also choose to answer the question.

Questions to Ask During a Job Interview

During an interview, the job applicant will probably be given an opportunity to ask some questions, and he or she should take advantage of it. Asking questions demonstrates an interest in the job and indicates that the interviewee is listening. Here are some examples of possible questions.

"What types of benefits are available?" Do not be too specific. Give the interviewer the opportunity to talk about the benefits. Ask a follow-up question for more details.

"What types of responsibilities will I be expected to fulfill?" Besides general job responsibilities, the answer to this question may hint at expectations to work overtime and nights or to take evening classes in the job area.

"What are the opportunities for advancement or expansion of responsibilities?" This question shows that the person being interviewed is interested in more than just a job. It indicates that he or she is interested in a long-term commitment.

"What type of wage or salary range can be expected?" While the answer to this question is obviously important, wait until the end of the interview to ask it. Asking earlier may give the impression that the applicant is only interested in the job for the money.

"When will the position be filled?" Most businesses will know when they plan to fill a position. Asking this question will give an idea of how long to wait before calling about the job.

Figure 9.1 - Follow-Up Letter

128 Kenelm Road
Casaton, Missouri 60003
June 8, 19--

Carol Miro
Personnel Manager
Clifton Corporation
42 Lawrence Street
Casaton, Missouri 60002

Dear Ms. Miro:

Thank you for giving me the opportunity to talk with you on June 7. The information you shared with me about the Clifton Corporation was very enlightening.

My experience and training in sales will be particularly valuable for this position. I am excited about the possibility of applying my education and experience to the position we discussed.

Thank you again for meeting with me. If I can provide you with any additional information, please contact me at (816) 200-0505. I look forward to hearing from you soon.

Sincerely,

Dave Holloway

After the Interview

If a job is offered after the interview, asking for time to consider the offer is generally acceptable. The amount of time will depend on the commitment involved. If it requires relocating or unusual conditions, more time may be needed to think it over. If it is a job at a local business for minimum wage, the prospective employee may want to accept it right away before the business interviews someone else. When taking time to think about a job offer, be sure both parties agree on the amount of time allowed.

The job applicant may have to take the initiative and contact the interviewer after their meeting. A follow-up letter should be written soon after the interview. If the interviewer does not make contact after the interview or respond to the follow-up letter within a reasonable length of time, the applicant should call to emphasize his or her continued interest in the position.

Follow-Up Letters

Sending a follow-up letter is appropriate after submitting a letter of application, making personal contact (in person or on the phone), or coming in for a job interview. This letter is a tool used to thank the potential employer for his or her time, express further interest in the job (or an interest in any future positions), and maintain contact with the potential employer. Many people do not bother to complete a follow-up letter, so writing one may give an individual an edge in obtaining the job. Figure 9.1 is an example of a follow-up letter.

When sending a follow-up letter after an interview, the job applicant should begin by thanking the interviewer for his or her time and mentioning the interview in the first paragraph. In the second paragraph, the applicant should restate his or her interest in the position and reemphasize a few of his or her qualifications. The third paragraph should include a final thank you and indicate where the person who was interviewed can be reached.

Summary

Once some possible job opportunities have been identified, an individual must go through the process of applying for the position. A very important part of this process is the interview. Be prepared by doing background research on the company, practicing the interview, dressing appropriately, and being familiar with questions the interviewer may ask and possible responses to them. Follow up after the interview.

Credits

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Lesson 1:
Verbal and Nonverbal Communication

Effective communication skills are an integral part of everyday life, as well as agribusiness sales and marketing. To be truly effective at communicating, one must know and understand the main components of communication, which involves verbal, nonverbal, and listening skills. This section will discuss these skills and how to use them to become an effective communicator.

Verbal Communication

Verbal communication is any form of communication that consists of either spoken or written words. In agribusiness sales and marketing, it will form the content of a presentation. The salesperson must always be sure that the words correctly express the message he or she is trying to send. Spoken or written words need to inform the customer about the product or service that the salesperson is providing and persuade him or her to purchase it. Verbal communication is used to supply the customer with technical information, facts about features or benefits, and information about problems or concerns about the product. Lesson 2 will discuss in detail the forms of written communication, such as letters, memos, flyers, and visual aids. This lesson will focus on the spoken word.

A person in sales and marketing will find that spoken communication is used on a daily basis to conduct business. It is therefore important to the salesperson and the customer that technical and product-related terms are accurately used. The words that the salesperson uses and the manner in which they are used are the foundation for a solid business relationship with customers. Jargon, slang, or industry terminology must be used carefully to avoid confusing the customer. An effective communicator makes sure that the customer understands these terms. If this is not so, an entire sales presentation may be wasted because the customer is not receiving the message the salesperson is trying to send. In addition, salespeople must ensure that they do not become too technical and discuss the product at a level the customer cannot understand. They should also avoid discussing it in very simple terms that insult the customer's intelligence. A salesperson can alienate, annoy, or lose the interest of the customer if he or she goes to either of these extremes.

Effective Listening Skills

Like good spoken communications skills, effective listening is a crucial part of the communication process (see Figure 1.1). A salesperson must not only be able to speak well but also cultivate his or her listening skills, which can be vital to picking up the information needed to make a sale. One key in closing a sale is listening carefully to the customer's needs, concerns, and acceptance of being "sold." The salesperson must probe for needs, so that he or she can match those needs with the appropriate benefit that the product or service can provide. Customer concerns must be identified and appropriately addressed. Careful listening can give the salesperson signals about when to close the sale. He or she should not attempt to close before meeting all the customer's needs and concerns. The salesperson also does not want to extend the sales presentation past the point that the customer decides to make a purchase, thus wasting both the customer's and his or her own time and possibly annoying the customer.

A salesperson with effective listening skills is more aware of the customer's listening skills and anything that might cause a distraction that might hinder making a sale. Any distraction may cause the message either to not be received or to be received inaccurately. Four types of distractions may build barriers to the listening process that can hinder effective communication.

One type of barrier is distractions from the surrounding environment, such as the temperature, noise level, or personal appearance of the speaker. When making a sales presentation, select a comfortable, quiet environment. This is the first step in ensuring that the listener will receive the correct message. In addition, the salesperson must always be aware of his or her appearance. Wearing something unusual can distract the listener. Outrageous clothing, jewelry, or hair styles can prevent the listener from concentrating on the subject of the salesperson's discussion.

Distance or space between the speaker and listener can also affect listening. Standing or sitting too close to listeners can make them uncomfortable, but being too far away will make it hard for them to hear and concentrate on what is said. An appropriate distance should be selected for each situation and maintained throughout the presentation.

Figure 1.1 - Keys to Effective Listening

KEYS	GOOD	BAD
1. Distractions	- Concentrates on subjects - Avoids distractions	- Lacks concentration - Distracted easily
2. Level of Interest	- Listens for opportunities, asking, "What can I gain from this?"	- Tunes out uninteresting subjects
3. Rate of Speech	- Anticipates, summarizes, and listens to tone for feeling and emotion	- Has mental lapses/ vacations/daydreams
4. Delivery of Presentation	- Overlooks delivery mistakes and focuses on content	- Distracted by poor delivery
5. Search for Ideas	- Finds overall ideas and themes	- Listens only to detail and fact
6. Difficult Subjects	- Recognizes the importance of difficult material in expanding knowledge	- Tunes out difficult material - Prefers easier, light information
7. Listening Actively	- Concentrates on listening - Gives feedback (verbal and non-verbal) - Shows enthusiasm	- Fakes attention - No feedback - Lacks enthusiasm
8. Emotional Content	- Does not react to emotional words or terms - Does not let it be a distraction	- Negative reaction to emotional words or terms
9. Note Taking	- Minimal, concise notes taken - Uses appropriate system for each presentation - Uses memory triggers	- Goes by memory only or takes extensive notes
10. Response and Evaluation	- Does not judge the speaker - Waits for the conclusion of presentation	- Looks for an argument - Jumps to early conclusions

Another barrier to effective listening is that the listener may not be physically or mentally prepared to be a good listener. In either case, the customer does not have the energy to be an effective listener. The salesperson should postpone the presentation, if possible; if not, then he or she must give special attention to the way the presentation is made. The salesperson may want to write down more things for the customer than he or she normally would.

The last barrier to effective listening consists of content distractions, which include bias for or against a subject, unfamiliar terminology, poor organization, and poor delivery.

- Bias for or against the subject can hinder effective listening. A bias is the opinion or feeling the listener already has about the subject. A customer may have a bias about the subject that colors how he or she perceives that subject and distracts him or her from the salesperson's message. The salesperson must strongly emphasize the facts about a product to overcome bias against it.

- Terminology can distract the listener if he or she does not understand the terms used. If the salesperson uses complicated or new industry terminology, customers may not be familiar with these words. They may take a mental "vacation," trying to figure out what that term means, or they may become annoyed. Either way, the customer is no longer listening carefully to the presentation.

- A disorganized presentation can confuse a listener, clouding the message the salesperson is trying to convey. The presentation should flow logically so the customer may follow it more easily. The salesperson also wants to organize information in a manner that will be interesting to the customer in order to keep his or her attention.

- Delivery consists of a combination of the terminology used, rate of speech, tone of voice, and nonverbal elements (i.e., hand gestures, facial expressions, and body language). The delivery can keep the attention of the listener if it is well planned. However, poor delivery can distract the listener from the content of the presentation.

Being able to give and receive feedback is an important part of effective listening. It can be vital in making a sale. When the salesperson is listening, he or she should give feedback to the customer by nodding, commenting to reaffirm ideas (such as "Yes," "I understand"), and rephrasing the customer's idea to make sure they are on the same wavelength. While talking, the sales representative should look for these same signs from the customer. The most important aspect is to confirm that the customer has received the correct message. If a customer does not attempt to rephrase what has been said, the salesperson should try to get him or her to ask questions or make comments to see if he or she understood the message.

Nonverbal Communication

Nonverbal communication is anything other than the spoken or written word used in the communication process to convey a message from sender to receiver. Forms of nonverbal communication include facial expressions, gestures, body language, dress, rate of speech, tone of voice, and eye contact. Nonverbal communication may help or hinder communication, depending on the manner in which it is used.

Facial expressions include a smile or frown, raising an eyebrow, or wrinkling the forehead, to name only a few. Gestures are motions made with the body, such as placing a hand on a hip, clenching a fist, or moving the hands while speaking. Some examples of body language are posture, stance, and body position (i.e., leaning forward or back). Dress refers to the care with which a person dresses and the appropriateness of his or her dress. Rate of speech is the speed (quickly or slowly) at which the words are spoken. Tone of voice is the pitch at which words are spoken (e.g., shrill, monotone, loud, or soft). Eye contact refers to looking someone in the eye instead of looking down or off into the distance.

Nonverbal Communication Skills and Sales

Nonverbal communication is a large part of the communication process. The salesperson can use a knowledge of nonverbal communication in two ways: to reinforce his or her own message in order to influence the customer or to interpret the customer's attitude. Nonverbal communication by the salesperson can affect the message sent to the customer in both positive and negative ways. Salespeople need to use it to help convey knowledge, confidence, enthusiasm, and sincerity to the customer, all of which may be vital in closing the sale. Nonverbal communication by the customer is

also important. If a customer shows definite positive signs of interest (nodding, smiling, making eye contact, leaning forward) during the sales presentation, his or her behavior may be an indicator of receptivity to the close of the sale. If the customer shows little or no sign of interest (tapping fingers, turning away, leaning back, frowning, avoiding eye contact) then the salesperson may not have identified the customer's needs and the benefits of the product or service correctly. However, the customer may also simply be having a bad day. At this point, the salesperson can reevaluate the approach used in the presentation or its timing to try to avoid losing a sale.

Facial expressions reveal feelings. For example, raising the eyebrows may mean surprise or interest, while a furrowed brow may show concern or a bad mood. A smile generally shows acceptance, while a frown indicates disapproval or disbelief.

Gestures may be used to emphasize the points of a presentation; they may also reveal attitudes. In making a presentation, the salesperson should use hand gestures, especially when emphasizing specific points. Salespeople must be careful not to be overzealous in the use of hand gestures because they may seem too flamboyant or out of control. Controlled, specific, yet natural gestures are usually the best. Gestures also can help a person read someone's attitudes and feelings. For example, a hand on the chin or side of the face usually expresses thought, whereas tapping the fingers shows boredom or impatience. Clenched fists are a sign of anger or frustration, and crossing the arms is usually a defensive move.

Body language can also show a person's level of interest in a subject. Leaning forward generally expresses interest, but leaning back shows limited interest or the need to separate oneself from the subject. Good posture conveys confidence, whereas slouching may indicate that a person is tired, frustrated, or lacking confidence.

The way a person dresses can communicate his or her attitude. For example, dressing sloppily for a business meeting can indicate a lack of respect for the other person. Overdressing can make the other person feel inferior.

Rate of speech is especially important to the salesperson. The appropriate speed makes the presentation interesting and easy to understand. Talking too slowly allows the customer to become uninterested and easily distracted, while talking too rapidly makes it hard for the customer to grasp the main points of the presentation. It is also important to pay attention to the rate of speech of the customer because it can indicate his or her level of interest and attention. If the customer speaks slowly, his or her interest level may be low. The salesperson must then try to increase interest in the product.

Tone of voice can greatly affect how a message being sent or received is interpreted. For example, a monotone voice indicates little interest in or excitement about the subject, even if the content of the words suggests otherwise. Moderate fluctuations in the voice can stress important points, directing a listener's attention to them. A loud voice suggests confidence, excitability, or great interest, while a soft voice implies a lack of confidence, timidity, or little interest in the subject.

Eye contact is *vital* to good communication. Eye contact or a lack of it reveals the level of trust, confidence, and honesty of the people involved in the communications process. Common wisdom says, "You can't trust someone with shifty eyes." Most people share this perception. If they are going to have a relationship of any kind with another person, they want to be able to look him or her in the eye so they can feel that they have established a level of trust. Remember, however, that looking someone in the eye does not mean "staring down" the person. Good eye contact is consistent, not constant.

The salesperson should always keep in mind that while he or she is using nonverbal cues to "read" what the customer is thinking or feeling, the customer is reading him or her in the same way. Therefore, salespeople must always be conscious of what they are doing and how the customer may perceive these things. The nonverbal skills that a salesperson uses will have a huge impact on the message the customer receives and the image he or she forms of the salesperson.

No single nonverbal sign should be taken as an absolute. The salesperson must observe all of the signs and listen to what the customer says to figure out the appropriate message. For example, imagine that a seed company salesperson is talking to a customer about a new hybrid line that the company is going to have available for the next planting season. Samantha found Joe, a farmer, working on equipment in an unheated shed. As Samantha is

talking, she notices that Joe has crossed his arms. She has to consider the possibility that Joe is not open to the idea of being a trial farm for the new hybrid seed. If this were the case, Samantha might need to go back and try to find weak areas in her presentation before trying to resell the seed to Joe. However, she had noticed earlier that the shed was unheated. When Joe crosses his arms, Samantha must decide if he is truly not interested in the new hybrid or is simply cold and trying to stay warm. To make this decision, she must obtain some verbal feedback from Joe to find out if he is having a problem with the product. Depending on Joe's response, it may become evident that he is just cold.

Summary

A person must develop communication skills to be successful as a sales representative. Verbal, listening, and nonverbal skills are the most powerful tools a salesperson will use in his or her career. Salespeople must be able to write and speak correctly, listen well and identify any distractions to listening, and recognize and use nonverbal communication.

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Lesson 2: Written Communication Skills in Agribusiness

Verbal communication consists of both spoken and written communication. Written communication skills are used frequently in the sales process and can be very effective if utilized properly. Several forms of written communication are used in the sales process. This lesson will discuss the different forms of written communication, their importance, and how to write an effective business letter and memorandum (memo).

Forms of Written Communication

Written communications used in agribusiness take several forms. The more commonly used forms are letters and memos, sales proposals, reports, product analysis/information sheets, manuals, bulletins and flyers, and demonstration materials. The format used by a salesperson depends on the situation and the type of information that he or she needs to convey.

Letters and memos (which are briefer and less formal than letters) are often used as part of the sales process. They may inform customers about existing or future products or about changes in the company, such as payment plans, ordering policies, or special discounts. Letters and memos can be sent to specific individuals or mass mailed to all customers and potential customers. Within the salesperson's company, memos are usually used to supply information to coworkers and superiors.

Sales proposals are prepared before the sales presentation so that the salesperson can organize the material and ensure that all relevant information is included. In the sales proposal, the salesperson outlines how he or she is going to present the product. Sales proposals should contain the product description, use, price, and other positive information about the product.

Reports may be internal or external. Internal reports will be directed to superiors or other salespeople within the company. They usually describe the sales representative's activities, progress on individual projects or with customers, and future targets for sales. External reports are written for current or potential customers. These reports are used to update customers about activities concerning the product or service that they are using, new products or services that will be on the market, or any changes in the company that will affect them.

Product analysis/information sheets contain specific information about a limited number of related products. This form of written communication can provide the customer with information about cost, effectiveness, useability, and popularity of a product with consumers. Product analysis/information sheets can be sent to a customer by mail, but they are more likely to be effective when presented with a one-on-one presentation. The presentation will allow the salesperson to help the customer appropriately interpret the information and immediately deal with any objections that the customer may raise.

Manuals contain detailed information about the sale, use, or promotion of a product. Salespeople may receive manuals from the company to aid them in the selling process. They may pass these manuals on to the customer, or the salesperson may use them to write his or her own manual for the customer. Manuals are especially helpful when the company has developed a new product or service or made a change in an existing product or service.

Bulletins or flyers are usually sent by mail to customers. They are used to inform a customer about a product or service, price changes, or upcoming events that the company is sponsoring.

Another form of written communication is demonstration materials. Demonstration materials include charts, graphs, or other materials a salesperson would use during a presentation or demonstration. They should emphasize positive points and important facts about a product or service.

Most of the types of written communication used in agribusiness are produced with computers or word processors. Using one of these machines is generally the easiest way to write them, since the information produced can be saved and reproduced later for reference or use. Formats for various documents can also be saved, which reduces production time when a similar document has to be produced. Finally, computers allow a salesperson to compile charts and graphs easily.

Importance of Effective Written Communication Skills

One reason that effective written communication skills are important is because written communication is used to support the oral part of the sales presentation. The salesperson should keep in mind that written communication is the most effective way to make a sale with some customers. Many people prefer to see information on paper rather than hear about it in an oral presentation. Also, written communication presents information in black and white, which may make it easier for the customer to absorb and retain that information. A final advantage to the use of the different forms of written communication is that customers can often keep them and review the information later, thus allowing them to become more familiar with the product or service.

In general, using written information reduces the chance of a misunderstanding between the salesperson and customer about a product or service. As discussed in the last lesson, the message that the salesperson is trying to send and the message that the customer receives may not always match in spoken communication. When written communication skills are used effectively, a sales representative can make the correct message more clear to the customer.

Forms of written communication such as letters, memos, and bulletins are important in agribusiness sales because they allow salespeople to maintain contact with customers through the mail. Effective written communication skills are crucial in using them well. Many agribusiness salespeople have large territories, sometimes covering eight to ten states. They are not able to make frequent visits to current customers. Therefore, a salesperson must use written communication. Not allowing customers to feel ignored or neglected is very important because they may choose to find a new source for the product or service with a representative who is more readily available.

Written communication can only be effective in fulfilling each of these functions if it is done properly. As in spoken communication, a concise format, appropriate terminology, and accurate information should be used so that the customer can easily understand the message. The salesperson does not want the written information to be too complicated because much of this information will be reviewed when the salesperson is not present, and the appropriate message must be easy for the customer to recognize. A concise, easy-to-read format should therefore be used in all written communications. Salespeople should avoid jargon, slang, and large amounts of technical terminology. The information must be accurate so that it does not conflict with what the customer already knows or with something the salesperson says. Making sure that data, quotes, and prices are correct is important.

When using written communication, the salesperson must proofread the material carefully. Errors in spelling, punctuation, and grammar reflect poorly on the salesperson's professionalism and competence. Customers may not take the salesperson or his or her company seriously if written communications contain errors. *Proofreading is extremely important.*

Components of Business Letters and Memos

To be able to put together an effective business letter or memorandum, the salesperson must know the components of letters and memos. A business letter is illustrated in Figure 2.1. Business letters are generally done in block style. In block format, each line of the letter begins at the left margin.

Date - Letters should be sent on business stationery with a letterhead that includes either the salesperson's or the company's name, address, and telephone number. If letterhead stationery is not available, type this information centered at the top margin. Type the date four to six lines below the sender's address.

Inside address - After typing the date, space down four times and type the inside address. The inside address includes the recipient's name, title, company, and mailing address. In sales, targeting a specific person to whom to address the letter is crucial. Before the salesperson writes, he or she *must* be sure of who is in charge. If the letter is not sent to the decision maker of the company, the effort of writing it may be wasted, since it may never reach the person who will decide whether to buy the product or service.

Salutation - The salutation is the greeting at the beginning of the letter. It is double-spaced below the inside address. The salutation should begin with the word "Dear," followed by a courtesy title (e.g., "Mr., Ms."), the recipient's last name, and a colon. The recipient's first name should not be used unless

Figure 2.1 - Business Letter

Shoestrings 'R' Us
100 Any Street
Anytown, USA 12543
(666) 555-1001

March 3, 19--

William Doe
Doe's Shoes
1000 Somewhere Lane
Anytown, USA 12345

Dear Mr. Doe:

On behalf of Shoestrings 'R' Us, I want to inform you of an upcoming sales promotion beginning on April 1 of this year.

You are familiar with the new self-tying shoestring that our company has developed. From April 1 until October 1 of this year, for every 50 pairs of the self-tying shoestrings you sell through your store, our company will give you one certificate. These certificates will be redeemed for various prizes, based on the number of certificates you hold. The grand prize is a 48" big screen television set! A bulletin giving more information about the prizes available is included with this letter.

I wanted to get this preliminary information to you so that you can start thinking about setting up demonstrations for your store. I will contact you on March 12 between 1:00 and 3:00 p.m. to discuss more details about the promotion and set up an appointment for us to meet in person. If there is a problem with this date or time, please contact me at 1-666-555-4444.

Sincerely,

Julie Wang
Sales Representative

JW/sn

Enc: Bulletin

c: Jane Jackson
Lawrence Edet

the salesperson is on familiar terms with that person.

Body - Following the salutation, double-space and begin the body of the letter. The body explains the purpose of the letter. Double-space between the paragraphs of the body.

The body should begin with an *introductory paragraph* that briefly states the sales representative's purpose for writing. Be sure to state its purpose clearly and concisely to make sure unnecessary information will not distract the recipient.

The letter continues with *body paragraphs* that more fully explain the purpose of the letter. Include any relevant facts or information but avoid giving unnecessary details. If the salesperson is familiar with the recipient's personality, he or she should tailor the content of the letter to match it to make the letter more interesting to the reader. An attention-getting item that is directly related to the purpose of the letter may be included to help get the customer excited about the topic, even if the salesperson is not present to motivate him or her directly. For example, if the company is going to offer a sale or discount or introduce a new feature or product, this information could be included to attract interest.

A *closing paragraph* ends the body of the letter. After discussing the purpose of the letter, the salesperson should close by setting a specific time and method for him or her to contact the recipient personally to discuss its contents further. The closing paragraph should also include the sales representative's telephone number in case the recipient needs to contact him or her.

Close - The close is double-spaced after the body of the letter. It indicates that the writer has finished. "Sincerely," which should be followed by a comma, is the most appropriate closing for business correspondence.

Writer's identification - After the close, space four times to leave room for the signature. The salesperson's name and title should appear below the signature.

Reference initials - If someone else types the letter, the writer's and typist's initials should be included at the bottom of the letter. Double-space after the writer's identification and type the initials, separating them with a slash. The typist's initials should be lower-cased.

Enclosure notation - If separate materials are enclosed with the letter, indicate it by double-spacing after the reference initials, typing "Enc.:", and listing the items included.

Copy notation - When copies of the letter will be sent to other people, double-space after the enclosure notation and type "c:" followed by the names of the people receiving copies.

The format of a memo is much simpler than that of a letter. A sample memorandum is provided in Figure 2.2. This memo shows one possible format; different formats are possible.

Recipient - Like a letter, memos should be sent on stationery with a letterhead. If letterhead stationery is not available, type "Memorandum" or "Memo" at the top margin. Space down four to six times and type "To:" and the name of the person who will receive the memo.

Sender - Single-space and type "From:" and the sender's name.

Date - Single-space again and type the date of the memo.

Subject line - The subject line indicates the topic of the memo. It is single-spaced after the date. Type "Subject:" followed by a short description.

Message - Double space after the subject line and type the message. The message, like the body of a letter, explains the purpose for writing. Cover the most important information first, followed by less important items. Because a memo should be brief, any additional information included must be relevant to the topic.

Reference initials - If someone else types the letter, the writer's and typist's initials should be included at the bottom of the memo, as in a business letter.

Copy notation - If copies of the memo will be given to other people, double space after the message and type "c:" and the names of the people who will be receiving a copy.

Figure 2.2 - Memorandum

Shoestrings 'R' Us
100 Any Street
Anytown, USA 12543
(666) 555-1001

To: William Doe
From: Julie Wang
Date: April 1, 19--
Subject: Price change on JX-7 shoestrings

Due to an increase in business costs for manufacturing and shipping of our JX-7 shoestrings, the price will increase from $ .58 to $ .60. This increase correlates with the rise in costs. I hope that the price increase will not have a severe impact on sales. Please contact me immediately at 1-666-555-4444 if you have any questions or concerns.

JW/sn

c: Jane Jackson
Lawrence Edet

Summary

Written forms of communication are an essential part of the sales process. A salesperson will need to use these different forms. To express professionalism and competence, a sales representative must know how to complete the various forms of written communication correctly. Effective written communication skills are important because written communication is used to support the oral part of the sales presentation, to reduce the chance of a misunderstanding between a salesperson and customer, and to maintain contact with customers through the mail.

Credits

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Lesson 3:
Using Communication Technology

Communications technology is becoming more advanced. Today's salesperson must keep up with the changes so that he or she can work in the most efficient manner possible. This lesson will discuss the more common types of electronic communications systems used today. However, keep in mind that technology is dynamic, so what is in use today may not be tomorrow.

Electronic Communications Systems and Their Uses

Several different types of electronic communications systems may be used in agribusiness, depending on what is available to the salesperson and the personal preferences of each person or company. Some more commonly used types are voice mail, facsimiles, computers and word processors, e-mail, Internet, Intranet, and, most frequently, the telephone or cellular phone. Media such as videos and television are less frequently used, but are still valuable in some situations.

Voice mail, an electronic telephone answering system, is used in many organizations. Each person in the company has his or her own voice "mailbox" number. Incoming calls may be routed to this number so that callers can leave a message for that employee, as they would with an answering machine. However, voice mail can also be used to record and send messages to another person or to a group of people who are on the system. Voice mail may thus be implemented internally or externally. Internally, voice mail is used between upper and lower management and field sales staff to keep all parties informed of current activities, changes, or news. Externally, companies may use voice mail to take messages and orders and confirm upcoming activities for customers.

Facsimile, or fax, machines are widely used today. This machine translates written material into signals transmitted over the telephone lines and prints a copy based on the signals received from other machines. Anything that a salesperson might mail may be sent over the telephone lines to another fax machine. It provides a faster, more efficient way to send correspondence to a customer.

Most salespeople, their companies, and often their customers use computers and word processors. Sales representatives most frequently use computers to type reports, create spreadsheets, store product and customer information, develop time schedules and calendars, and produce graphs, charts, and other visual aids. Each of these functions aids the salesperson in more effectively covering his or her sales territory.

E-mail, or electronic mail, is also used internally and externally in the sales profession. Companies that use computers and have e-mail software capabilities can send reports, messages, and other information from one employee to another through e-mail. If customers have computers and a modem, sales representatives can send them product information such as price changes and discounts. However, the salesperson should use e-mail with care because information should preferably be given personally (i.e., by phone call or personal visit).

The Internet is becoming a powerful force in the sales industry because it allows people to retrieve information easily and communicate with others. The Internet is a web of networks that connects computers. The World Wide Web, which consists of files with text and graphics, is one part of the Internet. A salesperson may use the Internet to get the most current information about what is going on in an industry, the government, or other areas that could affect the company or its customers, the product, or future sales of the product. Also, the ability to communicate with others on the Internet can allow a salesperson to develop new ideas about sales, people skills, and selling obstacles by discussing these issues with salespeople all over the world.

An Intranet is an internal information system that is based on the same technology as the Internet. The computers of all the users within a company are connected to a central computer interface, forming a network that people outside the network cannot access. Many different types of company information can be shared between all the members of the network. For example, policies and employee training manuals can be put on-line so that employees could access them from their individual computers. Salespeople could pull presentations and marketing information off the network. The Intranet can also connect to the Internet to access outside sources of information.

While these communications systems are helpful, the telephone is the salesperson's most useful selling tool. Wireless telephone technology, in which radio waves carry a signal from a cellular phone to an antenna that connects to landlines or other wireless phones, has made it possible to use the telephone from any location. A salesperson can use his or her office phone or a cellular phone to perform a number of different functions. Setting up and changing appointments, prospecting for new business, following up on sales, and maintaining customer relations are only a few of the tasks done over the telephone.

To make the most effective use of time, a salesperson tries to set up appointments by telephone with both established customers and prospects. In agribusiness sales, a single salesperson may cover a large territory. Salespeople want to reduce the possibility of driving a long distance and then not being able to meet with a prospect or customer. They also do not want to arrive unannounced when it is inconvenient for the customer. If a salesperson simply shows up, the customer may feel pressured to meet with him or her and may then not be in the right frame of mind to purchase the product or service. He or she also may find this unexpected arrival rude and discourteous, which will decrease his or her respect for the sales representative. Calling ahead to schedule a meeting is best for both the salesperson and the customer.

Occasionally, salespeople may have an unexpected stop or emergency that throws them off schedule, causing them to be late or miss a meeting entirely. If the salesperson will be unable to meet as scheduled, he or she should call the customer to inform him or her of the problem. Be considerate of the customer's feelings if he or she acts inconvenienced or upset. Work with the customer to find the best time to reschedule, whether later that day or another time. If possible, try to confirm a date and time immediately to prevent the customer or prospect from backing out of the appointment later.

Employing the telephone to prospect for new customers is cheap and effective if done correctly. Lists of potential customers can be obtained from many sources. These lists can be random names or specific individuals who have an interest in a product or service. Using the telephone in an appropriate way can enable the salesperson to decide whether a person is a valid prospect. The salesperson can find out if this person shows any interest in the product or service and whether he or she can purchase it, identify the person who will make the decision about the purchase, and, hopefully, set a time and date for a face-to-face meeting to discuss the product further. He or she must be careful not to reveal too much information about the product, because that may give the potential customer the ammunition to say "no" before the salesperson has a chance to give the full sales presentation face-to-face. Give the prospect enough information to present a well-rounded picture of the product and to spark interest, then stop and attempt to make an appointment.

Telephone calls can also be very beneficial in the post-sale follow-up. Most salespeople do a follow-up interview one or two days after the sale was closed. This follow-up is used to express appreciation for the customer's patronage and confirm order amounts and delivery times. This courtesy leaves the customer with a positive outlook about the salesperson.

Telephone calls can help maintain customer relations, which are an important part of the sales process. If the customer does not like the sales representative, he or she is less likely to do long-term business with that representative and company. If a salesperson has a large territory, frequent visits to each customer are impractical. Regular (perhaps weekly or biweekly) telephone calls to customers keep the salesperson and the customer informed of any changes or problems that need to be addressed before the next visit.

The salesperson can perform these functions from his or her office or cellular phone. Setting up appointments, prospecting, following up on sales, and maintaining customer relations are generally done from the office. Salespeople should designate certain days and times each week to make these calls. Some of the above calls can be made on the road from the salesperson's cellular phone, if the company provides one, but calling from the office is ususally more economical. The salesperson must therefore weigh the time management benefits of making calls on a cellular phone against the expense of the call. Usually, the more mileage covered in the sales territory, the more the cellular phone is used. The main use for a cellular phone is to notify customers of an appointment change.

Telephone Etiquette

Proper etiquette should be followed when using the telephone in any part of the sales process. Out of courtesy to the customer, these rules of conduct should guide the salesperson's use of the telephone.

- If possible, find out the name of the person who makes decisions about purchases before making the call, and ask for him or her when calling. The salesperson should not settle for a subordinate because it will probably be a waste of time for both of them. If the salesperson has not identified the decision maker before the call, then he or she should ask the person who answers the phone the name of the person in charge of making purchasing decisions.

- Never be rude or degrading when talking to support staff. They may later block the salesperson's access to the decision maker.

- Once the correct person has been reached, inform the customer about the call. Let the customer know how much time the call will take and check whether he or she is free. If the customer agrees that he or she has time for the call, state the purpose of the call.

- Keep telephone calls short. Salespeople must keep in mind that their phone calls are intrusions into the customer's day, so they should take as little of his or her time as possible. The length of a call will depend on its purpose and the customer. The customer should never have time to become bored or impatient with the salesperson.

- *Briefly* discuss the purpose of the call. Give the customer or prospect limited but complete information. Limited information should be presented because if all the information was covered, a face-to-face sales presentation, which is more likely to be successful, would have no purpose. However, the salesperson must give complete information so that the customer or prospect is well informed and develops an interest in the product.

- While supplying the customer with information, the salesperson must listen for feedback, both positive and negative, to decide if this person is a possible sales candidate. For example, having the customer or prospect ask questions that reflect a positive perspective on the product or service and the salesperson is a good sign; if he or she is "grilling" the salesperson about the negative aspects, the prospect of future sales is not as great. Listening for this type of feedback can benefit the salesperson by allowing him or her to determine whether to pursue this sale further.

- The salesperson should close the call by concluding the purpose (i.e., asking for and setting an appointment). It is a good idea to check with the customer or prospect to confirm that he or she is leaving the telephone call with the appropriate understanding of the message. The salesperson should restate the purpose of the call and listen for agreement or affirmation from the customer.

- Always use a pleasant voice. On the telephone, the voice is the only tool for making an impression on the customer. The salesperson has to think about what he or she sounds like to the other person. A sales representative should not talk too loudly or too softly. However, he or she must also avoid speaking in a boring monotone. The salesperson should speak with controlled expression.

- *ALWAYS BE POLITE!* Manners are an important consideration in using the telephone. Do not interrupt the customer. If the customer or prospect is doing a lot of talking, the salesperson may want to interrupt. However, if he or she does so, the customer may feel that the salesperson is dominating the conversation. While talking to a customer, do not be rude or pushy. Avoid hanging up on the other person. When the salesperson achieves the purpose of the call, he or she should let the customer or prospect hang up first. Doing so will prevent any possibility of accidentally cutting off the customer that could leave him or her with the impression that the salesperson is rude.

Summary

Communications technologies are rapidly changing and improving, and a successful salesperson must keep up with the changes. Depending on the market, the product, and the individual sales representative's preferences, different electronic communications systems will be used. The most commonly used form of communication is the telephone. A salesperson must know proper

telephone etiquette and be able to use the phone effectively in the sales process.

Credits

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Lesson 1:
Selling Environments

In agribusiness sales, a salesperson can work in different markets, or selling environments. For example, he or she might sell corn to a business that will process it into a final product for use by consumers and also sell a product directly to the final consumer. Because so many options are open to salespeople, they must be familiar with the characteristics of the different environments and the sales representatives' duties in each environment.

Selling Environments

Most agribusiness salespeople work in one or more of four types of selling environments. The four types are retail, wholesale, processing/industrial, and direct sales.

Retail sales is a market in which a product is sold directly to the final consumer. Examples of retailers include feed stores, lumber yards, hardware stores, and implement dealerships. Wholesale sales is a market in which the wholesaler purchases a product in bulk with the intention of dividing it into smaller portions to sell to retailers or directly to the final consumers. Wholesale clubs (like Sam's Wholesale Clubs) and feed distributors are examples of wholesalers. Processing, or industrial, sales is a market in which a salesperson sells either services or inputs like raw materials or processing equipment to a manufacturer to produce a saleable product. Grain elevators, feed mills, and implement manufacturers make industrial sales. Direct sales are made by the salesperson directly to the final consumer at the consumer's home or business. This selling environment includes door-to-door sales for products such as insurance and direct feed or seed sales. Direct sales can also take place through the Internet. Many companies have a web site on which orders for products can be placed.

The Salesperson in Retail Sales

The agribusiness salesperson involved in retail sales will most commonly be dealing with an agribusiness retail store. The sales representative must call on the business frequently to maintain a good working relationship with its owners, employees, and customers. He or she is responsible for aiding the business in setting up sales promotions and advertising, educating its employees about products, and helping the business deal with customer complaints and questions.

Promotional work is a significant part of the duties of a salesperson in retail sales. The salesperson's company may have established standard promotions and advertising for all retailers for a new product, an existing product, or an improved feature of an existing product. The salesperson may also need to work with the retailer on an individualized promotion or advertisement specifically for that area. In either case, the salesperson is the person who is most knowledgeable about the product and its features and benefits; therefore, he or she should help the retailer with an appropriate promotion or advertisement for the product.

Educating the employees of a retail business about the salesperson's products is another important duty. He or she must make sure that all of the people who will be involved in the selling process fully understand the product, its features and benefits, and any selling techniques that have been successful in other locations. This knowledge will aid the employees in making sales to both new and existing customers.

Helping the retailer handle customer complaints and questions is probably the most common and difficult task for the salesperson in retail sales. A customer may have a problem with the results he or she obtained from the product. To try to salvage the possibility of future sales to this customer, the salesperson needs to deal with these complaints. The salesperson may need to give a refund for a faulty product or a discount on a future purchase. Besides dealing with complaints, the salesperson should always be available to the customer to answer any questions that he or she might have. Sometimes customers find information directly from a company representative rather than a retailer more reassuring. A further explanation of the product, its design, and its uses may clear up some consumer concerns.

The Salesperson in Wholesale Sales

The agribusiness salesperson's role in a wholesale situation is a little different from that in retail sales. The salesperson still needs to make frequent visits to the wholesaler, make contact with customers to answer questions or provide any support that is necessary, and attempt to make sales to the final customer or retailer. The actual sales made to the

wholesaler are products sold in bulk that the wholesale business divides for resale. The salesperson will not be involved in any extensive promotional campaigns because a wholesaler generally does little advertising. For the sales representative, the biggest task is usually getting the orders placed and deliveries made quickly and accurately, so the wholesaler never runs out of the product to ship to retailers or customers. If the wholesaler does run out, the business may lose sales because it is perceived as an unreliable supplier.

The Salesperson in the Processing Industry

Sales to processors are generally quite different from wholesale or retail sales in that the salesperson is selling a product or service to help produce another product. In agribusiness, a salesperson could be selling inputs for production, like machinery, parts, and raw materials used to manufacture a product, or services, such as improved management or record-keeping techniques, used to improve the way the business is run. Usually, customers are not seen as often, since territories tend to be larger and more spread out. Actual sales occur infrequently but are large (in terms of the amount of money involved). The sales representative usually has to be more highly trained in the technical aspects of the product or service than he or she would be in other selling situations and prepared to answer very specific, detailed questions. This is especially true when the salesperson is selling equipment. The salesperson must know the machinery inside and out, answer questions, and act as a troubleshooter if the customer has any mechanical problems. The salesperson also generally deals with fewer products than in a retail or wholesale situation because he or she must focus on acquiring specialized product and market knowledge and because the sales process is usually time-consuming.

The Salesperson in Direct Sales

Agribusiness sales made directly to the final consumer are usually thought of as door-to-door sales. In this environment, the sales representative directly approaches the final consumer, or user of the product, at his or her location to make a sale. The salesperson's duties are similar to those applying in a retail sales environment: conducting sales promotions and advertising, educating others about the product, and dealing with customer complaints and questions. He or she is also responsible for making sales by performing sales presentations. Making sales includes such tasks as identifying the needs and motives of customers, understanding their buying situations, setting up the delivery, and explaining the use of the product.

Summary

Retail, wholesale, processing/industrial, and direct sales situations can all be found in agribusiness sales. Some sales positions may focus on one of these areas or may require the salesperson to operate in a combination of selling environments. The salesperson's tasks in each of these situations differ depending on the characteristics of the selling environment.

Credits

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Lesson 2:
Identifying Different Communication Styles

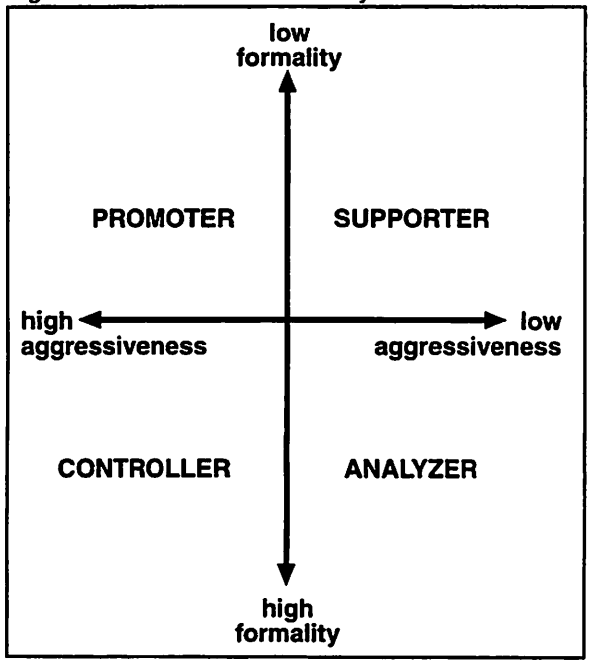
Each individual has his or her own personality, which affects the style in which he or she communicates and perceives messages from others. A salesperson must be flexible and adapt his or her personal style to that of the customer. This lesson will discuss the different types of communication styles, how to identify and understand them, and how to use this knowledge to conduct an effective sales presentation.

Types of Communication Styles

Communication styles reflect an individual's preferred mode of working and communicating with other people. They are generally separated into four categories, and every person falls somewhere within one of the categories. The four styles are analyzer, controller, promoter, and supporter. They are generally placed on a matrix to more easily represent the differences between the styles in regard to formality and aggressiveness, as shown in Figure 2.1.

The analyzer is lower on the aggressiveness scale and higher on the formality scale. Analytical customers prefer detailed data about the product. They take a substantial amount of time to digest information thoroughly and make a decision. Analyzers are inclined to show little emotion and are calm and quiet. They are generally task-oriented, generally preferring to focus on a task and work independently rather than work with other people.

Figure 2.1 - Communication Styles Matrix



Controllers are higher on the aggressiveness and formality scales. They prefer quick decisions and immediate action. People belonging to this communication type are task-oriented and extremely motivated, efficient and thorough, and very organized. They are also impatient and unemotional. The controller prefers to be in control of decisions and is often seen as a decision maker.

The promoter is inclined to be higher on the aggressiveness scale and lower on the formality scale. People with this communication style are often seen as enthusiastic, expressive, and energetic. They are people-oriented, preferring to work with people rather than work individually on a task, and are perceived as talkative. Promoters are creative. They are usually stimulated by their egos; they respond well to appeals to their reputation.

Supporters are usually low on the aggressiveness and formality scales. They are generally regarded as friendly, cooperative, open-minded, and empathetic. Supporters are people-oriented and are considered to be true team players.

None of these types of communication styles is "right" or "wrong." All of the categories include good and successful people. A successful salesperson must understand that people are different. The key to productively communicating with a customer, or, for that matter, with anyone, is recognizing the different styles and knowing how to approach individuals with each style. Effective communication depends on the ability of the sales representative to be *flexible.* Salespeople should not expect others to communicate with them in their preferred style. They should always assume that they will have to adapt to the customer.

The Importance of Understanding Different Styles

The salesperson needs to understand the different communication styles to relate to his or her customers better. The more knowledgeable the salesperson is about a customer's style, the more effective the sales presentation will be, because it can be customized. Customizing the presentation will make it easier for the customer to retain the

information that the salesperson is conveying, since the presentation will be in the style with which the customer is most comfortable. Learning to identify, understand, and use the different styles will enable the salesperson to become more successful.

Communication Styles and Sales Presentations

Each communication style has certain characteristics associated with it, and the salesperson may study those and choose the approach most likely to win over each customer. Different approaches appeal to people with the various styles. Knowing the traits associated with each type and which approaches are preferable helps the salesperson prepare the presentation. Once the customer's style has been identified, the salesperson should adapt the presentation to it.

For example, if a customer is an analyzer, the presentation should include components that will appeal to him or her. This type of person likes to have very detailed information when making a decision, and the presentation should reflect this preference. A salesperson should appeal to the customer's desire for complete and accurate information, showing proof of reliable research, detailed reports, and guarantees. The information should be presented in a formal, businesslike manner rather than in a friendly, personal way. Analyzers prefer a presentation that takes a problem-solving approach, allowing them to study the idea before taking any action. They prefer to think through ideas slowly, which may be interpreted as hesitation. The salesperson should remember not to push analyzers to make a decision before they are ready, because that will usually cause them to back off.

The approach for customers categorized as controllers should take into account their formality and aggressiveness. They should be approached in a businesslike manner. The presentation should be direct and fast paced. It should also appeal to them by including information on saving time and money and by discussing the purchase in terms of "winning." Without overselling the product, the salesperson should be sure to cover all the facts to convince the customer that buying the product would be a good investment. Generally, overselling is very easy to do with this type of person if the salesperson spends too much time discussing the features and benefits of the product or service. A sales representative should cover points thoroughly and quickly and finish before the controller gets bored. The presentation should be focused on a choice or decision, over which the customer has control.

Promoters should be approached in a more informal manner. The salesperson should respond to the promoter's friendly personality and attempt to build a personal relationship. The presentation should be inspirational, stimulating, dynamic, and fast paced to keep the promoter interested in the material. To avoid losing the customer's attention, the salesperson should not overload the presentation with details or spend too much time on important points. The presentation should be imaginative to appeal to the customer's creativity. The salesperson can also appeal to the promoter's ego by stressing what the customer will gain with the purchase of the product, such as the benefits he or she could bring to his or her company.

Supporters should also be solicited with a presentation that appeals to their desire for a personal relationship. Since supporters prefer to establish a feeling of friendship and cooperation with the salesperson, the presentation should be casual and helpful to the customer. The salesperson should be specific when explaining features and benefits and walk the customer through them, explaining the positive results of a purchase. The sales representative should design the presentation to make the customer feel good. He or she should always avoid conflict because it would clash with the feelings of friendship that the customer prefers.

Summary

Understanding and being able to identify the different communication styles is important for successful sales. Each style has very distinct traits that are easy to recognize once a salesperson has been trained to do so. This training is one of the most valuable tools a salesperson can have; it can never be overused.

Credits

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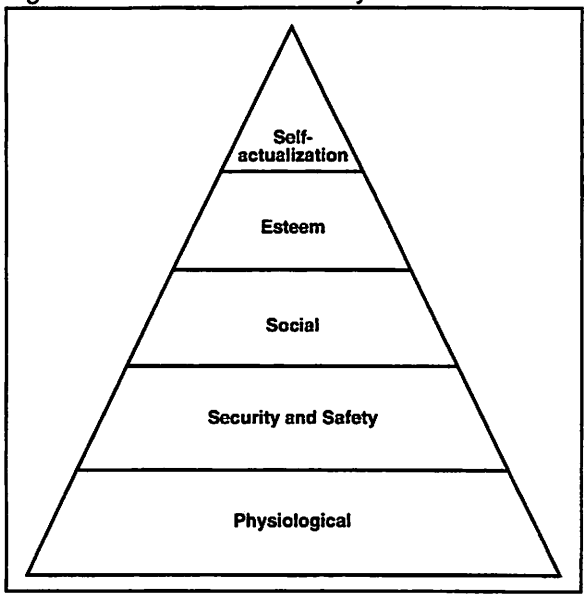
Lesson 3:
Motives for Making Purchases

Each human being has a hierarchy of needs that he or she wants to fulfill, and a salesperson must understand this concept to be successful in sales. Salespeople must also recognize the steps a customer goes through in deciding whether or not to make a purchase, so that they can adapt to these steps. Being able to identify the needs and wants of customers is important as well, because the difference between the two will affect the structure of the sales presentation.

Maslow's Hierarchy of Needs

Extensive research has been done to understand what factors motivate people to act. The psychologist Abraham Maslow developed the best-known theory. Maslow described what is now known as Maslow's Hierarchy of Needs. The hierarchy identifies people's needs and how their needs motivate them to act. His ideas are illustrated in Maslow's Pyramid (shown in Figure 3.1).

Figure 3.1 - Maslow's Hierarchy of Needs



The first and most basic needs of a human being are physiological needs. Included in this category are the things that a person *must* have to survive, such as food, water, sleep, and shelter. The next level is the need for safety and security, the need to feel both physically and emotionally safe. The third level is social, consisting of the need of an individual to feel as though he or she belongs to a group or society. The fourth level involves esteem, or a person's need to have self-respect and respect from others. The final level in the pyramid is the need for self-actualization, which is the full realization of personal potential.

Maslow's theory is based on the idea that people normally will not try to satisfy needs from the upper levels of the pyramid until they have satisfied lower-level needs. For example, if a customer does not feel financially secure (satisfying the need for safety and security), he or she will not respond to a sales presentation based on appeals to esteem. Esteem is simply not a factor when the customer feels that he or she is lacking in funds.

Salespeople must be aware of their customers' current needs, which will allow them to help the customers fulfill their needs so that they will be willing to make a purchase. Imagine that a salesperson is attempting to make a sale to a customer who is currently having financial difficulties. Since the customer is not going to want to make an unnecessary purchase, the sales representative may try different approaches. He or she may wait to try to make the sale until the customer is financially secure or attempt to help a customer with financial problems by offering advice about improving business activities, helping the customer find lending institutions that might grant a loan, or (occasionally) lending the customer money.

While this hierarchy cannot always predict the behavior of individuals, it does give the salesperson an idea of how to begin figuring out what is motivating the customer. Once the salesperson has identified the customer's level of need, he or she can motivate the customer to buy the product being offered. Suppose that a customer has fulfilled his or her lower-level needs (i.e., physiological and safety/security needs). The next step is to determine what other needs remain unfulfilled. At that point, one customer may be motivated by a need for esteem (rather than social needs). In that case, the sales representative should attempt to approach the customer with the idea that purchasing the product or service will be a good move financially and that others will view him or her as a superior businessperson for making such a purchase. Another customer may want to fulfill a social need. The salesperson's approach should therefore suggest that he or she would "belong" to a particular peer group if this purchase were made.

The sales representative might inform the customer of other people, such as friends or competitors, who have also purchased the product or service.

Deciding to Make a Purchase

People go through a process when deciding to make a purchase; although the process differs somewhat for each individual, the basic steps are the same for everyone. In this process, a customer identifies a need or a problem, possible solutions to the problem, and who might provide the solutions. He or she then decides what the best solution is and whether it is economical.

First, the customer must recognize that he or she needs a new product or perceive a problem with a current one. The customer must believe that a need exists, or he or she will not be motivated to buy anything. A salesperson can aid the customer in discovering a need, if necessary, but must be sure not to create the impression that a need exists when it does not. Identifying a need or problem that does not exist may initially trigger a sale, but this violation of trust could damage the sales representative's long-term relationship with the customer.

The next step has two parts. First, the customer identifies possible solutions; he or she then determines who can provide them. Customers may do this by talking to others with a similar need or problem to research what is working for them, looking at advertisements from various companies to see what is available on the market, and reviewing the experiences that they have had with a particular company, salesperson, or product. Sales representatives can help customers by providing information, answering questions, and customizing the product for the customer, all of which will build a better relationship between them. This relationship will influence the next step the customer takes.

The last step for the customer is to select the best solution. If a salesperson has a product that fits the customer's needs and has established a good relationship with him or her, the customer is more likely to purchase that product over a competitor's. The salesperson can attempt to convince the customer that his or her product provides the best solution by pointing out the product features that will most benefit that customer. Remember, a sales representative should not try to influence the customer's decision unless he or she believes that the product is truly the best solution, because doing so might destroy the customer's trust in him or her.

In order to select the best solution, the customer must analyze the economics of the solution. To be the best, the solution must be economical. Depending on the customer's current financial situation, product price can be a limiting factor in making a purchase. A customer may see the benefits of a more expensive product but may not be able to make a large purchase. The best product may not be the best solution for that particular customer.

Determining Wants and Needs

Determining the customer's wants and needs is a skill that is developed over time. A customer has a need if an item is something he or she has to have. A want is an extra, something the customer does not need but would like to have. Identifying the two is not as easy or obvious as it may seem, because often what the salesperson sees as an obvious need is not one in the customer's opinion.

Generally, a sale that meets a need is easier to make because the customer perceives the purchase as necessary, while fulfilling a want is usually not seen as vital. A salesperson must determine whether the customer has a want, a need, or both. The salesperson can then alter the sales presentation to adapt to that customer's motives. For example, if the salesperson knows that the customer needs the product, his or her job is to convince the customer that the product is the best one for him or her. However, if the salesperson identifies a want, the customer needs help justifying the purchase. The salesperson should try to show the customer that this product can benefit him or her.

The best way to determine a customer's true wants and needs is by asking probing questions that get the customer involved in a conversation with the salesperson. For example, the salesperson might ask the customer a question like, "What problems do you see with your current system?" If he or she can use such questions to get the customer to begin discussing problems and ways to solve them, the salesperson can begin to identify the customer's possible needs, wants, and motivations. After asking questions, the salesperson should give the customer enough time to talk. The more the customer talks, the more insight the sales representative will gain. The salesperson should be prepared to spend a considerable amount of time with the customer to learn about his or her needs, wants, and motivations. Once the salesperson has

this information, he or she can start the sales process. A sales representative who is highly skilled in this process of identification is more likely to be successful in making a sale.

Summary

Different people make purchases for different reasons. A salesperson must learn to recognize where the customer is on Maslow's Hierarchy of Needs so the sales presentation can be structured to that level. It is also important for a salesperson to understand the steps a customer goes through in deciding to make a purchase so that the sales representative can provide the appropriate information for the customer. The salesperson must be able to determine the difference between a customer's needs and wants, because the sales presentation must be structured differently for each.

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Lesson 4:
Product, Company, and Industry Knowledge

Product, company, and industry knowledge is vital to the sales process. Without this knowledge, a salesperson cannot be successful, since his or her job is to educate customers in a positive way so that they are motivated to buy a product. To be competitive, salespeople must also be aware of their competition and of trends in the market that may positively or negatively affect customers.

Product Knowledge

Several types of product knowledge are necessary for the sales presentation. This information falls into four categories: general information, application information, maintenance information, and company support information.

Each of these four categories contains many details that the salesperson should know. For example, general information includes the number and types of models or styles available, the materials in the product and how it is made, price, discounts, size, color, packaging, product improvements, company history and reliability, and identifying characteristics, such as brand names and logos. Application information includes the use and capability of the product, instructions for operation, and performance standards. Maintenance information consists of data on the care and maintenance of the product, guarantees and warranties and their limitations, and maintenance and repair costs. Company support information includes credit options provided by the company, ordering policies, shipping policies and reliability of delivery, and training provided on the use of new products and systems.

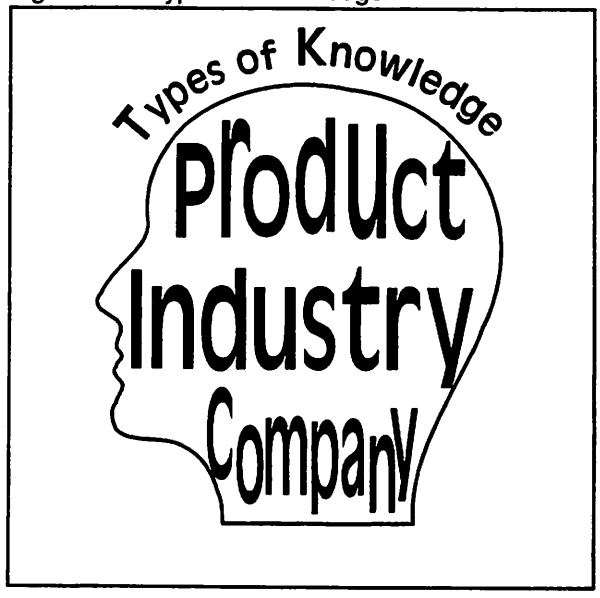
These aspects of product knowledge should be introduced to the customer during the presentation so that he or she is fully informed about the product and confident about the salesperson's knowledge and experience. If these items are not covered in the sales presentation, the customer is likely to raise questions about them. The salesperson should be well informed and able to answer any questions the customer might have.

Industry and Company Knowledge

Industry and company knowledge should be included in the sales presentation to inform customers about items and events that will affect them and their purchasing decisions and to convey the competence, knowledge, and reliability of the salesperson and his or her company. Industry knowledge that may be used in a sales presentation includes market trends in the supply of and demand for the product and the components used to manufacture it. Another component of industry knowledge is a knowledge of the products of competitors (which is discussed in greater detail in the next section). The salesperson might also discuss developments made or technologies being introduced into the industry that will affect buying decisions. For example, a sales representative selling a new drill that could apply herbicides or pesticides with great precision might learn that one of the major chemical companies would soon be releasing a new pesticide for soybeans that had to be applied in highly precise amounts. He or she would want to include this information in the presentation, because the drill might become a more economical purchase if the customer also bought this pesticide.

Company knowledge should also be used in the sales presentation. The salesperson should discuss the company's history and its standing within the industry, company policies, the reliability of the company and the product, and warranties and product guarantees. These items are important to

Figure 4.1 - Types of Knowledge



a customer who is considering whether to purchase a product. Customers want information about the company that they may be doing business with so that they have some sense of its reliability and professionalism. Customers are not going to do long-term business with a company that they do not know and trust.

Both industry and company knowledge should be included in the sales presentation, but they should not *become* the presentation. The salesperson is selling the whole package, but the most important part of that package is still the product and its features and benefits. The information about the industry and company is complementary to the essential information about the product. Without all these types of information, the presentation would not be complete.

Knowing Competitors' Products

Salespeople must be almost as familiar with their competitors' products as with their own. They cannot present their products in the best light if they do not know what they are competing against in the market.

Competent salespeople know the same type of information about competitors' products as they do about their own. Knowing competitors' products allows the salesperson to focus the presentation of his or her own product on the areas in which it has a definite advantage over the competition. In addition, the salesperson must be ready to answer any questions concerning the advantages of buying his or her product. For example, a customer may claim that he or she has been offered a discount price by a competitor. The salesperson must be familiar with these offers so that he or she is ready to emphasize other benefits of buying his or her product.

The Necessity of Product and Industry Knowledge

Sales representatives in any field must have an extensive knowledge of their product and the industry in which they work to aid in the sales process. The more knowledge a salesperson has, the more readily he or she can answer questions, identify product features or benefits, forecast future needs of the company and the customer, and understand trends that may affect future sales.

Product knowledge is vital when dealing with customers or prospective customers. The salesperson can use this knowledge to inform, provide advice and make suggestions to, and solve problems for the customer. He or she must have product knowledge not only to provide information but also to identify the product features that will provide the most important benefits for each customer. A salesperson cannot sell a product that he or she does not know and understand.

Industry knowledge is a necessity for a salesperson because it allows him or her to understand the attitude of customers toward competitors and the industry, what kind of and how much competition must be overcome to make a sale, and any market developments. The salesperson can then prepare for them. A sales representative needs to understand these factors to improve the success rate of attempted sales. The salesperson who is not aware of the market and competition cannot be fully prepared for a sales presentation.

Resources for Product and Industry Knowledge

A salesperson must know the best sources of information in the particular industry in which he or she works. Knowledge about both the product and the industry may be obtained in several ways. Resources will vary, depending on the industry. The salesperson must not be afraid to ask for help in finding product and industry information. Asking for help is better than going into a sales presentation without the appropriate knowledge.

Product knowledge is available from many sources. The most common resource for product knowledge is the salesperson's company. The company will provide information about the product, such as how it works, how and of what it is made, and its unique features. However, when using this source, a sales representative must remember that the information will be presented to make the product look as good as possible. Because of this slanted viewpoint, a salesperson may want to look at other resources for unbiased information about the product. These sources may be research reports from independent companies or universities, consumer reports, customer testimonials, newspaper or magazine articles, or even the salesperson's personal experience with the product.

Many sources of industry information are the same as those for product information. Industry knowledge can be obtained from the salesperson's

own company. The company or other sales representatives within it can provide knowledge about the market, customers, and competition. This resource is extremely valuable because the company can supply information from its experience in the industry, such as how the product has done in the past and the most successful tactics for dealing with customers and the competition. Unbiased sources include research from independent sources, market reports, newspaper and magazine articles, and discussions of the market with representatives from other companies and with customers. A successful salesperson will look at several of these sources when studying the industry.

Utilizing Product, Company, and Industry Knowledge

Knowledge about the product, company, and industry is used to make a successful sales presentation. A salesperson who is knowledgeable in these areas will be more credible to the customer and will more likely be able to match features and benefits to each customer. The salesperson must gather all available information and then find the best details to use in the sales presentation. The information should be truthful, yet show the product in the most positive light possible. The salesperson should have as much information as possible and be prepared for customers' questions.

Product knowledge is important when making a sales presentation because the customer must be well informed about the product. Customers must be familiar with the product before they will decide to buy it. Also, the customer must be convinced that the purchase of this product will produce enough benefits to justify the cost, so the salesperson has to indicate the product features that will appeal to the customer. For example, a sales representative may be providing a livestock feed that has the same nutrient content as the product of the major competitor. However, his or her company can provide the feed in pellet form, while the competitor cannot. If this customer prefers to purchase pelleted feed, then this feature may be a selling point.

Company knowledge is also an important part of the sales presentation. Some of this information should be provided in the presentation, whereas some of it may be required to answer questions asked by the customer during the presentation. In either case, the salesperson must have a significant amount of knowledge, because it may provide important selling points. If the salesperson's company provides a financing option for larger purchases (and a competitor does not), the customer might choose it over the competitors'.

Industry knowledge is a vital part of the sales presentation. The salesperson is expected to provide the customer with information about the market, such as trends in supply and demand and new technologies that are being developed and implemented within the industry. Events occurring in the industry will affect the decisions made by customers. The salesperson needs to think through the industry knowledge that he or she has obtained and present any information that will be relevant to the customer making the buying decision. An example is a sales representative in retail sales who has evidence (such as a new ad campaign or a proven seasonal use increase) that the demand for a product is on the rise. The salesperson would inform retailers about this increase in demand so that they could use the information to decide whether and how much to buy.

When supplying industry information during a presentation, a sales representative should not directly mention competitors. First, he or she does not want to provide free advertising for the competition. Second, being critical of the competition may have negative consequences. The customer may be very loyal to the competition and become offended by critical remarks; the customer may also feel that the salesperson is implying that he or she is "dumb" for buying an inferior product. Products should be sold on their strong points, not on a competitor's weaknesses. Both colleagues and customers view talking negatively about a competitor or making a sale based on the competitor's weaknesses as very unprofessional. However, the salesperson must know the competition's strong and weak points and make comparisons to close the sale.

Summary

A salesperson must have product, company, and industry knowledge for two reasons. First, the salesperson must know this information so that he or she can select the appropriate information to include in the sales presentation for individual customers. Second, he or she must be able to explain information to the customer if the customer asks a question. Knowing all the important information about a product, what events are taking place in the market, and the competition and their

products is vital for a sales representative hoping to make a sale.

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Lesson 5:
Identifying and Approaching Potential Customers

Identifying and approaching potential customers are the vital first steps in the sales process. Salespeople constantly search for customers. Once potential customers have been identified, they must be approached. The approach creates the customer's first impression of the salesperson and the company and, therefore, is very important.

Methods for Identifying Potential Customers

Salespeople can use several methods to identify potential customers for a product. This lesson will focus on the main methods used in agricultural sales. Sales representatives learn about new customers through their company, personal experience, other customers, noncompeting salespeople, public sources, and commercial sources.

The salesperson's own company will often give him or her a list of prospects. This list may have been compiled by the sales department, research department, a group of sales representatives, or other sources within the company. The sales department has a list of current customers; these customers are good prospects for any new product the company may be selling because they are already comfortable with the company. Some companies have research departments that will compile lists of prospective customers based on research done to find out who might need or want to buy the product. The company may also have meetings of sales representatives in which they brainstorm about possible prospects. Other sources of information are divisions such as the credit department or the service department. Credit departments have records of the credit accounts of current and past customers who may be excellent prospects. Service departments can also be a source of leads because they have records of repair requests by current customers. If a current customer has an older product that is being repaired frequently, he or she may be ready to make a new purchase. Any department within a company may have valuable information about prospective customers, so a salesperson must be aware of the possibilities that exist in his or her company.

The salesperson's personal experience in the field can be a valuable source of information about prospects. Some methods used to learn about potential customers are personal observations, cold canvassing, and telephone calls or direct mail. The first of these, personal observation, requires the sales representative to be aware of changes occurring within his or her territory. The salesperson can learn about changes by reading local newspapers, joining clubs or groups, and attending community activities or other events that place him or her in contact with people in the sales territory. This contact allows the salesperson to become aware of new prospects quickly. For example, a salesperson in the home siding business might discover a prospect at a club meeting, where he or she learns that a new family has moved to the area and bought a "fixer-upper."

Another way a salesperson can find prospects personally is through cold canvassing. In cold canvassing, the salesperson calls on a group of people in a particular area without considering whether they are good prospects. This process is called cold canvassing because it is done "cold," with no prior research or contact with the customers. It is usually thought of as door-to-door sales, but a salesperson can cold canvass an area with business cards or flyers. The idea behind cold canvassing is that if the sales representative gives enough people the opportunity to buy the product, he or she will eventually find a customer. Cold canvassing may uncover prospects not revealed through other sources.

Salespeople can also conduct personal searches for prospective customers through telephone calls and direct mail. Both are similar to cold canvassing, except that many times the lists of phone numbers and mailing lists come from some type of research that at least starts the process of qualifying them as potential customers. The salesperson using the telephone to search for customers calls people who could be valid prospects; the salesperson can then make a sales presentation over the phone to attract the prospect's attention and interest. Depending on the product being sold, telephone prospecting can be very successful. Direct mail is the process of mailing out information about sales, discounts, new products, or new features to gain interest from prospects. A mailing list, like the telephone number list mentioned earlier, can be used, or an entire mailing area can be covered. Retailers frequently use this method because direct mail can spark enough interest to get the prospect into the store,

which will usually lead to a purchase. Salespeople can also use faxes to find customers in a variation on direct mail. Using lists of fax numbers, the sales representative can fax the direct mail information to potential customers.

Current customers can also help the sales representative find new prospects. Because customers know the salesperson, the company, and how the product performs, they may make referrals to good prospects among their friends, family, and business associates. Referrals can be direct, but sales representatives should listen carefully to their customers, because they sometimes offer subtle clues that a salesperson can pursue as well. Customers can also help the salesperson qualify a likely prospect by giving him or her insight into who the decision maker is, if the prospect is financially able to purchase the product, or if the prospect is interested in the product.

Two ways that the salesperson can obtain referrals from customers are through an endless chain or from a center of influence. The endless chain method is used when the sales representative asks a current customer for a list of names of people who he or she feels would be interested in a sales presentation. Getting a short list from each customer will give a salesperson a significant number of prospects. Centers of influence are people who have high standing within the community. They may be current customers or just acquaintances of the salesperson. They generally have many varied contacts who could be useful to the salesperson. He or she may learn of many prospects from a center of influence. If a center of influence is a customer, his or her business is an advertisement for the product. Their reputation in the community may attract people who wish to emulate them. Centers of influence may cause other people to consider making a purchase because they look up to them.

Current customers can also help gain the interest of prospects by giving customer testimonials. In a testimonial, a customer makes a statement about his or her satisfaction with the product so the salesperson can present it to prospective customers to help make more sales.

Noncompeting salespeople, both inside and outside the company, can help a sales representative to find prospects. Other salespeople may have contact with people within the sales territory interested in a particular product, and they can keep fellow salespeople informed about any new prospects. A salesperson should always try to reciprocate by passing on information.

Public sources, such as government agencies, can provide lists of names that a salesperson could find helpful when prospecting for new customers. For example, land purchases are public knowledge; a sales representative selling lawn care equipment can go to the county recorder and get the name of a new landowner who might be very interested in that type of product. Most of the information from public sources either is free or available for the cost of copying and shipping. However, the information included is at times both extensive and vague; it must then be recategorized to suit the salesperson's needs.

Commercial sources of information can provide more direct and focused lists of potential customers for an individual salesperson, but obtaining them costs a substantial amount of money. The sales representative or the company may contact a research firm and request a list of names based on certain specified factors. The factors would depend on the product, the industry, and the type of customers. These companies can provide very good information if the salesperson or company is willing to pay for their services.

The sources listed above are the most commonly used, but a salesperson must always look for other possible sources of information. A sales representative must be aware of his or her environment so that he or she can attempt to make a sale to any new prospects. He or she must constantly be on the lookout for new possibilities.

Information about the Customer

While prospecting, a salesperson must find out several things about the customer to prepare for the sales presentation. The sales representative must determine who the decision maker is and identify his or her personality type, substantiate his or her financial capability, determine whether a need for the product exists, calculate the potential volume and longevity of the business relationship, and ensure that the prospect is accessible, both physically and mentally.

Identifying the decision maker and his or her personality type is very important. The salesperson should not waste time trying to make a sale to an employee who does not have the power to make

buying decisions. Determining the buyer's type is important because the sales presentation must be structured to suit the personality style of the customer. The information about the decision maker and his or her personality can be determined during the prospecting process by asking the right questions and listening carefully to the responses.

The salesperson needs to determine that the prospect is financially able to purchase the product before preparing and giving the sales presentation. If the customer cannot make a purchase, then the salesperson should not waste the customer's and his or her own time making a presentation. Asking questions during prospecting may elicit this information, but the salesperson must be careful not to ask questions that should be off limits to an outsider or that would offend the prospect. A good question to ask would be "Are you financially prepared to make a purchase of this size at this time?"

During the process of identifying the prospect as a potential customer, the salesperson should try to determine if he or she truly needs the product and if that need can be met with the purchase. A sales presentation should not be made if the prospect does not need the product, because either a onetime purchase will be made (if the customer feels pressured to commit to a purchase) or no sale will be made at all. The prospect should be asked probing questions to get him or her to talk about needs to determine if the product fits them.

The potential volume of sales and longevity of the business relationship between the company and the prospective customer can be a determining factor in whether or not to pursue the sales presentation. The amount that the customer may purchase and the length of time that he or she will do business with the company will affect the salesperson's decision about trying to make a sale. Small-volume purchases may not be worth the salesperson's time or the shipping costs unless the business relationship will grow and become a long-term one. Onetime purchases, unless they are very large, also may not be worth the time and effort the salesperson and company would have to invest. The ideal customer is one who will make either large or long-term purchases, or both.

Finally, a salesperson should determine the accessibility of the customer. Accessibility means that the salesperson can get to the customer to make the sales presentation. It refers to both physical and mental availability. Physical accessibility is being able to make personal contact with the customer to perform the sales presentation. The salesperson must learn whether the customer is available for a personal (or at least a telephone) meeting. If the prospect is routinely unavailable, then he or she may not be a good prospective customer. Before giving the sales presentation, the salesperson should make sure that the customer is mentally accessible. He or she should not be too busy, distracted, upset, or emotional to listen to the presentation carefully and then make a reasonable decision.

Customer Perceptions of the Salesperson

The customer's impressions of the salesperson, formed before, during, and after the sales presentation, may have a significant impact on the buying decision. These perceptions may be either positive or negative. Although the salesperson cannot control the customer's perceptions, he or she can try to influence them.

The first and most obvious factor that may influence the customer is the salesperson's appearance. The salesperson should be dressed professionally and appropriately for the market. The usual guideline for dressing is to dress just a bit better than the customer. Dressing appropriately shows the sales representative's concern for his or her appearance, respect for the customer, and respect for the company he or she represents. Clothing and jewelry should be clean, neat, and not too flashy to be professional.

The salesperson's attitude may also affect the customer's perception of him or her. The salesperson must be aware of the image and attitude that he or she projects through manner of speaking, language used, and tone of voice. Salespeople want to be seen as friendly, honest, knowledgeable, and sincere. The way they act may project other images, however. For example, if a salesperson brags or interrupts the customer, the impression the customer receives may be of an arrogant or conceited individual.

The salesperson must be aware of the nonverbal signals (discussed in Unit 2, Lesson 1) that he or she may be unintentionally sending the customer. The salesperson may send the wrong signal through facial expressions, gestures, and body positions. A frown at the wrong time could give the customer the impression that a salesperson is not pleased. The

salesperson must CONSTANTLY be aware of his or her nonverbal communication.

The customer must receive the impression that the salesperson is knowledgeable about the product, the market, and the company. Including the product, company, and industry knowledge discussed in the last lesson in the presentation may help form this perception. It builds the customer's confidence in the sales representative's level of knowledge.

The most important quality a salesperson must convey to the customer is trustworthiness and credibility. The customer must believe that the salesperson and the company are honest, ethical, and reliable. The salesperson must never lie, make a promise that he or she knows cannot be kept, or deceive the customer in any way, at any time. If a sales representative misinforms the customer by mistake, he or she should immediately acknowledge the mistake and explain it. Such honesty will build customer confidence and trust in both the salesperson and the company.

Sometimes the customer may be influenced by factors that are beyond the control of the salesperson. He or she may have had past experiences with the sales representative's company, product, or another salesperson from that company that could affect the customer's perceptions. A bad past experience will generally make the customer reluctant to do business. The customer may also have a bias against the sales representative based on his or her age, gender, or race. The salesperson must be aware of these obstacles and be patient and persistent in the hope that he or she can overcome the obstacle and eventually make the sale.

Sales Environment

In sales, the term *approach* refers to the way the salesperson solicits a purchase from the customer in a presentation. The environment in which a sales presentation will be conducted determines the approach used by the salesperson and has an impact on the success of the presentation. As indicated in Unit 3, Lesson 1, the environments encountered in sales are retail, wholesale, processing/industrial, and direct sales. These environments require the same general ideas or tactics, but the focus for each presentation is customized to the environment's specific needs.

Retail prospects may be either existing customers to whom the salesperson wants to introduce a new product or new retailers with whom the salesperson wants to do business. The approach to retailers should emphasize one of the most important areas of interest for them--market information about the future demand for the product. Retailers require information about demand because they are not going to buy something they cannot sell. The salesperson should take into account the type of customers that a specific retailer will be dealing with to determine the need for the product. The financial capability of the retailer is another important consideration in the approach, because generally a retailer will make a fairly large purchase to stock store shelves. Finally, the salesperson must approach the retailer with ideas for promotions or advertisements and make sure that the retailer is willing to participate in them.

The approach in the wholesale environment is similar to that in retail. The wholesaler must provide information about the number of retailers in his or her area who want to carry the product, because they will make up most of the demand. The financial capability of the wholesaler must be determined because the wholesaler will buy a very large quantity of the product and must be able to afford a purchase. The salesperson should inform the wholesaler of any volume discounts, because they may be of aid in making the purchase. Information about delivery and order procedures and policies should also be provided to the wholesaler.

Sales in the processing sector will be approached differently than in either the retail or the wholesale environment. Businesses in this sales environment will be more interested in product efficiency and technical support because they are buying such things as equipment and raw materials. The salesperson should focus on this information in the approach. In addition, the salesperson should find out whether the processor needs this type of product and is financially able to purchase it.

The approach in direct sales should focus on the benefits the customer will receive by purchasing and using the product. The salesperson must identify the needs of the customer and the features of the product that can meet them and so benefit the customer. The salesperson must also inform the customer about the support that he or she will receive from the company in response to questions or problems.

The Salesperson's Appearance

This subject was mentioned earlier in this lesson but will now be discussed in more detail. The first thing that a prospective customer will notice during a personal meeting is the salesperson's appearance. It may have a negative or a positive effect on the sales presentation.

The salesperson should wear professional dress, but what professional dress is depends on the salesperson's market and customers. A sales representative should dress in the same style but a bit better than the customer. For example, many agricultural sales involve visiting a producer. Most of them wear very casual clothing, like blue jeans that are usually fairly worn and sometimes dirty. The salesperson should wear a casual shirt with clean dress jeans or very casual slacks. Being underdressed or overdressed gives customers the impression that the salesperson either is not prepared to sell to them in their environment or does not have enough knowledge of their environment to know what is appropriate.

Clothing and jewelry should not be gaudy or flashy because the salesperson does not want them to distract the customer from the presentation. Trendy clothing and jewelry fit into this category. For example, a female salesperson wearing very large, dangling earrings could distract the customer. The earrings would be obtrusive; they might even make noise when the salesperson moved her head.

Even if it is not especially trendy, jewelry may still be distracting if the salesperson plays with it when speaking. This may draw the attention of the customer away from what is being said. Salespeople should be careful not to toy with jewelry during a presentation.

Another consideration is the general appearance of the salesperson. The sales representative should be clean, with well-kept hair and nails. The salesperson should keep his or her hair cut and neatly styled. Fingernails should be trimmed and well cared for. Women should wear moderate makeup.

Greeting the Customer

The sales representative should follow some general steps for greeting a customer and conducting the first meeting. Since the meeting is often the first physical contact the customer has with the salesperson, he or she must be comfortable with these steps to make a good first impression.

When greeting a customer, the first thing the salesperson should do is shake hands. Many people read a lot into a handshake, so the salesperson needs to practice shaking hands so a meeting can get off to a good start. The salesperson wants to initiate the handshake with the potential customer, if possible. A good handshake is firm, of medium length, and dry. It should not be bone-crushing or limp; it should not be too long or short. The customer should be addressed by name, but the sales representative should use his or her first name only after getting permission to do so. If the salesperson is unsure of the correct pronunciation of the customer's name, he or she should ask how to pronounce it as an expression of respect for the customer.

Next, the salesperson should introduce him- or herself and the company. He or she should do so very slowly so that the customer will be more likely to remember the names. They should be repeated during the presentation. The salesperson will also want to supply each customer with a business card. A sales representative should always express his or her appreciation to the customer for taking the time to meet. This courtesy may make the customer more receptive to the sales pitch.

The next step is to state the purpose of the meeting. This alerts the customer to the direction of the conversation and indicates his or her role in it. Being informed allows the customer to more easily follow the presentation. A salesperson might say something like "Mr. Baker, today I'm going to tell you about a new type of seed corn that will be available next year."

After stating the purpose of the meeting, the salesperson wants to gain information from the customer, which is accomplished by asking probing questions about such things as the products he or she is currently using. The salesperson will also verify that any information he or she already has is correct. Doing so shows that the salesperson has researched this customer and his or her business. The salesperson does not want the entire presentation to consist of questions for the customer, however. He or she will want to introduce some investigative comments that will hopefully draw out more information without direct questioning.

After the body of the presentation, the salesperson should ask the customer if he or she has any more questions or comments. If not, the meeting should be ended to avoid wasting any of the customer's time. The sales representative should thank the customer for his or her time and attention. He or she should also let the customer know how to contact him or her with any questions or problems and shake hands again before leaving, if possible.

Summary

Learning to identify and approach a prospective customer is an important part of the sales process. Identifying a customer must be done carefully to make sure that valid prospects are found and the salesperson does not waste his or her time. The approach to a prospective customer is also important because it can set the climate for the future business relationship. It gives the customer his or her first impression of the salesperson. The salesperson should practice the approach so that the process is as smooth and businesslike as possible.

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Lesson 1:
Building Rapport with Customers

A salesperson must attempt to build and maintain rapport with his or her customers to have successful sales relationships. Several factors that affect the development of rapport will be discussed in this lesson.

The Importance of Developing Customer Relationships

Developing a relationship with the customer is important to the success of a sales presentation. A customer is more likely to do long-term business with a company if he or she feels that a stable relationship exists between them. If the salesperson establishes a good relationship with the customer, the salesperson, the company, and the customer will all profit from it. Their relationship becomes a win-win situation. In a win-win relationship, if all the parties involved do their part, they all benefit. However, if one participant does not cooperate, everyone loses.

One benefit of establishing a relationship with a customer is customer loyalty. A competitor will find it extremely difficult to interest customers in its product if they have a well-established relationship with another sales representative and his or her company. If the integrity of the salesperson and the product have satisfied the customer, he or she is less likely to be interested in doing business with another company. The customer feels an obligation to be loyal if a salesperson has treated him or her fairly and honestly.

Another benefit of a good customer relationship is that obtaining referrals and testimonials may become easier, which may make prospecting for new customers easier as well. A customer who has a good relationship with a salesperson will be more willing to give him or her the names of friends and acquaintances who may be good prospects. One motivation for sharing their names is that the customer wants to share his or her good experience with others. The customer may also want to do the salesperson the "favor" of providing referrals in return for services rendered. A good relationship may also pay off in prospecting because current customers can provide well-substantiated customer testimonials. A longtime customer has worked with the salesperson and company long enough that he or she can give the prospect a positive view of both them and their product.

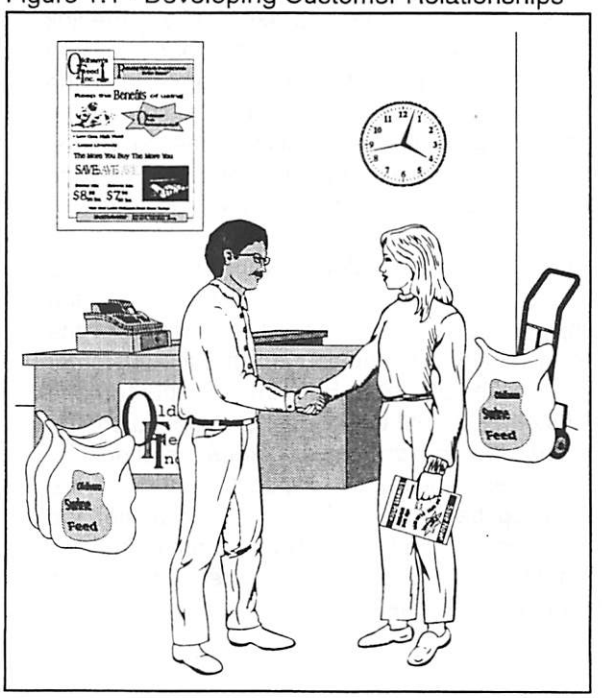
A third benefit of a good relationship is the potential for long-term purchases. Once a relationship has been established, the customer generally finds it difficult to stop doing business. If the customer and the salesperson have invested time in building a relationship, they have both made a commitment to a long-term buyer-seller relationship. No good business person is going to waste time building a relationship for a one time purchase.

Developing Rapport with a Customer

The salesperson must consider different factors when developing rapport with a customer. Rapport is established when both parties share feelings of honesty, trust, comfort, and support, as well as a common goal. To develop a sound business relationship, these factors should be considered from the first meeting with a customer. All of them require work. Once established, rapport must be maintained throughout the business relationship.

Honesty, trust, and comfort are closely related. The salesperson and the customer must be honest with each other to build trust. The salesperson should never deceive a customer, either by lying or by failing to reveal information that may reflect negatively on the product, company, or sales

Figure 1.1 - Developing Customer Relationships



representative him- or herself. Being honest allows the salesperson to let the customer know about any negative information and, therefore, explain it in the most positive light possible.

Developing trust involves more than just being honest. The customer must feel that he or she can depend on the product, company, and salesperson to do long-term business, and the salesperson must feel the same way about the customer. To establish trust, the salesperson must be professional and businesslike. He or she should be friendly and polite, which shows eagerness to work with and respect for the customer. The sales representative should let the customer know that he or she is available to provide help at any time, and at the same time confirm his or her competence and knowledge about the product. The salesperson should inform the customer about what steps he or she plans to take to discover and meet that customer's specific needs.

Once the salesperson and customer have established trust, both parties will develop a certain comfort level in the relationship. Being comfortable in a sales situation means that both the customer and salesperson feel that discussing almost anything about the product and company is acceptable.

Support from the salesperson and the company aids in establishing rapport. The salesperson should be available to answer any questions or give advice to the customer. The sales representative is the link between the customer and the company for any technical support that may be necessary. He or she may also find it necessary to provide support by advising the customer on specific business matters, such as financial planning. However, such advice should only be given at the customer's request.

The final factor in developing rapport is finding a common goal. When making a sales call, the salesperson should announce the purpose of the meeting immediately and confirm that the customer agrees with the purpose. Both the salesperson and the customer should then develop expectations for both parties for the long-term business relationship. This process develops rapport early in the relationship because each party knows that the other has long-term plans. Their commitment to a mutual long-term goal helps ensure that they will continue to work together.

The Importance of Establishing Credibility

Establishing the credibility of the salesperson and company is an essential part of the sales process. A customer must be able to believe in the salesperson to build a long-term business relationship. The salesperson can prove his or her credibility by being honest, supplying complete information, and backing up any promises that have been made. The customer must feel that the salesperson is a good source of information and can be counted on to take care of any concerns or problems that may arise during the business relationship. The customer will not likely make purchases for very long, if at all, from a salesperson who is not credible.

The Importance of Identifying Reasons for Doing Business

To establish a good relationship with customers, the salesperson must inform them of his or her reasons for doing business and the mission of the business relationship. Identifying reasons for doing business is necessary to ensure that the customer and salesperson have the same expectations. At the beginning of their association, the salesperson should explain in detail the purpose of the sales presentation, what he or she will provide, and what will be expected from the customer. The customer then has the necessary information to decide whether to proceed with the business relationship. The salesperson may learn that the customer does not want to do business and can avoid wasting any more time. If the salesperson is rejected, he or she might try a different approach with that customer later, or use the rejection to improve his or her approach with other prospective customers. If the customer wants to do business but is not comfortable with some part of the purpose, clearly stating the purpose gives the customer an opportunity to bring up any areas of concern or changes that he or she may want to make. This process can stimulate a conversation in which the salesperson can gain a substantial amount of pertinent information about the customer and his or her business priorities.

Summary

One of the salesperson's priorities when dealing with customers is developing and maintaining rapport. If a customer and salesperson do not have good rapport, neither one of them may feel comfortable with the possibility of a long-term

relationship. Building rapport involves cultivating honesty, trust, comfort, support, and finding a common goal. Establishing credibility and identifying reasons for doing business are also important parts of forming a good relationship with a customer.

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Lesson 2:
Identifying Customer Needs

Identifying customer needs is crucial to making sales. The process of discovering needs is many times a long one, entailing several steps. One must become familiar with the process to be successful in a sales career.

Importance of Identifying Customer Needs

Identifying customer needs is important for two reasons. First, since needs motivate the customer's buying decision, the salesperson must know what the customer's true needs are to be able to make a sale successfully. If a need does not exist or if the purchase of the salesperson's product cannot satisfy it, then a business relationship is unnecessary. Identifying the customer's needs is also important because the salesperson will discover valuable information about the customer and his or her personality and business at the same time.

The first step in the process is discovering a need. The salesperson must ask probing questions and listen carefully to the responses to learn what the customer's true needs are and if the salesperson's product can meet them. Asking questions also gives the salesperson valuable insights about the customer and his or her concerns. Another way a sales representative can uncover needs is by observing and researching the customer's business; often, a salesperson comes up with a better idea of a need or problem area when not distracted by the bias of the customer.

Once the salesperson has established a list of possible needs, the second step is making the customer aware of them. The salesperson should question the customer to see if he or she agrees about the nature of the needs. Although the salesperson was able to identify the needs, customers may not recognize their needs themselves. A customer may have focused on other areas of the business, may not have researched his or her own needs thoroughly, or may not think that a reasonable solution to a need exists. The salesperson's job is to help the customer recognize his or her true needs by informing the customer about the research conducted by the salesperson or by revealing ways to meet seemingly unfulfillable needs.

After the salesperson has identified needs by completing these two steps, he or she should satisfy those needs, preferably through the sale of a product. The salesperson must go through the process of identifying needs to make a sale. He or she cannot accurately discuss customer benefits without understanding the customer's needs. The salesperson must connect product features with specific benefits to the customer and the business during the presentation, or the customer may not be convinced that a need exists or that a product can meet it.

Types of Sales Personalities

A salesperson must be aware of the different personality types that exist. These personality types can affect the salesperson's approach to the customer. These three types of sales personalities are extrovert, introvert, and ambivert.

An extrovert tends to be very outgoing, friendly, and talkative. Extroverts are more people-oriented and less opinionated. They like to talk and get to know the salesperson immediately. Extroverts are an easier initial sale than other types because they tend to be more open-minded. An extrovert should be approached in a friendly and open manner so the salesperson can build a personal relationship with the customer. These customers enjoy praise for their accomplishments and an abundance of assistance and technical support from the salesperson to enhance their egos.

Introverts are more subdued and private and less emotional than extroverts. They are task-oriented rather than people-oriented and are extremely analytical when making a decision. This personality type likes to have extensive information on which to base a decision. In comparison to extroverts, introverts are more openly opinionated and predictable. Introverts are harder to sell to initially but are generally very loyal after making a decision. The best approach for dealing with an introvert is to have a detailed, specific, and fact-filled presentation. Introverts should not be rushed; they like to digest all the facts before making a decision.

The ambivert is a combination of introvert and extrovert traits; most people fall into this category. In an ambivert, the salesperson will recognize behavior that is typical of both an introvert and extrovert. The salesperson must observe the customer's behavior to learn which elements of each

personality type the ambivert expresses and mold the sales presentation to fit these characteristics.

Salespeople should look for the different qualities associated with these sales personalities during each contact with the customer. They must take the time to figure out which of the personality types each customer is. This information can make the difference between a successful and an unsuccessful presentation.

Open-Ended and Close-Ended Questions

When using questions to discover needs, the salesperson may ask both open- and close-ended questions. Open-ended questions, like "What can you tell me about your business?", require a more extensive answer than just yes or no. They should be thought-provoking. These questions can help the salesperson to understand the customer and his or her point of view. They are generally nonthreatening and allow the customer some control over the conversation, which generates feelings of friendliness and trust for the salesperson.

Close-ended questions are questions that generally provide information through very short answers. "Do you own finishing hogs?" is an example of a close-ended question. They are useful if the salesperson needs to learn specific information about the customer. With this type of question, the salesperson has almost total control of the conversation. The salesperson must be careful not to overuse these questions, or the customer may feel as though he or she is being interrogated and become defensive.

Questions to Determine Needs

Questions that serve several different purposes can be used when determining the customer's needs. The types that will be discussed in this lesson are questions to focus attention, questions to gain information, questions to confirm information, questions to give information, questions to qualify customers, thought-provoking questions, defining questions, and closing questions.

Questions to focus attention are often used at the beginning of a sales meeting to focus the conversation on the subject of the meeting. They can also be used in the middle of a presentation if the conversation has strayed from the subject. The salesperson uses these questions to gain control of the presentation. They are usually close-ended questions. For example, a feed salesperson might ask a customer, "Have you seen the results of the trials on our new higher protein hog finishing feed?" This question has a simple answer, but it draws the customer's attention back to the subject the salesperson wants to discuss.

Questions to gain information may be used at any time by the salesperson to identify needs and obtain information about the customer's business. These questions can be close- or open-ended but tend to be close-ended. A salesperson at an implement dealership might inquire of a customer, "Have you ever used our company's no-till drill for planting soybeans?" This question has a yes or no answer, but it gives the salesperson some insight into the experience the customer has had with the company.

Questions can also be used to confirm information the salesperson has already gathered about the customer, allowing the salesperson to find out if his or her research and assumptions are correct. If the information is not correct, the salesperson can gather clues about how to improve his or her methods of obtaining information. These questions also let the customer know that the salesperson has enough interest in his or her business to have done research; they may indicate that the salesperson has been paying attention to the customer's comments as well. For instance, a chemical sales representative might say to a lawn and garden retailer, "I have read that there is a new nursery business in town that may make large purchases of your products. Do you think you will get the bid on their business?" This question lets the retailer know that the salesperson has checked possible business opportunities and is willing to work with him or her to get this business.

Other questions can give the customer information about the salesperson, his or her company, and the product. They can be useful because they not only inform the customer but also draw him or her into the conversation. These questions ask the customer whether he or she knows something about the product or company. A seed salesperson might ask a farmer, "Have you heard about our new line of nematode-resistant, higher-yielding soybean seed, CS123?" This question lets the customer know that this new line of seed exists and suggests some of its important features.

Qualifying questions help the salesperson decide if a prospect is potentially a good customer. These questions provide the salesperson with information

about the customer's buying ability and interest in the product. For example, a chemical company representative might ask a row crop farmer, "Do you control your weed problems by mechanical or chemical means?" Although most fields have weed problems, not all are bad enough to use expensive chemicals; the farmer also may not wish to use chemicals. This question lets the salesperson know whether this farmer would be interested in purchasing the company's new weed control program.

Thought-provoking questions are very useful for getting the customer involved in the presentation and thinking about the information and the product presented. These questions are usually open-ended, so the customer must give more in-depth responses, which cause him or her to think about the product in greater detail. Verbalizing his or her thoughts about the purchase of the product may help the customer see the benefits of doing business. A salesperson might ask the question, "What do you think the pros and cons of purchasing the product are?" After asking this question, the salesperson should sit back and listen to the customer, avoiding interruptions that could disturb the customer's train of thought.

Defining questions are used to confirm a statement the customer has made. They are important if the salesperson is not sure what the customer meant. Usually these questions restate the customer's comment in different words. After restating the comment, the sales representative should obtain confirmation from the customer that his or her understanding is correct.

The salesperson uses closing questions in an attempt to close the sale or get a decision from the customer. The salesperson can directly or indirectly ask the customer to make a purchase. For example, at the end of a sales presentation, the salesperson might ask, "How many units of the product would you like to order for the first shipment?" This question is direct; it assumes that the customer is definitely going to buy the product and only the size of the purchase has yet to be settled.

The salesperson can use any of these types of questions during the sales process. However, some questions are more appropriate at certain times. Practice and experience will help the sales representative learn when and where to use certain types of questions.

Reflective Questioning

Reflective questions are defining questions used when a salesperson rewords something a customer has just said to confirm that he or she has understood the customer. They provide a check of the salesperson's listening skills. Although the salesperson may be listening to the customer, he or she may not be listening carefully enough to understand the message correctly. After the customer makes a statement, the sales representative should rephrase it in his or her own words and get confirmation from the customer that he or she is correct. If correct, the salesperson knows that he or she has done well in listening to the customer; the customer will realize it as well and understand that the salesperson is interested and is paying attention. If the salesperson has difficulty recognizing the customer's meaning, however, then he or she knows that practice in listening is required. The ability to listen carefully is one of the most important skills a salesperson can have. A salesperson must be able to listen and understand what a customer is saying to determine needs and make a sale.

Using Summarizing Techniques

After the salesperson has used questions to discover the needs of the customer, he or she should put together a list of needs. The salesperson should get confirmation from the customer that they agree on the validity of the needs by summarizing the list for the customer. If the list is short, the salesperson should discuss the specific features of the product at the end of the summary and ask the customer for agreement. If the list of needs is long, the salesperson should match the needs and product features one at a time while going through the list and then ask the customer if he or she agrees. In either case, if the customer agrees with the list of needs and the benefits of corresponding product features, the salesperson can attempt to close the sale. In most situations, the customer should not object to the purchase because he or she has already signaled agreement. Done correctly, a summary of needs can lead to a smooth and easy close to the sale.

Summary

Identifying customer needs is essential to making a sale, since the sales presentation must be molded around each customer's specific needs. The customer's personality affects the methods used to

gain information about needs. Different types of questions can be used to learn this information. Open-ended and close-ended questions are used to obtain specific types of answers, and the salesperson must understand when it is best to use each type. Questions can also be formulated to learn different kinds of information. The salesperson must understand the importance of listening carefully and using reflective questioning to check his or her listening skills. A salesperson who does not have good listening skills will have a difficult time learning the customer's needs. Once needs have been determined, the salesperson must confirm them with the customer.

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Lesson 3:
Effective Sales Presentations

The sales presentation is the tool used by salespeople to convey information about a product or service to convince a customer to buy it. It is an essential component of the sales process because the sales presentation gives the salesperson the opportunity to convince the customer that he or she has correctly identified the customer's needs and the product features that meet those needs. While each salesperson has his or her own technique based on personal preference and the personality of the customer with whom he or she is dealing, this lesson covers the components and organization of a standard presentation.

When to Make a Sales Presentation

After a rapport has been established between the salesperson and customer and the salesperson has discovered and confirmed the customer's needs, the sales representative should prepare to begin the presentation. During the earlier steps, the salesperson receives feedback from the customer. This feedback will indicate if the customer is receptive to the salesperson and his or her product. If the feedback has generally been positive, then the salesperson may begin the sales presentation.

Key Components of an Effective Presentation

The key components of a sales presentation are the pre-presentation planning, opening, body, summary, and close. Each of these components is an integral part of the presentation.

Pre-presentation planning - Pre-presentation planning is very important for a successful sales presentation, because it prepares the salesperson to present the product to a specific customer or prospect. Before the actual presentation begins, the salesperson must spend time planning how he or she will tailor the presentation to attract that customer. The sales representative begins by developing a way to open the presentation that will attract the attention of the customer. The salesperson should then identify the features of the product or service that the customer might appreciate and the benefits of those features for the customer. The next step is to organize a list of possible objections to the product that the customer may express, as well as the most appropriate responses to each objection. Finally, practicing the sales presentation in front of others before giving it to the customer will help the salesperson to be more comfortable with it. He or she can use the practice to identify areas that do not flow smoothly or are confusing. It will also help the salesperson to remember how the material is to be presented, which will make the presentation professional. The result of good pre-presentation planning is that the salesperson is better prepared and more confident about the upcoming sales presentation. The more knowledgeable and prepared the salesperson is, the more likely it is that the sale will be successful.

Opening - The opening is an important part of the sales presentation because it sets the stage for the entire presentation. One way in which the opening prepares the customer for the rest of the presentation is by attracting the customer's attention. Gaining the customer's attention is integral to a successful sales presentation. If the customer is not mentally engaged from the beginning, he or she may not pick up on all of the important points of the sales pitch. Attracting the customer's attention is usually done by appealing to a combination of the customer's senses (sight, sound, smell, touch, or taste). For instance, a presentation might begin with a demonstration that would have the customer touch or look at a product while the sales representative talks about it. Once the salesperson has secured the customer's attention, he or she must strive to hold it throughout the rest of the presentation.

Besides attracting attention, the opening also prepares the customer for the content of the presentation. The opening should outline the presentation that will follow. An outline gives the customer an idea of the information that will be presented so that he or she can mentally prepare for it and thus find it easier to absorb the key points.

Three approaches can be used to first address the customer and gain his or her attention. They are the methods approach, merchandise

approach, and service approach. In the methods approach, the focus of the approach is the greeting. The salesperson should greet the customer pleasantly and use his or her name if possible. The sales representative should be direct and straightforward and take control of the conversation. In the merchandise approach, the salesperson's first comments should be about the product, pointing out its main features and advantages. The salesperson using the service approach should begin by asking if he or she can be of service, while avoiding using yes or no questions.

Body - The body of the presentation is the main part of the sales presentation. In the body, the salesperson describes the key features of the product and the benefits the customer will receive with its use. The sales representative should discuss the features and benefits in a logical order, addressing each thoroughly before moving on to the next one. He or she may want to use visual aids to illustrate the product's benefits.

As the salesperson goes through the body of the presentation, he or she should be alert for feedback from the customer. Feedback is important not just in the body but throughout the presentation. When properly monitored and employed by the salesperson, feedback can be used to help the salesperson and customer understand each other. The salesperson should be alert for both positive and negative feedback from the customer to determine what impression he or she has of the product. An example of positive feedback is a favorable remark about the product, while negative feedback could consist of a negative comment or a refusal to buy it. Feedback may also take the form of objections that the customer has about the product or company, which will be covered in greater detail in Lesson 4. In responding to the customer, the salesperson should always give him or her positive feedback.

Summary - When the salesperson has explained the features and benefits and addressed any feedback received from the customer, he or she should provide a summary of the key points of the presentation. The summary allows the salesperson to make sure the selling points of the product are fresh in the customer's mind before attempting to make the sale. The salesperson should then obtain feedback from the customer to ensure that he or she remembers and understands the important points.

Close - The close is the actual confirmation of the sale. Several different methods of closing a sale can be employed. Each salesperson will use different techniques depending on his or her personal preferences and the personality of a particular customer. The various techniques that can be used to close a sale are discussed at length in the next lesson.

Resources for Presentations

A salesperson can use several different resources in the process of constructing a successful presentation. Some of the more common resources used by sales representatives include a customer/prospect profile, product and company data, a list of standard objections and related answers, a list of product features and possible customer benefits, a list of possible approaches or strategies based on personality type, a list of closes, a list of potential attention getters, and visual aids and demonstration materials. These resources can be prepared ahead of time and used as needed.

Customer/prospect profile - After an earlier visit or telephone call, the salesperson (or another salesperson previously in that territory) may have done a customer/prospect profile. The profile can contain vital information about the customer or prospect and his or her company, including identification of decision makers, personality type, financial power, and problem areas. This material can be helpful in the process of personalizing the presentation for a particular customer.

Product and company data - The salesperson should know product and company data well so that he or she can reply to customers if they ask questions. Being able to produce this information readily suggests that the salesperson is confident and knowledgeable about both the product and the company--key points that a customer uses to evaluate a salesperson.

List of standard objections and responses - Salespeople find it very beneficial to list

anticipated objections and responses to them before attempting to make a sale. This list helps prepare the salesperson for customer objections before they arise. If prepared, the salesperson is more confident in his or her responses and is less likely to respond poorly. After a sales representative begins selling a product, customers may raise objections that he or she has not considered. If this occurs, the salesperson may want to add these objections to his or her list so that responses to them can be prepared.

List of product features and related benefits - Writing down a list of product features and related benefits can be both timesaving and thought provoking. Each individual feature should be listed in one column, and all the possible benefits of each feature should be listed in another column. When the presentation is put together, the sales representative can pick the features and benefits that will be most appealing to a customer. Since features and benefits are considered beforehand, preparation time for the actual presentation is reduced. Another benefit is that the salesperson has time to examine the product calmly and pinpoint its best points.

List of approaches or sales strategies - A list of possible approaches or sales strategies based on personality type can be valuable information for a salesperson. The relationship between personality type and approach is not absolute, but this list can help the salesperson choose a strategy that will likely be effective with a certain personality.

List of closes - A list of different closes and how they are implemented can help the salesperson to memorize the techniques for confirming a sale. The sales representative can then readily incorporate the close that he or she feels will work best and implement it easily and accurately.

List of attention getters - Sales representatives should identify several different types of attention getters to attract and hold the interest of the customer during the presentation. They need to be thought through before the presentation to make sure that they will not only gain attention but will attract the right type of attention. Attention getters, which include stories, anecdotes, and special offers, need to be unique and interesting and reflect positively on the product or service. They are usually used in the opening but can be employed later in longer presentations.

Visual aids and demonstration materials - Visual aids and demonstration materials, such as charts, graphs, models, and displays, need to be created before the presentation takes place. The salesperson should make sure that they stress the positive points of the product. These materials represent the salesperson and the company, so they must be well developed and professional-looking, not sloppy or disorganized. The material should be easy to understand and avoid giving unnecessary information. Remember, visual aids are used to stress important points about the product; if they are disorganized or complicated, the material will not be beneficial to customer comprehension or the sales process.

Summary

The decision to buy a product is made during the sales presentation. The salesperson must prepare the best possible presentation to convince the customer to purchase the product. While the presentation will be different for each customer depending on his or her personality type, it requires adequate pre-presentation planning and should include an opening, body, summary, and close. Having good resources is also an important part of putting together a well-developed presentation.

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Lesson 4:
Techniques for Closing a Sale

As the presentation ends, the salesperson's goal is to get the customer to commit to making a purchase. To do so, he or she may have to overcome opposition in the form of objections. The salesperson then has to employ one of several techniques to close the sale, confirming that a sale has been made.

Handling Opposition

The salesperson should learn to handle opposition as effectively as possible, since almost every customer will express some type of opposition. During a sales presentation, the customer will likely give feedback in the form of objections that he or she has about the product or company. Despite their negative content such objections should be viewed positively, because they can benefit the salesperson and the presentation if they are handled appropriately. They indicate that the customer has an interest in the product or service and allow the salesperson insight into the customer's thought processes. This insight can be helpful to the salesperson because it allows him or her to determine whether the customer comprehends the important points of the presentation. A salesperson's openness to customer objections also helps customer relations. A customer appreciates being able to raise questions and concerns without feeling put down or dismissed by the sales representative. In addition, the salesperson conveys to the customer that he or she is confident enough about the product to fully explain both its advantages and its drawbacks. Objections should therefore be welcomed, even encouraged, by the salesperson throughout the presentation.

Objections should generally be handled immediately. This approach benefits the salesperson, since the customer is then more knowledgeable about the product. However, if a sales representative is not going to handle the objection at once, then he or she must acknowledge the objection and explain why it will be discussed later. For example, the customer may have jumped ahead in the presentation and asked a question concerning a feature that will be discussed in a few minutes. In that case, the salesperson should restate the objection to the customer to confirm that he or she understood it correctly and tell the customer that it will be discussed later. The salesperson should verify that the customer does not have a problem with the delay before continuing with the presentation.

Negotiation skills are essential to handling objections. The salesperson must negotiate between the customer's beliefs and the facts that the salesperson is using to overcome the objection. The method that should be used to handle resistance depends on the type of objection raised. Two types of objections are valid and hidden objections.

Valid objections are statements made by the customer that are true or at least true based on the customer's knowledge. The comment, "Your product is more expensive than the competition," is an example of a valid objection. These objections are a good indication that the customer has a desire to buy. The sales representative should immediately address valid objections; he or she should *never* ignore them or wait until later to respond to them. The salesperson should restate the objection and confirm with the customer that he or she has understood the point. The next step is to discuss the objection and attempt to downplay its importance by stressing other, more positive features of the product and all the benefits that the customer will gain from purchasing it. After attempting to decrease the significance of the objection, the salesperson should ask the customer if the positive features and benefits outweigh the objection in importance. After dealing with the objection, the salesperson should review the benefits of the product that will help to sell it.

Hidden objections, or smokescreens, are objections made by the customer to disguise true objections. The customer may use a smokescreen because he or she is embarrassed to reveal the real objection, may not recognize it, or may not want to deal with it. For example, the customer might say that he or she does not need the product, when in reality a need exists, but the money to make a purchase is not available. Hidden objections are clues to the salesperson that the customer has other objections that must be discovered and addressed. The best method for uncovering a real objection, especially if the customer has stopped talking, is to ask the customer direct, specific questions until all possibilities but one have been eliminated. An indirect question can also be used if the salesperson feels that the customer is still willing to talk openly. Once the salesperson thinks that the true objection

has been identified, he or she should restate the objection to confirm that it is correct. The sales representative can then follow the method described in the preceding paragraph for dealing with valid objections.

A related problem that a salesperson might encounter is a misunderstanding. In a misunderstanding, the customer raises an objection based on his or her misinterpretation of information or on misinformation. The salesperson should restate the misunderstanding to ensure that he or she has understood the customer and then candidly refute the misunderstanding by providing proof of the facts. If the customer agrees that the objection was based on a misunderstanding, the salesperson should reemphasize the features and benefits of the product and obtain verification from the customer that he or she understands them. The sales representative may then attempt to close the sale if the customer raises no other objections.

When to Close the Sale

Because closing can happen at any time, the salesperson should be ready to close the sale from the beginning of a meeting with a customer. Going through an entire presentation may not be necessary if the customer is ready to buy the product. If the customer is not ready to make the purchase, however, the salesperson should consider closing the sale when he or she has completed the presentation and dealt with all of the objections.

The sales representative should review the presentation before closing the sale. He or she should think about the customer's feedback. If the feedback has been extensive and positive, the salesperson can assume that he or she has done a sound job of presenting the appropriate information and can attempt to close the sale. If the feedback has been limited or negative, a possibility exists that the salesperson has not presented the product features and benefits that appeals to that specific customer. The salesperson needs to consider what he or she knows about the customer and the business and review the presentation to see if any important selling points have been omitted. If important information was not included, that material should be covered before the salesperson attempts a close.

Methods for Closing a Sale

Many different methods may be used to close a sale, but this lesson will focus on the six most common methods. They are direct, assumptive, summary, choice, conditional, and loss-in-waiting closes.

Direct close - In the direct close, the salesperson asks the customer to commit to purchasing the product. This type of close is extremely effective, especially when dealing with a person who has a very direct personality. The salesperson asks a direct question, such as "Why don't I fill out the order form?" or "What quantity would you like to buy?" A sales representative using this method should be very confident that all objections have been covered and that the customer is ready to buy. If the salesperson has not completed his or her job in selling the product, he or she risks offending the customer by forcing a decision.

Assumptive close - The salesperson using the assumptive close assumes that the customer or prospect is committed to buying the product based on the feedback received. This close provides an easy transition for both the salesperson and the customer because it flows directly from the presentation at the point that the sales representative believes that the customer is ready to commit. When the salesperson feels that the customer is ready to buy, he or she begins working out the details of a purchase (i.e., setting up the delivery, filling out paperwork, etc.). If the assumption is correct, then the sale has been made; if not, the customer will inform the salesperson about his or her mistake. The salesperson needs to discover what objections the customer still has and address those concerns. The salesperson may then use the assumptive close again or try another technique.

Summary close - The summary close is an indirect style. The salesperson summarizes the points of the presentation and emphasizes the features and benefits of the product that both parties have agreed on in a final attempt to assure the customer that it would be a good purchase. As each point is raised, the salesperson should obtain agreement from the customer. If they agree on all key points and the customer raises no other objections, the sale has generally been made. The sales representative then asks for the order, usually with a direct question. If the salesperson has done a good job of covering all the significant features and benefits and has

received positive feedback on each, the customer should be ready to buy.

Choice close - In the choice close, the sales representative gives the customer a choice between one buying option and another, but not the option of not purchasing the product. "Would you like to purchase one load of the new herbicide, or two?" is an example of a choice close. Technically, the salesperson has not even acknowledged that saying "no" is an option. This method is employed when the salesperson is confident that the customer is going to buy something and just needs to decide what to purchase. The salesperson would not want to use this close unless he or she has received only positive feedback and is certain that the customer has no more objections. Although the customer can still refuse to make a purchase, a refusal is not likely if the salesperson has done a complete job of selling the product.

Conditional close - This close is generally used if the customer is expressing some hesitation about buying the product. The salesperson might then present a condition, or qualifier, for purchasing the product. For example, he or she might say "If I can _____ (get a better price, ensure a faster delivery, etc.), will you purchase the product?" This close can be very effective, especially if the salesperson believes one detail is keeping the customer from agreeing to the purchase. However, no promises should be made that cannot be fulfilled. In other words, the sales representative should not ask for a commitment if he or she cannot deliver what is promised to the customer.

Loss-in-waiting close - The loss-in-waiting close can be employed in different ways. The sales representative may inform the customer of the positive aspects of buying now rather than later. Considerations such as future price increases may convince a customer to proceed with the purchase. The salesperson may also use this close when telling the customer that an item may be unavailable later. In either case, the salesperson must always be truthful. He or she should not mislead the customer into thinking that purchase is a "now or never" situation if it is not.

When closing a presentation, the sales representative should take the customer's personality and communication style into consideration. For example, most controllers would prefer a direct or choice close, because they give them the opportunity to make a decision. Supporters, in contrast, may prefer a more casual assumptive close. The timing of the close may also be affected by the customer's personality; an analyzer, for instance, will need more time to make a decision than a controller.

Summary

In making a sales presentation, the salesperson will likely face some form of opposition from the customer. The salesperson should be prepared to handle it in the most positive way possible and overcome any objections the customer may have. When all objections have been addressed, the salesperson should attempt to close the sale. Several different methods can be used to close the sale successfully, depending on the sales representative, the customer, and the sales situation.

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Lesson 5:
Customer Service

The salesperson's duties do not end once a sale has been made. He or she still has a responsibility to maintain a positive long-term relationship with the customer. Providing good customer service is an important part of this relationship.

Supporting the Customer's Decision to Purchase

Once the customer has decided to purchase an item, the salesperson's job is to reassure the customer that he or she has made a good decision. One of the first things that a salesperson should do is compliment him or her on the decision. The salesperson should then restate the benefits that the customer will gain from the purchase to reassure him or her about its positive aspects.

The salesperson should inform the customer of the delivery time of the product and assure the customer that he or she will personally check to make sure that all orders are delivered. After the shipment is delivered, the sales representative should immediately contact the customer to confirm that the order was correct and the customer is satisfied with it. This phone call will give the customer a feeling of security by assuring him or her that the salesperson is still interested in their business relationship. If any problems do occur in the delivery, the salesperson should deal with them honestly and as quickly as possible.

The salesperson should also be readily available to the customer to answer questions or deal with problems. The customer will then likely feel more secure about the long-term relationship between them. The customer will also feel as if he or she has made a good decision in choosing the salesperson's product and company.

Processing an Order

Certain steps must be completed when placing an order for a customer, although different companies or customers may require variations of these steps. The first step is to get the order from the customer and fill out the paperwork required to place the order. After writing down the order, the salesperson should review the order with the customer to make sure that the information about the product and amount of payment is correct. The salesperson should also check the customer's name and the shipping and billing addresses on the order for mistakes.

The second step is to discuss the method of payment for the product. If the customer is going to pay cash, then both the salesperson and the customer should agree on the time of payment--either immediately, at delivery, or within a certain time after delivery. If the customer is going to set up a credit account, the salesperson must explain the details of the credit account, such as the length, number and size of payments, penalties for delinquent accounts, etc. He or she then normally calls the company's credit department and gets approval to set up the account.

The next step is to place the order with the company so they can begin processing it. The salesperson may call in the order to the company. If possible, the salesperson should find out the delivery time when placing the order and check with the customer to make sure he or she will be available to take delivery. If this cannot be done at the time the order is made, the customer should be contacted when a time is set.

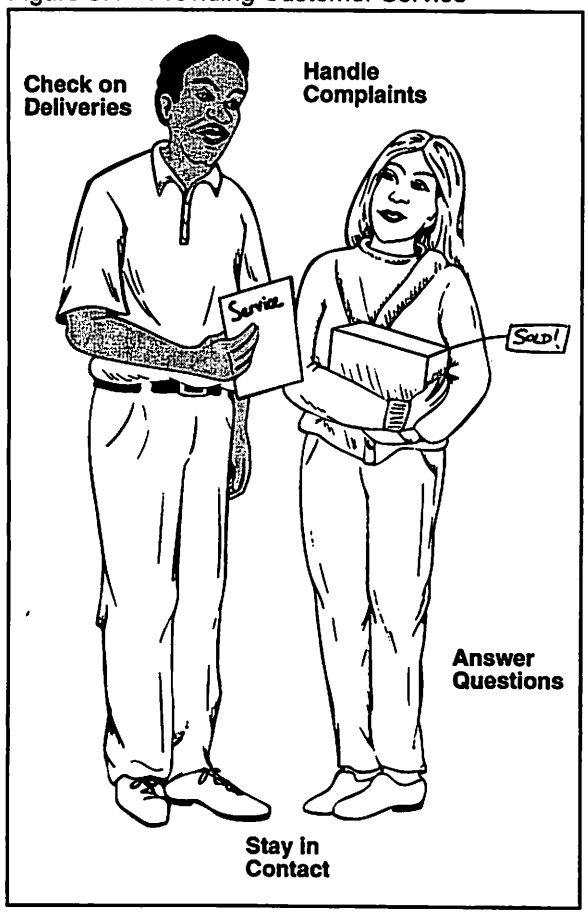
The last step is to process all the paperwork involved in placing the order. The order may need to be typed up or entered into a computer system. The customer should always receive a receipt for his or her records. Other copies may need to be sent to the salesperson's supervisor, as well as the credit, shipping, and accounting departments.

Maintaining Positive Long-Term Relationships

Maintaining the relationship between the customer and the salesperson must be an ongoing process. The salesperson has to invest a great deal of time and effort in the relationship if it is to remain a profitable alliance. The salesperson will initiate different strategies for maintaining the relationship based on his or her personal preferences, the customer's personality, and the type and size of the account. These activities are usually not directly related to the sales process but are still vitally important to continued sales.

One of the most important things that a salesperson should remember is to stay in contact with the customer. Frequent contact lets the customer know that the salesperson is still interested in his or her account. It also gives the customer an opportunity

Figure 5.1 - Providing Customer Service



to discuss any progress or problems with the salesperson.

An essential component of maintaining a good long-term customer relationship is handling complaints well. Depending on the customer, handling complaints may be a difficult job for the salesperson. When a customer voices a complaint, the salesperson must find out if the customer, product, or company is at fault. Once this has been determined, the salesperson must handle the complaint appropriately. To do so, the salesperson must obtain information about the customer, know the company's policy for handling complaints, and learn how to get any necessary information concerning the complaint. If the product and company are at fault, the customer must be compensated in some way so the business relationship will not be permanently damaged. The salesperson should follow the company's guidelines in compensating the customer and *never* promise the customer something that he or she cannot deliver. If the salesperson finds out that the problem is due to the customer's error, the company is not liable. However, if the customer thought that he or she was at fault, no complaint would have been made. The salesperson therefore needs to be very diplomatic, since he or she does not want to anger or offend the customer.

Another part of maintaining a good relationship with the customer is being reliable and honest. The customer needs to know that the salesperson will be available to help with difficulties. If the customer cannot count on the salesperson to provide assistance, he or she will likely find another company and sales representative. Besides being reliable, the salesperson should always be honest with his or her customers. Being dishonest will eventually catch up with a salesperson, and he or she will lose business. Even if the truth is uncomfortable or might cost some short-term business, long-term relationships will be stronger because customers will know that they can trust the salesperson.

Strategies for Collecting Past Due Accounts

The subject of overdue accounts is very sensitive for customers, salespeople, and the company. The salesperson may handle overdue accounts in different ways based on the reason the account has not been paid and the amount that is due. The reasons why an account is overdue may or may not be legitimate and reasonable.

The first thing that a salesperson must do is to find out why the account is overdue so that he or she can deal with the problem appropriately. The salesperson must talk to the customer about the problem. In a worst case scenario, the customer does not intend to pay or is attempting to wait as long as possible to pay. This situation does not occur often. Usually the customer is having a genuine problem with paying; he or she may be having financial difficulties but intends to pay the bill as soon as possible. The customer may also have not realized that the payment was due or may have misunderstood the terms of the credit agreement.

The sales representative should follow company policy for dealing with overdue accounts. Often, the appropriate response depends on the reason the account has not been paid. The customers who do not intend to pay or who are waiting to pay are obviously not good long-term customers, and the credit department of the company should take over the collection process. Customers with financial

problems could use the assistance of the salesperson, either to help them through their financial problems or to work out some type of extended payment plan. Customers who simply do not realize that payment is due are often poor financial managers, and the salesperson should work with these customers to help them remember to pay on time. Usually, a polite but firm phone call will yield the payment. In the future, the salesperson may want to keep track of when payments are due and give the customer a phone call a few days ahead of time as a reminder. Finally, the salesperson should meet with customers who have misunderstood the terms of the credit agreement and review the terms so no future misunderstandings about the payment plan will occur. The salesperson should be patient with the customer, because the salesperson's job is to cover this material at the close of the sale and make sure that the customer understands.

Summary

The best customers are long-term, loyal customers. Maintaining a good business relationship starts with supporting the customer's purchase and processing the order. The salesperson then needs to provide reliable customer service, which includes maintaining contact with the customer, handling any complaints, and being reliable and honest when dealing with the customer. The salesperson is the liaison between the customer and the business, so problems like product complaints or overdue accounts will be handled by the salesperson first. The salesperson must do everything possible to address these problems and satisfy the customer.

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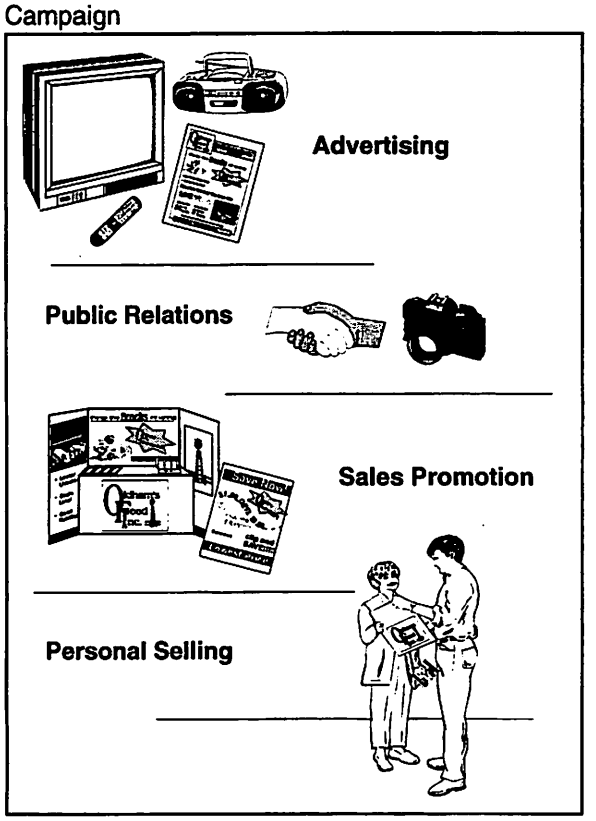
Lesson 1:
Developing a Promotional Campaign

Promotional campaigns are used to inform potential customers of products and services that are available, to create interest in the products, and to persuade potential customers to make a purchase. Knowledge of how to develop a promotional campaign is important because they can be expensive and need to be used wisely to create sales.

Components of a Promotional Campaign

Promotional campaigns are programs instituted and paid for by a business that present the merits of its product or service or of the business as a whole to increase sales. Product promotion publicizes the products of a business, while institutional promotion is designed to improve the image of the business. The components of a promotional campaign are advertising, public relations, sales promotion, and personal selling (Figure 1.1). While these components may be a part of a unified promotional campaign, they are also sometimes used separately.

Figure 1.1 - Components of a Promotional Campaign



Advertising is a promotional message that a sponsor pays to have placed in different media such as newspapers and radio. Advertising can inform potential customers about the nature of the product or service being offered, where or when they can purchase it, and how much it will cost. Advertising seeks to influence consumers' perceptions of their wants and needs. It generates business by convincing customers that the product or service satisfies one of their needs or wants. A business may use advertising to tell consumers about how a product or service saves time and money, provides greater convenience, increases knowledge, improves their health or safety, improves a skill, increases recreational time, or fulfills another necessary or desired function. Advertising can also increase sales by influencing potential customers to see their wants as needs.

In order for a business to continue to operate, sales transactions must take place. Advertising is important to continued sales because it can increase business by attracting new customers and encouraging previous customers to return. Once the customers are drawn to a business, other components of a promotional campaign can be used, such as public relations, product display, and personal selling.

The public relations component of a promotional campaign involves performing various activities designed to create a positive image to promote goodwill toward a business. Businesses develop public relations programs to help consumers recognize what a business contributes to the community. Public relations programs can help a business and its product or service gain acceptance by the community. A good public relations program pays off by increasing the sales of a product or service. A public relations program might consist of several elements, such as participation in the community, educational tours of facilities, or newsletters. A good product or service, a good physical appearance, trained and courteous employees, and good service are also important in developing a good image for a business.

Sales promotion is a third component of promotional campaigns. It includes the use of coupons, rebates, contests and sweepstakes, and visual merchandising such as displays. The goal of using these devices is to increase the sales of a business by encouraging customers to make purchases. Coupons and rebates induce customers to purchase

a particular product by offering savings. Contests and sweepstakes generate excitement about a product or business. Displays attract buyers by using the well-designed presentation or the product itself to catch the attention of potential customers.

Of these sales promotion devices, display is the most complex to use because it involves visual presentation and must be put together to be appealing to the eye. Displays promote either a product or a business. A product display involves making a prominent exhibit of the product or service being sold. Product displays vary, from counter displays, to large stacked displays in retail stores, to window displays, to products featured at fairs, trade shows, or other exhibits. Institutional displays serve a public relations function, promoting the image of the business rather than a specific product. Examples of institutional displays include displays devoted to a community activity in which the business participates and decorations for holidays.

Personal selling is the fourth component of a promotional campaign. It often requires the person selling a product or service to perform the tasks of advertising, public relations, and sales promotion. He or she must add personal persuasion to these elements in a sales presentation made to convince the potential customer to make a purchase. Personal selling involves advertising in that the person selling the product must present the merits of the product or service. Public relations is a part of personal selling because the salesperson must promote goodwill toward the business by creating a positive image. A salesperson is involved in the product display aspect of sales promotion because he or she must show the product in a positive way to persuade the potential buyer that the product being sold meets his or her needs.

Personal selling may also require that different people perform various tasks to complete a sale. Even businesses that people consider to be self-service require certain aspects of personal selling to complete or increase sales. The person who greets customers as they enter a business performs a public relations function by making customers feel welcome and letting them know they are appreciated. The person who directs a customer to the location of a product, the person who operates the cash register, and the person who is responsible for keeping the business clean and orderly all perform public relations tasks. A person who puts signs or labels on merchandise is involved in advertising the price or description of the product being sold. The employee who fills the counters or creates a display performs the sales promotion segment of personal selling.

Ultimately, promoting sales is the responsibility of all employees of a business. Promotional campaigns are a vital part of a market economy in a free enterprise system like the United States. By encouraging customers to make purchases, they provide the means by which businesses can make a profit.

Determining Promotional Strategies

Determining the best promotional strategy for a business will depend on the type of business it is and the product or service it provides. A carry-out pizza place might not remain in business if it were not listed in the yellow pages of the phone directory, because that is the first place customers will look for information about that type of business. An insurance agency would not do very well without personal sales of policies, because customers require a great deal of information to convince them to purchase an intangible product. Although a particular promotional strategy may work best for a business, however, the right combination of advertising, public relations, product display, and personal selling forms a promotional mix that is the formula for success for most businesses. The pizza place might rely heavily on the advertisement in the yellow pages, but personal selling may be used to obtain extra sales; employees might ask whether customers would like some bread sticks or a beverage with their order. The insurance company may rely heavily on personal selling, but advertising to raise the confidence of customers is also a major promotional tool for insurance companies. The slogans, "Like a good neighbor," "You're in good hands," and "The Rock," are readily identified with State Farm, Allstate, and Prudential.

The result of any promotional campaign should be an increase in demand for the product, service, or institution being promoted. One question that needs to be answered when formulating a promotional campaign is what segment of the population forms the market. The next question that needs to be answered is what promotional tool will be the most effective at reaching that market. The final question that needs to be answered is how demand for the product or service can be generated. The amount of money to fund a campaign available will also influence the promotional strategies chosen by a business.

To choose a successful promotional strategy, a business needs to know who its target customers are. It therefore needs to examine the characteristics of the market for its product or service. Information on place of residence, age, sex, income, preferred media source of information, and the competitors that potential customers currently patronize is important. A business also needs to determine what motivates the target customer to buy a product or service--price, quality, prestige, etc. Once all this information has been gathered, the business can use it to determine the form of promotion that will reach the most customers and how demand for a product or service can be created. For example, information on where targeted customers live suggests where the business should focus a public relations activity to do it the most good. A business can use data on the age, sex, and income of customers to determine whether an ad should be placed in the sports, business, or community news section of the newspaper.

To determine the effectiveness of a promotional method, information on its cost, the total number of people reached, how often potential customers come in contact with the promotional message, and the level of sales generated is required. A business can gather this information in several ways. New businesses often conduct surveys that question customers about where they heard about a product or service, which may indicate that one part of a promotional campaign is more effective than another. Businesses that include coupons in their newspaper advertisements can use details about where the ad is placed and how many coupons are returned to determine what sections of the newspaper offer the best return and which items draw the greatest response. Newspapers and radio and television stations may give a business information about their audience. If the sales and general effectiveness of a promotional strategy do not justify its cost, the campaign may need to be changed.

A business needs to know exactly how and where competitors promote their product or service to be able to improve on their strategies. The business might run a special sale on an item as a part of its promotional campaign, but if the price is still higher than a competitor's, the promotion is wasted. One way to avoid such problems is to keep a record of the promotions carried out by competitors in the past. Information on past prices, especially on competitive items, can be especially helpful when planning a promotional campaign.

Example: Jerry has operated a lawn and garden center for several years. He sells trees, shrubs, evergreens, annuals, and perennials, and repairs lawn mowers, gasoline trimmers, and chain saws. Jerry has the only business of this type in the community and is doing well. He has now decided to expand his business to include selling new lawn mowers, trimmers, and chain saws. Another business in town sells the same products, and Jerry wants to find out how he can create a demand for his own. He talks to several of his customers who have purchased products from his competitor, asking them what they liked and disliked about purchasing lawn equipment from the other business. Some customers tell him that they liked the low prices on some of the equipment, while others liked the fact that they could buy higher-priced, quality products. Jerry receives the same answer on what they disliked. All of the people he asks say that they disliked purchasing a product and then having to take it somewhere else to have it serviced or repaired.

Using this information, Jerry puts together the following promotional campaign for the first year to test the market.

- Create a prominent display area for the new merchandise.
- In his next lawn and garden newspaper advertisement, include one low-priced lawn mower and trimmer and one high quality lawn mower and trimmer. Feature them at a lower price than the competition. At the bottom of the advertisement, print in large letters "WE SELL AND SERVICE LAWNMOWERS, TRIMMERS, AND CHAIN SAWS."
- Run a similar program in late summer for chain saws to promote chain saws for the peak fall selling season.
- Change the advertisement in the yellow pages to include the phrase "Sales and service of lawn equipment."
- Instruct all of his employees to include the information in their personal selling presentations that the business not only sells but also services and repairs lawnmowers, trimmers, and chain saws.

- Include the store's name and address and the telephone number to call for service or repair on all product displays, packages, and business cards.

- Sponsor a youth softball team.

Jerry used information on what his target customers liked and what motivated them to buy to design his promotional campaign. He has used advertisements, public relations, sales promotion, and personal selling to increase demand for the product and service. Once Jerry sees how the changes affected sales and studies how his competitor reacts to his promotion, he can make further adjustments to the promotional campaign.

Summary

The components of a promotional campaign include advertising, public relations, sales promotion, and personal selling. Knowing how to develop a promotional campaign is important to a business because such campaigns are expensive and need to be used wisely to create sales. Choosing the right combination of components for a promotional campaign depends on the type of business, the market for the product, the effectiveness of different promotional strategies, and the strategies used by the competition.

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Lesson 2:
Advertising

Advertising is essential in building a business. Because of its expense, advertising needs to be used effectively to reach as many customers as the advertising budget allows.

Advertising Media

Advertising media are the means of communication by which a business tries to encourage customers to purchase a product or service. The advertising media available to a business may vary depending on the size and location of the community. Newspapers, magazines, billboards, and direct mail are all commonly used forms of print media, in which advertisements are presented in writing. Radio and television are forms of broadcast media. Internet technology has now made web advertising another option for businesses.

Newspapers are the main source of advertising for many types of businesses because of their many advantages. They are popular with businesses because they are generally available in most communities, which allows a local business to reach its customers with information. Newspapers also have a large readership, because they have in-depth coverage of national and/or local news stories as well as coupons for various products and businesses. These coupons are an important asset in advertising, because they can be used by the customer. The circulation of a paper is known, which allows a business to insert advertisements that can reach a targeted group of customers. Newspapers are especially useful for promoting specific items and can create sales very quickly. Another benefit of newspaper advertising is that space can be purchased and ads printed in a very short time, making changing existing advertisements to meet new circumstances fairly simple. Finally, newspapers are a relatively inexpensive way of advertising due in part to the quality of the printing and paper. In addition, many daily papers charge subscribers for the newspapers, which lowers the cost of publishing and therefore the cost of advertising.

Newspaper advertising also has certain disadvantages. Many newspapers have a wider circulation than a business's targeted customers, and the advertiser must pay to reach people who will not be interested in the product or service. A newspaper ad may not be very noticeable because of the large number of advertisements that appear in the newspaper. The advertisement may have limited usefulness, since many subscribers will dispose of the newspaper after it is read. Newspaper ads may not be very attractive because of their quality.

Magazines are often used to advertise to a national audience, although some areas may have local magazines for a city or region. Magazines used for advertising may include general interest magazines that will reach a wide audience, specialty magazines that are targeted at people with particular interests (hunting or music, for example), or trade publications that are aimed at a specific business area. One major advantage of magazines as an advertising medium is that the characteristics of the readers are known, which allows advertisers to select a magazine that targets their business's customers. A business that sells sporting goods would advertise in a sports magazine, while a business that provides medical supplies would advertise in a trade magazine. A second advantage is that magazines are often read more slowly and thoroughly and are kept for longer period, both of which make it more likely that an advertisement will be read. The quality of magazine ads is also generally much better than newspapers. Most magazines use high quality, glossy paper and include full color ads.

Compared to newspapers, advertising in magazines has less appeal for small businesses. Most magazines have a wider readership than the geographic area served by a small business. Advertising dollars would be wasted outside the business's market. Because of wider circulation and increased costs for paper and printing, magazine advertisements are much more expensive than newspaper ads. Finally, because the ads must be submitted six to eight weeks before the publication date, magazine advertising is not very flexible.

Most billboards are located on major highways to inform passing motorists of the services available in nearby communities. While they are still commonly used by both national and local advertisers, concerns about safety and the quality of the scenery have led some areas to restrict their size and usage. The advantage of billboard advertising is that the location of the billboard--next to major roads where it may be read by potential customers for 24 hours a day--allows many people to read it. Billboards are

also relatively inexpensive compared to other forms of advertising.

Advertising on billboards has some negative features. The message on a billboard must be simple. A customer will only have a short period of time to read the message. In addition, some people try to ignore billboards because they consider them to be a form of highway litter and a hazard to traffic safety.

Both large and small businesses may advertise through direct mail by gathering lists of previous or prospective customers and sending them some sort of mailing to advertise their product or service. Some companies sell lists of potential customers to other businesses to use for direct mail advertising. Advertisers can be highly selective when deciding who will receive the advertisement, which gives the ad a better chance of reaching the target audience. Direct mail advertising can be a timely method of informing customers about the business. It can make use of many different formats, giving the advertiser a wider choice about how an advertisement will be put together. Finally, using direct mail can keep competitors from seeing the advertisement.

A disadvantage to direct mail advertising is that mailing lists can become outdated. The advertisement is then not received by the intended targeted customer. Another problem is the advertising dollars may be wasted on direct mail, because many people see the mailings as junk mail and discard them.

Radio advertisements consist of spots ranging from fifteen seconds to a minute in length. It is fairly inexpensive, particularly when compared with magazine or television advertising. Radio advertising is available in most communities, providing wide coverage of the market that is very useful for local businesses. Advertisers using radio can target specific types of customers by advertising on radio stations to which they are more likely to listen. Most radio stations do extensive market research to gather information on the type of people that listen to their station. Another advantage is that radio advertisements can reach customers wherever a radio is present. Many people listen to their radios in their cars, at work, while exercising, or even while attending a sporting event. Radio advertising is also very flexible; ads can be adjusted just by changing the announcer's script.

Advertising on the radio has some disadvantages for advertisers. The ad lasts a very brief time and leaves the potential customer with no reference for the information. Because no visual component is provided, listeners may also be easily distracted during advertisements. The short life of ads and the possibility of being distracted makes repetition necessary for successful radio advertising. Most radio advertisements are repeated several times during a day to increase the likelihood that potential customers will receive the message.

Advertising spots on television range in length from ten seconds to one minute, with 30 seconds being the most common length. The cost varies according to length and when the commercial is aired. The prime time hours of 7 to 11 p.m. are the most expensive. Television commercials have the advantage of consisting of both visual and audio elements that can appeal to an audience. Repetition is still a necessary feature, but the message has a greater chance of catching the attention of targeted customers because of the added visual element. Another benefit of the visual component is that people are more likely to accept what they can see. Television can also be used to reach a mass national audience or on a regional level.

While television advertising does have several benefits, television is also the most expensive advertising medium. The high cost keeps many small businesses from using television for advertising or limits them to using it only during less desirable time slots when rates are cheaper. A second disadvantage is that the size of the audience fluctuates according to viewer interests. Many viewers consider commercials a nuisance and ignore them. Viewers also may not be interested in the programming airing on that station when the commercial is broadcast; the majority of viewers may be watching something else. In either case, advertising dollars are wasted.

The increasing use of the Internet as a means of communicating information has led many businesses to hire Internet marketing businesses and web page development companies to develop web advertising as a part of their advertising mix. In addition to web sites promoting their products or services, some businesses also post banner advertisements on sites that many people visit, such as search engines, with links to their web pages. Advertising on the Internet can have several advantages. Advertising on the Internet can

potentially reach millions of customers. Because of the growing number of Internet marketing and web page development businesses, prices are becoming very competitive. The costs of implementing a home page can be relatively low compared to other forms of advertising. Internet advertising can therefore be a cost effective way of reaching a large number of consumers. Another advantage is that the technology of the Internet allows advertising to be very creative. Sound and animation can be used to enhance the web site and attract customers. Disadvantages include the difficulty customers may have in finding the advertisement of a particular business among the huge number of web pages available on the Internet. A second disadvantage is that it is difficult to determine how effective the page may be in attracting customers, leading to wasted advertising dollars.

Components of an Advertisement

Certain guidelines should be followed to develop an effective advertisement. The necessary components of print advertisements include the headline, copy, illustration, and signature or logo. These elements are illustrated in Figure 2.1 on the next page.

The headline is the line of print that is designed to catch the reader's attention. Headlines should be short and have a single, simple main idea. They should tell the reader only enough to attract interest and entice him or her to read the rest of the advertisement. A headline might announce a new product or include information to shock or surprise the reader. Putting a new spin on familiar phrases or sayings or using strategies like puns or plays on words can be very effective in getting the reader to examine the rest of the ad. Good headlines often appeal to the reader's self-interest in some way.

The copy is the main message of the advertisement. The copy should give more information related to the headline. It may be relatively short or consist of a number of paragraphs of information, depending on the needs and interests of the audience. The copy should make contact with the audience. Contact might be established by appealing to the reader's senses, using a dramatic tone, giving important information about a product or service, or explaining its benefits. The goal of establishing contact is to encourage enough interest in the reader for him or her to purchase the product or service being advertised. The copy should therefore also include a call to take action and make a purchase.

The illustration is the picture or drawing in the advertisement. The illustration is usually the first part of the ad to attract the reader's attention. It should encourage the potential consumer to read the advertisement and make a purchase. The illustration might highlight the product itself or explain the need for it. It might also give a sense of the product's benefits or uses.

The signature or logo is the symbol of the business. A well-designed signature is instantly recognizable. The signature generally consists of the name of the business as well as a trademark (like the Nike swoosh). It might incorporate a slogan--a short phrase that is identified with a business. For a local business, the signature could also include general information about the business, such as its address, telephone number, and hours of operation.

The layout of these elements in an advertisement can affect how effective it is. For example, the advertisement in Figure 2.1 is laid out in a "z" formation. The content of the ad roughly forms the shape of a "z," which helps the customer's eye flow to the most important information.

Billboards differ from other forms of print advertising in that they must be extremely short. The main component of a billboard advertisement is a short message that attracts the attention of the potential customer in a very brief period. It must convey the message quickly because potential customers pass by rapidly. In addition to this short message, a billboard should include an illustration and the signature of the business.

The key component of both radio and television advertisements is the script. The script can be read by a single announcer, or it can be more elaborate, with dialogue, music, and sound effects. The script can be written to dramatize a scene or incorporate customer interviews. It needs to be delivered by believable announcers or actors who inspires listeners to pay attention to the advertisement. Many radio and television commercials include a jingle associated with a business.

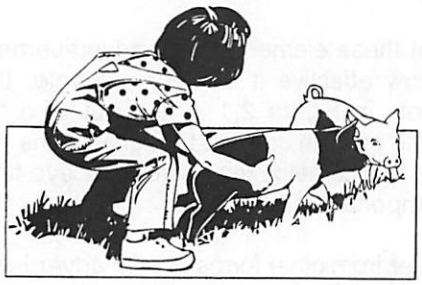
Television advertising also incorporates a vital visual element that appeals to the viewer's sense of sight. The ability of television to allow potential customers to see as well as hear the advertising message encourages the use of creative methods to grab the viewer's attention. Television advertising can include product demonstrations, dramatizations of events, and special effects. A television

Figure 2.1 - Print Advertisement

Oldham's Feed Inc.

Featuring Oldham's Own Hi-Protein Swine Starter™

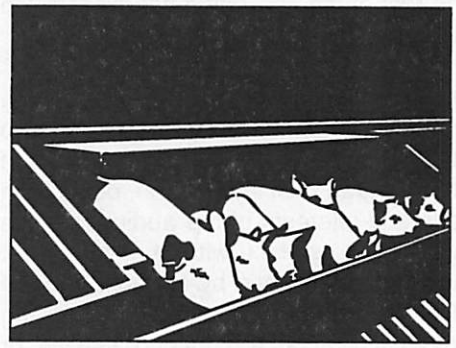
Reap the Benefits of using



Oldham's Own Hi-Protein Swine Starter™

- Low Cost, High Yield!
- Leaner Livestock!

The More You Buy The More You SAVE SAVE SAVE



Starter Mix $8.99 50 lbs.

Grower Mix $7.99 50 lbs.

Visit Your Local Oldham's Feed Store Today!

Mon.-Fri. 8:00 A.M. to 8:00 P.M.
Sat. & Sun. Noon to 6:00 P.M.

1200 West General Street
Any Town, Any State, 10000

advertisement can be delivered with action and color that effectively attract the viewer and encourage him or her to buy the product or service.

Creativity is important in developing any type of advertisement. The potential customer should be able to separate a business from its competitors based on its advertising. The imagination and creativity displayed in an ad may play a large role in convincing the customer to buy a product from a business rather than its competitors. Many newspapers, radio and television stations, magazines, and billboard advertising companies offer free services to individuals and businesses to help them develop ideas and produce advertisements. Professional advertising agencies can also be hired to help businesses develop advertising campaigns.

Summary

Many alternatives exist for advertising, including various types of both print and broadcast media. For some businesses, one advertising method may be all that is necessary for an effective advertising program, while other businesses may need to utilize a combination of several methods to reach their customers. When choosing a form of advertising, a business must take into account its advantages and disadvantages. It should also make sure that any ads it develops have the necessary components to make them effective in attracting customers.

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Lesson 3:
Public Relations

Many businesses use public relations as a promotional tool, not to promote a product, but to promote the business itself. A good public relations program can build approval for a business and its employees within the community. Although public relations can help a business, no promotional tool can offset an unsatisfactory product or service. A history of satisfied customers and employees provides the best public relations for a business.

Public Relations

Public relations involves attempting to create a positive image of a business. The primary function of a public relations campaign is to promote goodwill toward the business. It is designed to gain acceptance of a business and its product or service by the community to win the loyalty of customers. A public relations program should also contribute to an increase in sales by appealing to prospective customers.

Components of a Public Relations Campaign

A public relations campaign may consist of several different activities. Businesses need to take their needs and budget for public relations into consideration when choosing the activities for campaigns.

One component of a public relations campaign is community participation. Community participation has become a common promotional tool for public relations. It may include providing financial support for charities and local organizations like the United Way or the local Chamber of Commerce. Community participation may also involve encouraging and supporting employees who become involved in community programs and activities such as fund-raising programs, community clean-up projects, restoring community landmarks, remodeling a city park, or other projects that help the community. By participating in community activities, a business can show that it recognizes its responsibility to the community. It also helps the business to identify the needs of consumers and problem areas connected to its activities by providing members of the community with an opportunity to personally present their concerns about a business to its employees. By identifying problems or misunderstandings, a business can use participation in the community to help correct them. Community participation has the added benefit of providing a means for businesses to work together within a community to fulfill common goals.

Many businesses host educational tours as part of a public relations program. Tours help the youth and other members of the community obtain a better understanding of the business and its product. Some businesses work with local schools to aid in instruction by providing students with real-life examples that relate to material they have been studying. This public relations activity makes education more interesting for students in addition to helping the community to comprehend the activities of the business in producing a product or service.

A business may promote public relations by providing support for youth. Businesses frequently sponsor awards to support excellence in education. These awards might consist of scholarships for college or technical school or certificates for outstanding achievement. Another way that business provides support for youth is by sponsoring athletic teams or other activities. Supporting youth by providing awards and activities encourages parents to support the business in return. The business also tries to retain the loyalty of the young people.

The activities of a business may be newsworthy, and it may make press releases to local media are an important part of a public relations campaign. They provide the business with publicity, which consists of creating demand by releasing news about a product or business. Publicity differs from advertising in that the business does not pay for publicity. Events that could be reported include expansions that will provide new jobs for the community, a good safety record, product or service improvements, environmental improvements, or programs to inform the public about the use of a product or service. This type of information can aid in creating a stable image of a business as part of the community. Press releases can also be a very cost-effective method of public relations.

Businesses may use advertisements to promote public relations as well as a product or service. They might encourage customers to use what they provide by creating a feeling of goodwill toward the business. Such ads might feature a slogan like "Your Hometown Supplier of Agricultural Goods" to encourage positive feelings toward a business.

Some businesses provide speakers for community groups. Many businesses have employees who have expertise in certain areas. An agribusiness might supply speakers who can provide information to agricultural producers on animal medications, animal nutrition, agricultural chemicals, or agricultural seeds and fertilizers. While they might provide general information that is useful to an audience, these speakers may also publicize the product or service supplied by the business. They therefore serve a dual purpose of public relations and promotions.

More businesses have begun publishing their own periodicals as a part of their public relations program. These periodicals are circulated to all the employees of the business. The periodicals may be newsletters or direct mail flyers that contain information about the business or its employees. The information in such periodicals may include employee promotions, business developments, technical developments, or special problems facing a particular business or industry. Their purpose is to make employees aware of company news and activities in order to enable and encourage them to promote the business to others outside the company by inspiring pride and interest.

To improve public relations, businesses may also provide facilities for community meetings or activities. Many retail stores offer their facilities for bake sales, car washes, and community or national fund-raising activities. Allowing others to use the business' facilities encourages people to support that business in return.

Businesses should always take advantage of opportunities to improve their image in the community and to increase the demand for their product or service. Public relations can help a business prosper because consumers like to do business with companies they like and respect.

Developing a Public Relations Campaign

As with any other type of promotional campaign, a public relations campaign must meet a business's needs. When developing a public relations campaign, a business should consider the identity of the target customer. A business involved in providing agricultural products or services needs to target the customers for them, while a retailer who sells general merchandise must target the community as a whole. A public relations program should be appropriate for the audience that the business wishes to reach.

Decisions need to be made about how the program will operate within budgetary constraints. Businesses with little or no budget for public relations may take advantage of inexpensive opportunities to improve public relations by allowing others to use their facilities for community meetings or fund-raisers. They might also contact the local news media to inform them of important news about the business or its employees. In some cases, members of management and employees of a business may donate their time to community projects.

Decisions also need to be made about who will take responsibility for the campaign. In too many cases, a new employee or a member of management is assigned the duty of public relations. However, having one person be responsible for a campaign along with his or her other work generally does not create an effective program, although it may be unavoidable in a small business. Many larger businesses find that a public relations advisory committee works best. The members of the committee can divide the work and make joint decisions about how funds can and should be used best to create goodwill. The advisory committee can decide what they want the public relations campaign to accomplish and then work toward those goals.

If the management approves, the program can be carried out. The business should monitor the program to see if it is reaching its goals and make changes when needed.

The business should designate someone to be responsible for reporting public relations activities to local news media to get publicity. Often, a business with a well-planned public relations program can take advantage of opportunities to generate goodwill in spite of having little or no public relations budget.

The business and its management should recognize employees who donate their time to the community for helping the community and creating goodwill toward the business. Recognizing individual employees for their involvement in the community is just another way of using public relations as a tool to create goodwill. Employees who like and respect the business they work for will praise it to other members of the community.

Even after putting together a good public relations campaign, a business should remember that the best form of public relations is making sure customers are satisfied. A business that provides a quality product or service that customers rely on is already promoting good public relations. Employees can enhance this aspect of public relations every day by encouraging positive feelings toward the business through friendly and courteous behavior.

Summary

The function of a public relations program is to build goodwill toward a business. Community participation, educational tours, sponsorship of youth awards and activities, media coverage, informational speakers, and the use of business facilities are some activities businesses include in public relations campaigns. However, the best method of public relations for a business is a history of satisfied customers and employees.

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Lesson 1:
The Free Market System

The economy of the United States is based on a free market system, which operates through free competition of individuals and businesses in economic markets. This system stands in contrast to the economic systems in communist and socialist countries in which government control limits free competition and entrepreneurial enterprise.

Characteristics of American Free Enterprise

A free enterprise system is an economic system in which goods and services are produced and traded through a complicated system of prices and markets by private individuals and businesses. The interests of the people are met by the maximum production of whatever they demand by businesses motivated by competition and the reward of profit. The American free enterprise system has four key characteristics.

The first characteristic is private ownership of the land and capital needed for production. Capital is defined as the buildings, machines, and other equipment used to produce goods and services for a profit. In any business venture, the potential reward of profit motivates individuals and business firms to risk their private capital.

The second characteristic of a free enterprise system is organization and coordination of economic activity through the interaction of buyers and sellers or buyers and producers in the different markets. This interaction is guided by the needs of the buyers and the ability of the seller or producer to meet these needs. An important concept to keep in mind when considering this aspect of the free enterprise system is consumer sovereignty. Consumer sovereignty is the freedom of consumers to spend income in ways that will create the most satisfaction for them. Producers are forced to produce what best satisfies the needs of consumers. If they do not, their competitors who do meet those needs will receive the profits. Self-interest thus guides the production of goods and services.

The third characteristic is freedom of the owners of land and capital and the workers that they employ to pursue their own interests in seeking maximum gain from the use of their resources and labor in production. While consumers are free to spend their income in ways they believe will yield the greatest satisfaction, businesses and workers are free to seek the most profit possible from what they produce.

The fourth characteristic of a free enterprise system is minimal government supervision. If competition is present, economic activity will be self-regulated. For example, if one company can produce an item better or more cheaply than its competitors, they will be forced to try to equal its performance or lose profits. Less government involvement is needed because competition in the market meets the needs of the consumers for inexpensive, well-made goods. Freedom of choice, which is a major part of the free enterprise system, introduces the element of competition into the business world. In a free enterprise system, the government does not limit the choices of entrepreneurs; everyone has the right to invest his or her money in any type of business and compete with others in the marketplace.

The free enterprise system is one in which people can spend and invest money as they see fit. Consumers can buy what they want. Business people can freely choose how to handle their resources and will either reap the profits or suffer the losses of their investment choices. This system has helped make the United States an economic giant.

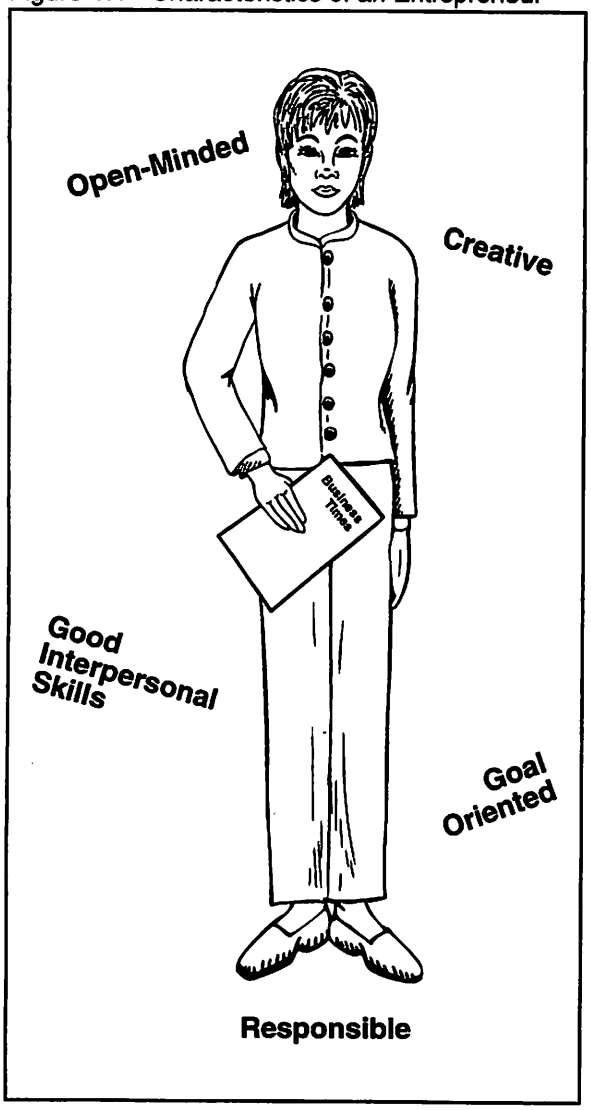
What Is an Entrepreneur?

The free enterprise system encourages entrepreneurship. An entrepreneur is a person who organizes and manages a business, assuming the risk for the reward of profit. Individuals become entrepreneurs by investing their resources and setting up businesses to produce products or offer services that are desired by consumers.

Many people have been entrepreneurs at one time or another. If an individual has ever sold lemonade from a stand in the yard, mowed lawns in the summer, shoveled snow in the winter, or baby-sat, he or she has been an entrepreneur. The risk need not have been great nor the business large, so long as a needed product or service was provided. If a profit was made, then the individual joined the ranks of successful entrepreneurs.

Entrepreneurs seem to have a combination of personal characteristics that are not present in everyone. They are creative in thinking of new ways to solve problems. They usually take responsibility for their own actions and will accept the blame for

Figure 1.1 - Characteristics of an Entrepreneur



failures or problems. Entrepreneurs develop plans and then work to achieve their goals. They are open-minded leaders who are not afraid to ask for advice. Finally, successful entrepreneurs have good interpersonal skills and can get others to follow directions. While not all of these characteristics are essential for success, individuals who do possess them are most likely to succeed as entrepreneurs.

Advantages and Disadvantages

Becoming an entrepreneur has a number of advantages. For example, a person is his or her own boss. Entrepreneurs would rather control their own destiny than work for someone else, even if it means risking losses. Careers in the companies of others are not rewarding.

Another advantage is that entrepreneurs have the chance to profit if their efforts are successful and their businesses prosper. Since they are not working for someone else, they receive the rewards of profit directly, increasing their capital. They can then use the profits as they see fit, perhaps using them to expand.

An entrepreneur can capitalize on creativity. If an individual has an idea for a business, and the idea is a good one, he or she can make money from it. A new business presents an entrepreneur with ample opportunity for creative management.

Being an entrepreneur can create pride and self-satisfaction. Starting a business is something to be proud of in itself. A great deal of self-satisfaction is also involved in running a successful business and offering a product or service that people want.

A final advantage of entrepreneurship is that it allows an individual to be involved in all aspects of a business and perform a variety of tasks. Entrepreneurs are concerned with all the objectives of the business, such as revenue growth, financial strength, market reputation, competitive ability, leadership, and operating efficiency. The entrepreneur is the one responsible for solving the problems that face the business and obtaining the desired results.

Becoming an entrepreneur also has some disadvantages that an individual would not face working for someone else. An entrepreneur takes risks by investing resources to start and maintain the business. The business may fail and the entrepreneur may lose his or her investment. Starting and running a business often requires more time and energy than other jobs. Not everyone is motivated or energetic enough to assume the extra work and responsibility of being the boss.

The Success and Failure of Small Businesses

Before an entrepreneur invests capital in a business, it is important that he or she carefully evaluates the proposed business. An entrepreneur needs to formulate a plan for starting the business; one of the most common reasons for the failure of small businesses is lack of planning. The plan should include an analysis of competitors. Entrepreneurs need to look at who will buy their product and what material and capital will be needed to operate their business. An entrepreneur needs to decide whether to rent or buy property and then choose the right

location for the business, making sure that it has enough floor space and room for expansion. The plan should include an estimate of the number of additional employees who will be needed in the business and the necessary qualifications of these employees. Entrepreneurs also need to be able to estimate the income and expenses the business will have in its first year. Finally, the entrepreneur must plan how to accumulate the capital necessary to start the business.

In spite of planning, a business may not be successful. Consumers may not exhibit the expected demand for a product or service. Competitors may be more efficient, be able to sell a product or service for less, or have better qualified employees working for them.

Summary

The four key characteristics of the free enterprise system are private ownership of land and capital for production, organization of economic activity through the action of buyers and sellers or producers in the different markets, freedom of owners of land and capital and the workers that they employ to seek maximum gain for the use of their resources and labor in production, and minimal government supervision. This economic system encourages individuals to become entrepreneurs, who are people who organize and manage a business, assuming the risk for the potential profit. The entrepreneur has to look for a good opportunity, based on what consumers want, and then develop a plan to start a business that meets the demand.

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Lesson 2:
Business Ownership

When planning to open a business, the entrepreneur must decide not only what type of business it will be, but also what form of business ownership will be used. Each type of ownership has certain advantages and disadvantages, which must be carefully weighed. The entrepreneur must also consider the laws and regulations that will affect the business when planning its opening.

Types of Businesses

In the business world, different types of businesses fulfill different functions. Some businesses produce tangible items. Some businesses perform the various market functions that are involved in the purchase and sale of these goods as they move from producer to consumer. Other businesses provide services rather than goods.

Manufacturers, processors, and producers take raw materials and transform them into marketable products. Businesses in this category would include a mill that produces fabrics from cotton, a manufacturer that produces parts for and assembles agricultural machinery, and an agricultural producer that grows and sells a crop to a processor to be canned or bottled.

Middlemen are individuals or businesses that specialize in performing the various marketing functions involved in the purchase and sale of goods as the goods move from the manufacturer, processor, or producer to consumers. Retailers are middlemen who sell products directly to the ultimate consumers. Most middlemen are retailers. Other middlemen are wholesalers who sell to retailers, other wholesalers, and industrial users. They do not sell significant amounts of merchandise to individual consumers, however. Wholesalers may handle many products or specialize in a limited number of products. One type of agricultural wholesaler is the local buyer who purchases goods directly from the producers and then ships the products to other areas where they are sold to other wholesalers and processors. This type of wholesaler includes local grain elevators and livestock buyers.

Service businesses do not produce or market tangible products; instead they offer services to consumers. Service businesses include insurance companies, repair shops, financial institutions, and many other business that offer services to manufacturers, producers, processors, middlemen, and consumers.

Forms of Business Ownership

The four basic legal forms of business ownership are the sole proprietorship, partnership, corporation, and cooperative. Often the amount of capital available is a deciding factor in choosing the form for a new business.

Sole proprietorship - In a sole proprietorship, the business is owned by one person. The owner is in charge of the business and is responsible for its success or failure.

Partnership - A partnership is a business association of two or more persons who have agreed to combine their financial assets, labor, property, and skills. A partnership contract may outline the general policies of the business, distribution of profit, partners' responsibilities, and term of the contract.

Corporation - A corporation is a separate legal entity owned by other people. Corporation laws, which establish the requirements for the entity that may incorporate, are set forth by each state. Corporations are established by raising capital from the sale of certificates of stock. Persons who invest in a corporation by buying its stock are called shareholders. Shareholders elect the board of directors and can exert a degree of control over policy decisions based on the number of shares they own. They receive their portion of the profits through dividends determined by their percentage of the total stock.

Cooperative - A cooperative is a special type of business. It is a system characterized by the absence of the profit motive. Its primary function is the distribution of goods and services. Cooperatives are owned, and in some cases operated, by members, who are individuals or businesses that join together to market their goods or services; a person involved in a cooperative may not own more than 8 percent of the cooperative. Cooperation with other businesses that offer the same type of product or service helps members to reduce costs. Many rural electric and water companies are cooperatives. They provide a service needed by residents and businesses and reduce utility costs.

A business may change from one form of ownership to another. For example, a hamburger stand in San Bernardino, California, changed from a sole proprietorship to a partnership and then to a corporation to obtain the capital necessary for expansion. The business was originally owned by an individual, but it was doing well, so the owner brought his brother into the business as a partner to help with the operation. They thought of expanding, but they had no real reason to do so--they were already making about $100,000 a year, and neither of them had a family. The business was known for fast and friendly service and for great hamburgers, fries, and milkshakes.

The business would probably not have changed if a man named Ray Kroc, a distributor of milkshake machines, had not noticed that the business had bought more milkshake machines than any other restaurant in the country. His curiosity led him to visit the brothers' business. He was very impressed with the hamburger stand and envisioned hundreds of possible locations where similar hamburger stands could be opened. Kroc enjoyed traveling and convinced the brothers to let him take over a franchising effort to open hamburger stands across the country. They decided to use the same name as that of the original hamburger stand in San Bernardino, which was taken from the brothers' last name--McDonald's.

Advantages and Disadvantages of the Forms of Ownership

Before choosing a particular type of business ownership, an entrepreneur should carefully consider the advantages and disadvantages of each. He or she should choose the form that will be most beneficial.

One of the main advantages of a sole proprietorship is that the individual who owns the business is his or her own boss. Making decisions or forming policies does not require obtaining permission from partners or shareholders. A sole proprietorship is also easy to establish, since it does not involve drawing up partnership agreements, issuing certificates of stock, or finding stockholders. A third advantage is that all the profits from the business go to the owner. In addition, these profits are taxed only once, when they are received by the owner.

A sole proprietorship has disadvantages as well. The sole proprietor is seldom able to invest as much capital as can be secured by a partnership or corporation. In addition, liability is unlimited, which means that the owner is personally responsible for paying all the debts and taxes of the business, even if it has losses. The money may come from selling personal assets or from personal savings. Finally, in a sole proprietorship, the owner has to bear the burden of responsibility for overseeing the operation of the business. If the sole proprietor becomes sick or has personal problems, no one else may be able to run the business.

A partnership has several advantages. One of the biggest advantages of forming a partnership is that someone is available to share the responsibilities and problems of managing a business. Also, financial institutions are more likely to lend money to a partnership because two or more people are responsible for the debts of the business. Profits are shared only by the partners, and they are taxed only once.

A partnership also has disadvantages. Unless a limited partnership has been established, in which one of the partners assumes complete financial responsibility for losses, all parties in the partnership share equally the burden of loss and debt. Since partnerships have unlimited liability, if one partner goes bankrupt, the other partners are still responsible for the debt. Another disadvantage is that each partner can enter into a contract without the permission of the other partner or partners, yet all the partners are equally responsible for fulfilling the contract.

The chief advantage of corporate ownership is that stockholders have limited liability. The debts of the corporation are the responsibility of the corporation and not the individual stockholders. The most a shareholder can lose is the amount paid for the certificates of stock. A second advantage is that if the corporation is doing well, getting loans from financial institutions is easier than for a sole proprietorship or partnership. A corporation can also sell additional shares of stock to raise funds.

Corporate ownership has disadvantages, too. A corporate certificate must first be issued by the state, and the certificate may be expensive. All decisions about the corporation must be made and approved by the shareholders or directors, and the larger the number of people involved the greater the difficulty of decision making. Another disadvantage is that profits on corporations are taxed twice. The corporation itself is first taxed, and then the income that has already been taxed is distributed to the

shareholders and taxed again as personal income.

The advantage of forming a cooperative is that individual businesses working together can reduce costs. The one disadvantage of this form of ownership is that a cooperative is not set up to earn a profit. However, businesses that are members of the cooperative can reduce their costs and in most cases increase their own profits.

Business Regulations

To start and maintain a business, specific laws and regulations must be considered and followed. Even though knowing all the laws that affect a business's operation is not necessary, it is important to know the laws that affect establishing a business. Ignorance of the laws is not accepted as an excuse for breaking them. In many cases, an entrepreneur may want to contact a lawyer who specializes in business law.

Operating a business requires entering into contracts. A contract is a legal agreement that creates an obligation binding the parties using the contract. Contracts are generally established to clarify an agreement. For example, contracts may be made to specify the quality of goods or services that the parties entering the contract have agreed upon. They may indicate the color, size, quantity, or price of the goods or services. The contract also serves as a reminder of those terms. In a legal contract, action must be taken to fulfill the contract. If one party does not act, the other party can initiate court action to collect payment for non-performance.

An enforceable contract has five elements: capacity, consent, genuine assent, legality, and consideration. Capacity refers to competency of the people entering into the contract. They must be capable of understanding the agreement. Consent is the offer and the acceptance of the offer. Genuine assent refers to the mutual understanding of the terms of the agreement. The action called for in the contract must be lawful; contracts cannot be written for illegal activities. Finally, consideration is what is exchanged between the parties to a contract. It may be money, property, or the promise to do something.

Contracts may be either oral or written. Certain contracts, in order to be enforceable, must be written and signed. Contracts that cannot be performed within a year after they are made, those involving the sale or transfer of real estate, and those involving the sale of goods above $500 in value must be written. Oral contracts are as legally binding as written contracts in some cases. For simple transactions, such as buying groceries or magazines, or for other transactions in which small amounts of money are immediately exchanged for goods, an oral contract is generally the best way of doing business. When buying or selling a car, real estate, supplies, equipment, or other items that require a detailed agreement or a large amount of money, an oral contract should not be used because it can be misunderstood or remembered incorrectly. It is also hard to prove that an oral contract was not fulfilled if legal action becomes necessary. When operating a business, the best policy is to get any agreement in writing.

In some cases, a license or permit must be secured before an entrepreneur may start a business. These licenses or permits may be required by federal, state, or local governments. Barbers, beauticians, private detectives, and employment agencies are just a few of the businesses required to have licenses. To get a permit or license, special training or testing may be required; periodic inspections of the business may also be made in some cases. An entrepreneur should get legal advice on what permits or licenses are required before starting a business.

Regulations concerning zoning and building codes will have an impact on any new business. Zoning and building codes are rules and regulations passed and enforced by federal, state, or local government agencies to protect citizens. Building codes include standards for safety, electricity, and plumbing. They also may include standards for the type and design of the business structure, depending on where the building is located. Zoning laws designate the purpose for which the buildings in an area can be used. Certain areas in a community may allow only residential buildings, while other areas of the community may be set aside for businesses.

Health and safety laws establish standards for working conditions to protect workers. One example would be child labor laws that set the minimum age for workers. They also include laws that establish environmental safety standards to protect the health of employees. For example, some businesses are affected by regulations that set guidelines for the handling of toxic chemicals or for the installation of specialized ventilation systems to remove dangerous fumes.

Laws have also been passed to prevent discrimination in hiring. These laws have been established by state and federal governments to prevent discrimination in the hiring of employees due to gender, age, religion, or national or ethnic origin.

The federal government has set a legal minimum wage for jobs that applies to most businesses. Under certain conditions, businesses may pay less than the established minimum wage. For example, small farms and certain businesses that earn less $500,000 in annual gross income do not have to pay their employees minimum wage. Entrepreneurs should check with the Wage and Hour Division of the U.S. Department of Labor to find out whether their businesses are exempt from the minimum wage requirements.

Summary

Businesses may fall into one of three categories depending on the type of activities that they carry out. A business may be involved in making a tangible product, marketing a product to others, or providing a service. In addition, a business may be organized under one of four forms of ownership (sole proprietorship, partnership, corporation, and cooperative), each of which has advantages and disadvantages. When starting a new business, an entrepreneur should carefully consider which form of ownership will most benefit that business. He or she must also think about the many laws and regulations that will affect the operation of the business.

Credits

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Lesson 3:
Evaluating Business Opportunities

Before starting a business, an individual must carefully evaluate business opportunities to determine if his or her idea is a good one. The evaluation of business opportunities can be accomplished by developing a business plan. A business plan can help a prospective entrepreneur decide whether and how to proceed in starting a business.

Recognizing Business Opportunities

Opportunities for businesses exist whenever people want a good or service and are willing to pay for it. The prospective entrepreneur should look at the businesses around him or her and the products or services that they offer. He or she might notice changes or trends that will create new opportunities or change existing ones. For example, new opportunities exist where new products or services are being introduced, often due to the development of technology. The growing use of cellular phones, personal computers, and CD players has created opportunities for new types of businesses in many communities. Other trends, such as customer demand for quick oil changes, the convenience of paying for gas at the pump, and pizza delivery to the home, have created opportunities for businesses that are similar to existing business but that meet these demands. An entrepreneur might also look for good business ideas that have been developed by others but could be better executed by his or her own business. Another way to discover a business opportunity is to search for needs and wants that are not being met by existing businesses. Finally, an entrepreneur may look for new ways to meet the needs and wants of consumers.

Business Plans

A business plan is a detailed proposal that describes all aspects of a new business, including its operations, marketing, and finances, for the use of the entrepreneur as well as investors and financial institutions.

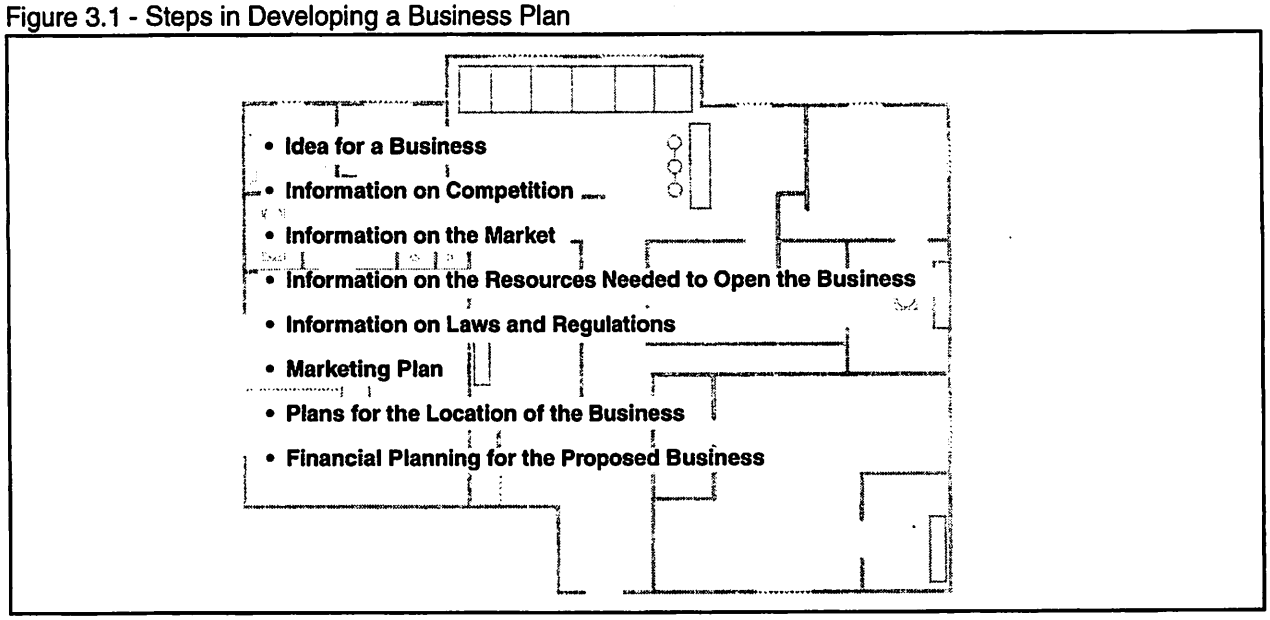
- A business plan is valuable when an entrepreneur is considering the opening of a business. Developing a business plan helps an entrepreneur evaluate his or her ideas for a business to determine if they take advantage of the opportunities available.
- A plan can also help the entrepreneur in determining whether the market can support a particular type of business.
- A business plan can be used to help an individual obtain financing for a proposed business.
- In addition, it serves as a guide for the operation of a business once it is started.

Developing a Business Plan

Putting together a business plan involves several steps, which are summarized on the next page in Figure 3.1. The first step in developing a business plan is coming up with an idea for a business based on an available opportunity. The idea is the foundation for the plan. Completing the business plan requires evaluating the idea for a business to see if it makes the best use of the opportunity. The business is used not only to evaluate the idea but also to expand or change it by including all the information needed to make a business successful.

To use the plan in evaluating the idea for a business, the writer of the plan needs to include information on possible competitors. The potential entrepreneur will have to compete with other businesses for customers or markets, and he or she should explain planned improvements on their operations and products or services. Evaluation of the competition involves answering several questions. Can the proposed business offer a better price to its customers, perhaps by operating more cheaply or efficiently? Can the proposed business offer a better quality product or service? Can the proposed business market a product or service that the customers will believe is a better product or service than that offered by competitors? The business plan should include a list of competitors and information on their prices, the quality of their products or services, and their marketing methods. The entrepreneur can then develop a plan for competitive pricing, a better quality products or services, and a better marketing plan than the competition. A new business may be unable to offer the same product or service competitively, and the idea for the business may need to be adjusted to improve the chances of achieving success.

Figure 3.1 - Steps in Developing a Business Plan



The business plan should also examine the market for the product or service. The market is simply the potential customers of the proposed business. What are the ages of potential customers? What sex are the customers? What is their income level? What location would be best for the customers? What are their interests? Will price, quality, service, or selection attract customers to the product or service of the proposed business? Knowing who potential customers are and where they are located helps when planning sales promotions, the location of the business, and management strategies. It also helps the entrepreneur determine if there will be enough demand for the product or service. This information may suggest whether the original business idea needs to be adjusted, expanded, or totally changed to meet the demands of the customers.

The business plan should list all of the resources, including capital, that will be needed to start and operate the proposed business. Resources are those things needed to conduct business, such as raw materials or merchandise, technical equipment or expertise needed to produce a product or offer a service, fixtures, office and bookkeeping supplies, sales and promotional supplies, and the capital to purchase resources. Resources also include the employees and managers (besides the owner) who will be needed to operate the business. Flexibility can be increased by hiring part-time employees with flexible hourly schedules when opening the business. The business plan should include everything that will be needed to get started and maintain the proposed business and an estimate of how much capital will be needed to purchase sufficient resources.

The business plan should include information on laws and regulations that will affect business operations. Information will have to be collected on the regulations that must be followed. What type of zoning and building codes affect the proposed business? What health and safety standards, discrimination laws, advertising laws, and employee pension regulations will affect it? What legal contracts must be entered into before and after the proposed business has been started? What licenses or permits will be necessary for the proposed business? The estimated cost of following the rules and regulations should also be included in a business plan.

The business plan should include a marketing plan. A marketing plan is simply a plan or program for achieving the forecasted sales for the proposed business. The marketing plan should answer certain questions. Will it be necessary to advertise? Will sales be seasonal or constant throughout the year? What is the estimated cost of the marketing plan for the proposed business? A marketing plan can help the business achieve the sales necessary to be successful. It is important to know how and when to advertise. Too much advertising or advertising that is ineffective is an unnecessary expense; not enough advertising may mean lost sales. A good marketing plan is one that can be adjusted to suit the proposed business. If the business is the only one of its type in the

community, enough advertising to inform customers that the business is open may be adequate. However, businesses in highly competitive markets may need constant advertising to inform customers that their products are of better quality or are less expensive than those of competitors.

The location of the business should also be included in the business plan. Where will the business be located? How large should the building be? Will the building or space be rented or purchased? Is there room for expansion at the proposed location? Other parts of the business plan need to be considered when choosing a location. The location of competitors, the location of potential customers, and zoning and building codes should be taken into consideration. The location must fit the type of business being proposed. Most importantly, the business should be conveniently placed and easily accessible to potential customers.

The last component of a business plan is financial projections for the proposed business, which should include estimated sales for the first year of business. Data gathered from other parts of the plan will help the entrepreneur estimate income and expenses in the first year of operation. Information about the competition, resources, regulatory costs, including permits and licenses, advertising costs, costs associated with location, and costs of wages and benefits can be used to come up with reasonable estimates to determine whether or not the business idea can be implemented to take advantage of an opportunity. An income statement, a balance sheet recording assets and liabilities, and a cash flow statement can be developed to determine if the market can support the business being proposed. For a small business loan, a lending institution may want to see statements for the personal finances of the entrepreneur starting the business.

Short- and Long-term Business Goals

If the business plan shows that a good opportunity exists, short- and long-term goals can then be established for the business. Every business should have both short- and long-term goals. The ultimate goal of every business is, of course, to make a profit. It is a good idea to express the goals in a statement that explains why the business exists. A service business may have a short-term goal of servicing customers within a ten-mile radius while earning a profit and a long-term goal of expanding the business to service customers over a twenty five-mile radius while increasing profits. Goals should be reviewed periodically and adjusted to meet changing economic and social conditions.

Once goals have been established, an entrepreneur should define a set of objectives that will help him or her reach those goals. Objectives should be stated in measurable terms so that they may be used to evaluate performance. For example, an objective for the goal of making a profit may be to achieve a certain level of sales. The objective might state that $80,000 in sales is needed in the first year to make a profit. If the objective is not achieved, operations can be evaluated to determine ways to increase sales. If the sales objective is met but the profit goal is not, other objectives, such as expense objectives, should be evaluated to determine whether changes must be made. If the sales objective is achieved, a higher sales objective can be established and work toward a long-term goal begins. The evaluation of objectives helps the entrepreneur make changes that will allow him or her to progress towards goals.

Goals are important because they can be used to help set operating policies. Every policy should contribute to achieving goals and objectives. For instance, before advertising policies are implemented, their effect on sales should be considered, as should how the advertising expense will affect expense objectives, and whether profit goals may be reached using the proposed policies. A realistic set of goals and objectives is a valuable management tool in establishing and maintaining a business.

Summary

Opportunities for starting a business exist when people want goods or services and are willing to pay for them. Entrepreneurs recognize business opportunities and develop ideas for businesses that take advantage of them. A business plan is a valuable tool for evaluating whether an idea for a business is a good one. The plan can also be used to obtain financing and to help guide the business once it is started. Goals and objectives are important because business owners and managers can use them to set policies for operations.

Credits

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Lesson 4:
Preparing an Income Statement

Income statements are financial statements that may be very important to the success of a business. They help entrepreneurs to make decisions about the business and to assess the effectiveness of those decisions.

Income Statements

An income statement is a summary of a business's income and expenses for a specific period. The income statement helps a business determine if it has made a profit or sustained a loss as of a specific date. It also measures the ability of a business to repay loans and debts. Finally, a business can use an income statement to secure loans for financing or refinancing a business. An income statement may be referred to as a profit-and-loss statement.

Components of an Income Statement

One component of an income statement is the amount of revenue, or income, received by the business. Cash sales of a product or service generate revenue. The money earned from selling assets and from interest income is also included on the income statement as revenue.

The income statement includes the expenses of a business. Cash expenses are the operating expenses involved in producing a product or service as well as the interest paid on loans taken out by the business. The income statement also has a section for noncash expenses like depreciation in which cash is not actually spent by the business. Depreciation is the reduction in potential usefulness of a fixed asset like equipment, vehicles, or buildings due to wear and tear or the passage of time. It is used in accounting to distribute the cost of a fixed asset over the estimated life of the asset.

One of the most commonly used methods of figuring depreciation is straight-line depreciation. In straight-line depreciation, the purchase price of the asset is divided by the estimated number of years of usefulness. The result is the amount of depreciation expense for one year. It is subtracted from the value of the asset each year until it equals zero.

The final component of an income statement is the net income or net loss for the business. Information on revenue and cash and noncash expenses is used to calculate net income or net loss, which is the increase or decrease in capital resulting from profit-making activities. A business pays taxes based on net income.

Preparing an Income Statement

To prepare an income statement, a business owner or manager must gather records of the types and amounts of revenue the business has received. The first steps in preparing an income statement are listing the cash revenues and then adding them to calculate the gross revenue.

Some businesses may also figure the cost of goods sold under the revenue section of the income statement. The business makes sales over the statement period; these sales are recorded as income in its financial records at the selling value of the items. The cost to the business of producing and acquiring these items is needed to estimate the cost of goods sold. The business takes the beginning inventory for the period and adds any additional expenses associated with increasing inventory to get the total cost of goods available for sale. The ending inventory for the statement period is then subtracted from this total to calculate the cost of goods sold. This amount is subtracted from sales to find the gross revenue from sales.

The next steps involve expenses. The business must gather information on cash expenses, list them on the statement, and add the expenses to find the total cash expenses.

Once gross revenue and total cash expenses have been calculated, net cash income is figured. Net cash income is equal to gross revenue minus total cash expenses.

Noncash expenses like depreciation, in which cash is not actually spent by the business, are then noted on the income statement. The amount of depreciation for the period is entered under noncash expenses on the income statement. Depreciation is subtracted from net cash income to determine the net income from operations for the business.

The final step in completing an income statement is figuring net income by adding or subtracting capital gains or capital losses from net income on operations. Capital assets are anything of value owned by a business that have a useful life of more than one year. A business experiences a capital

Figure 4.1 - Income Statement

INCOME STATEMENT

Name: Rowton Agricultural Supply

For the period ending: Dec. 31, 19--

REVENUE			
Sales			$95,000.00
COST OF GOODS SOLD:			
Beginning inventory	$10,000		
Purchases	40,000		
Cost of good available for sale	$50,000	$50,000	
Ending inventory		- 10,000	
Total cost of goods sold		40,000	
			(40,000.00)
		Gross Revenue	55,000.00
EXPENSES			
Rent			$ 2,640.00
Utilities			1,080.00
Supplies			29,500.00
		Total Cash Expenses	$33,220.00
		Net Cash Income	$21,780.00
NONCASH EXPENSES			
Depreciation			$2,350.00
		Net Income from Operations	$19,430.00
		Gain or Loss on Capital Assets	($208.00)
		Net Income	$19,222.00

*Parentheses indicate a negative figure.

gain when the income from selling a capital asset is more than its original cost less depreciation. A capital loss occurs when the income from selling a capital asset is less than its original cost less depreciation.

Figure 4.1 is an illustration of a sample income statement. The statement is for a business called Rowton Agricultural Supply. It shows that net income for the business was $28,922.00. The

owner of the business plans to use this information to obtain a loan for expansion.

Income statements may vary in format from the sample included in this lesson. On some statements, the interest expense generated by the business's financing activities and the tax expense imposed on the business are recorded separately from the expenses involved in operating the business. The preliminary total is referred to as the operating profit for the business, or earnings before interest and taxes (EBIT). These expenses must be subtracted to find the net income for the business.

Summary

An income statement is a summary of a business's income and expenses for a specific period. The information on income and expenses included on the income statement is used to calculate net income.

Credits

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Lesson 5:
Preparing a Balance Sheet

Keeping complete and accurate financial records is important for every business. These records allow the owner or manager to analyze the performance of the business by preparing financial statements. These statements also provide input used in making management decisions and assessing the effectiveness of those decisions. A balance sheet is one type of financial statement.

Balance Sheets

A balance sheet is a financial statement showing a business's assets, liabilities, and net worth as of a specific date. The balance sheet provides a statement of the nature and type of resources available to a business. It also shows what the business owes its creditors. A completed balance sheet reveals the net worth of the business.

Components of a Balance Sheet

As indicated above, a balance sheet contains information on assets, liabilities, and the net worth of a business. Assets are further broken down into two types of assets--current and fixed. Liabilities are categorized as current and long-term liabilities. They are listed on a balance sheet in a two-column format, in which the totals of the columns must balance, or equal, each other.

Assets are all of the resources and properties owned by a business. They may be tangible or intangible. A tangible asset is any resource of a business that can be touched, such as supplies, machinery, and buildings. In contrast, an intangible asset has no physical presence, but does have value. For example, a franchise to operate a business under a certain name is an intangible asset; it cannot be touched, but it can be bought and sold and increases or decreases in value.

Current assets are assets that can or will be used or sold within one year. They include savings accounts, checking accounts, accounts receivable (money owed to a business by others), short-term bonds, supplies that will be used within a year, equipment that will be used within a year and then sold or disposed of, and inventory that will be sold and converted into cash within a year. Fixed assets, also called noncurrent assets, are assets that will not be used or sold and converted into cash within one year. These noncurrent assets consist of such things as certificates of deposit and bonds that take over a year to mature, supplies that will not be used in one year, inventory that will not be sold and converted into cash within one year, vehicles, equipment, buildings, land, and breeding livestock that will not be sold within a year.

Liabilities are all debts owed by a business. They may be money, goods, or services that a business owes to a creditor. Current liabilities are liabilities that are payable within one year. They include interest and principle payments due within one year on loans, interest and principle payments on charge accounts, accounts payable (money that a business owes to others), and payments on insurance. Long-term liabilities, or noncurrent liabilities, are liabilities that are not payable within one year. Examples of these noncurrent liabilities are interest and principle payments for loans not due within one year.

A single asset or liability can be partially current and partially noncurrent. For example, a business might take out a loan to renovate a building and repay the loan over six years. If the loan is for $25,000, with $5,000 in interest and principle due in one year, the business's current liability is $5,000, and the remaining $20,000 is a noncurrent liability.

Net worth, or owner's equity, is the net ownership a sole proprietor, partnership, corporation, or cooperative has in a business. In other words, net worth is equal to the amount of investment in a business by its owners and any profits that have remained within the business. For a corporation, net worth includes money generated by the purchase of stock in the company and the earnings retained by the business. The difference between the business's assets and liabilities equals its net worth.

Preparing a Balance Sheet

A business must have good financial records in order to complete a balance sheet, since the first step in preparing a balance sheet is gathering information. All the business's assets and liabilities should be classified into current and fixed (assets) and current and long-term (liabilities).

Examine the illustration of a balance sheet in Figure 5.1. Notice that the list of current and fixed assets and their values go in the first column of the balance sheet. The total value of each type of asset is calculated. The two figures are then added together to determine the total assets of the business.

The same process is followed for liabilities. A list of current liabilities and long-term liabilities is written down in the second column, and the total values of current and long-term liabilities are calculated. The two figures are added together to find the total liabilities of the business.

Net worth is figured by subtracting total liabilities from total assets. If the business has more liabilities than assets, the amount will be negative. Total liabilities and net worth added together should equal total assets.

Figure 5.1 is an illustration of a balance sheet for Martinez Farms. It was completed to obtain financing to increase the size of the business. The balance sheet shows that total assets for the cow-calf operation equal $136,950 and total liabilities are $96,730, which gives the business a net worth of $40,220.

Solvency and Liquidity

A balance sheet shows a business's financial standing at the time it is completed. Data from the balance sheet can be used to perform calculations measuring a business's financial performance, particularly the solvency and liquidity of the business. These calculations are important because they allow the business to discover trends in its operations and to compare its operations to other businesses in the same industry. They are also used by banks when evaluating a business for a loan.

Solvency refers to the capital structure of the business. A business is solvent if the sale of all assets would generate sufficient cash to pay off all liabilities. A simple measure of solvency is whether total assets exceed total liabilities, or net worth is greater than zero. If assets are less than liabilities, the firm is not solvent, because it does not have the necessary assets to cover current and noncurrent liabilities. If assets are equal to liabilities, the business's solvency is questionable, because no assets would be available to meet unexpected expenses along with current and noncurrent liabilities.

The net worth/assets ratio is one measure of solvency. A ratio shows the relationship between two numbers when one is divided by the other. The net worth/assets ratio is a measure of net worth as a percent of the total assets of the business. It is calculated as follows:

$$\textit{Net worth/assets ratio} = \frac{\textit{Net worth}}{\textit{Assets}}$$

A second method of evaluating solvency is the net worth/total debt ratio. In this ratio, solvency is determined by looking at the total liabilities and net worth of the business. This ratio provides a measure of net worth as a percent of the total debt of the business.

$$\textit{Net worth/total debt} = \frac{\textit{Net worth}}{\textit{Total debt}}$$

The net worth/total debt ratio provides an indication of the financial health of a business. This ratio may be useful to assess how well the business may survive a crisis. A lower ratio means that the business may be on rather shaky financial ground, whereas a higher ratio indicates the business is in a relatively stable position. As a general rule, the higher the ratio, the better it is for the business. Bankers will evaluate this and other solvency ratios to determine the risk of lending money to a business.

Liquidity involves a business's capacity to generate cash to meet anticipated and unanticipated cash demands as they occur, without disruption of operations or a loss of value. A business is liquid if it can meet immediate financial obligations without selling the assets needed in the daily operation of the business. If a business is liquid, current assets will exceed current liabilities.

One measure used to determine liquidity is called the current ratio, or working capital ratio. Current assets are divided by current liabilities to give a ratio of current assets per dollar of current liabilities.

$$\textit{Current ratio} = \frac{\textit{Current assets}}{\textit{Current liabilities}}$$

Current assets include cash, accounts receivable (less any bad debts), and inventory. Current liabilities include accounts payable, salaries payable, and interest payable. If a company had current assets of $48,000 and current liabilities of $24,000, then the current ratio would be 2 ($48,000 ÷ $24,000). For every dollar of current liabilities, the business has $2 in current assets. A 2:1 ratio would

Figure 5.1 - Balance Sheet

BALANCE SHEET

Name: Martinez Farms

Date: December 31, 19--

Current Assets		Current Liabilities	
Checking account	$ 1,200.00	Accounts payable	$ 320.00
Savings account	2,500.00	Interest (truck)	560.00
Accounts receivable	4,200.00	Interest (trailer)	150.00
Calves	8,500.00	Interest (cows)	550.00
		Interest (bull)	150.00
		Interest (land)	6,000.00
Total Current Assets	$16,400.00	Total Current Liabilities	$7,730.00
Fixed Assets		**Long-Term Liabilities**	
Cows	$ 27,000.00	Truck loan	$ 5,500.00
Bull	2,400.00	Trailer loan	1,500.00
Stock trailer	3,000.00	Cow loan	15,000.00
Cattle feeder	650.00	Bull loan	2,000.00
Truck	7,500.00	Land Loan	65,000.00
Land	80,000.00		
Total Fixed Assets	$120,550.00	Total Long-Term Liabilities	$89,000.00
		Total Liabilities	$96,730.00
		Net Worth	$40,220.00
Total Assets	$136,950.00	Total Liabilities & Net Worth	$136,950.00

be considered strong in many businesses, but the ratio that is desirable varies with the type of business.

Another ratio used to measure liquidity, called the quick ratio or "acid test ratio," is similar to the current ratio but does not include the value of inventory. The formula is as follows:

$$\textit{Quick ratio} = \frac{\textit{Current monetary assets}}{\textit{Current liabilities}}$$

Many businesses consider inventory to be a buffer against an unexpected loss. This formula takes into account that inventories are often not very liquid and may not be converted to cash quickly. Ratios between .5 and 1 are generally considered acceptable.

Summary

A balance sheet is a statement of the assets, liabilities, and net worth (or owner's equity) of a business at a specific point in time. In a properly completed balance sheet, assets and liabilities are classified as current assets, fixed assets, current liabilities, and long-term liabilities. The total amounts of each are then used to figure total assets and liabilities and net worth. A completed balance sheet can be used as in aid in measuring the solvency and liquidity of a business.

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Lesson 6:
Preparing a Cash Flow Statement

The importance of keeping complete and accurate business records cannot be stressed too often. Complete records allow an entrepreneur to make decisions and assess the effectiveness of his or her policies. For example, records on cash flow let an entrepreneur know when money will be available and when it will be needed to make business payments, which may affect decisions that depend upon the amount of money available to a business.

Projecting Cash Flow

Cash flow is the way money flows into and out of a business. A cash flow statement and a statement of cash flows show cash inflows and outflows for a business. The sum of the net cash flows on both of these statements equals the change in cash during an operating period. This amount equals the total amount of cash that is available or needed at the end of the period. It will be carried over to the next operating period.

An entrepreneur projects cash flow for several reasons. Cash flow shows the liquidity of a business, letting the owner know if the business can meet its financial obligations by revealing whether cash will be available when needed to pay business expenses. It can be used to help the business establish and maintain a line of credit. Financial institutions use cash flow statements to determine if a business will be able to pay back loans. It can also be used by entrepreneurs to evaluate past financial practices and inform current decisions. An entrepreneur can look at a summary of past cash flows to help determine when cash will be available to the business for such things as purchasing capital assets and expanding the business.

Preparing Cash Flow Statements

A cash flow statement shows payments and receipts for a business. The cash flow statement can serve as a summary of past cash flows for a business. A cash flow statement can also summarize the projected business payments and receipts for a specific period of time. It gives the entrepreneur information on his or her cash flow projections by giving an estimate of cash inflows and outflows for his or her business. A lending institution looks at a projected cash flow statement to determine whether a business will have the ability to make loan payments over a period of time. The person preparing a cash flow statement should first break down transactions into income (receipts) or expenses (payments), then into quarterly values. When entering figures into a statement, add receipts to the beginning cash balance to find total cash available. Then subtract expenses to find the cash position before savings and borrowing. Add any money borrowed to find the ending cash balance, and repeat this procedure for each quarter and for the "Total" column. If the statement is completed correctly, the ending cash balance in the "Total" column should equal the ending cash balance for the fourth quarter.

Figure 6.1 shows a sample cash flow statement for the past year for a business called AgriProduction, Inc. The statement shows that the business will likely need to use savings or borrow money in the first and second quarters to meet cash requirements in the future. With this statement, however, the owners can show a financial institution that they will be able to pay back a short-term loan as cash becomes available in the last two quarters. The statement also suggests that the owners will most likely have cash available in the third and fourth quarters to purchase capital assets or to expand operations.

All the information in the statement of cash flows is also found in the cash flow statement. The statement of cash flows illustrates changes in cash or cash equivalents for a period. It takes the information from the cash flow statement and summarizes it in a more useable form, showing in what areas cash inflows and outflows occur in the business. This statement allows entrepreneurs to be more businesslike in the financial analysis of their operations. It also improves the quality of information used in management and credit decisions. The statement of cash flows can be used by the entrepreneur or lending institutions to determine where cash was generated and how it was used by the business.

The transactions used in the cash flow statement and the statement of cash flows are the same, but they are summarized differently. The figures used in the statement of cash flows are the total figures for the year; they are not broken down by quarters. When preparing a statement of cash flows, divide the transactions into operating activities, investing activities, and financing activities. Operating income and expenses come from the production and sale of

Figure 6.1 - Cash Flow Statement

CASH FLOW STATEMENT

Name AgriProduction, Inc. For the period Jan. - Dec. 19--

	TOTAL	QUARTER 1 (JAN-MAR)	QUARTER 2 (APR-JUNE)	QUARTER 3 (JULY-SEPT)	QUARTER 4 (OCT-DEC)
BEGINNING CASH BALANCE	$1,155	$1,155	($13,205)	($21,971)	$32,309
Receipts					
Crop	$99,500			$78,000	$21,500
Market livestock	12,096	$11,340	$756		
Breeding stock	19,600				19,600
TOTAL CASH AVAILABLE	$132,351	$12,495	($12,449)	$56,029	$73,059
Expenses					
Feed	$18,883	$3,220	$1,575	$6,475	$7,613
Rent	16,000	4,000	4,000	4,000	4,000
Utilities	631	171	137	155	168
Taxes	3,810		3,810		
Machinery	21,000		21,000		
Principal payments	32,200	9,100		10,500	12,600
Interest expense	15,544	9,209		2,940	3,395
TOTAL CASH REQUIRED	$108,068	($25,700)	($30,522)	$24,070	$27,776
CASH POSITION BEFORE SAVINGS & BORROWING	$24,283	($13,205)	($42,971)	$31,959	$45,283
Money borrowed	$21,000		$21,000		
ENDING CASH BALANCE	$45,283	($13,205)	($21,971)	$31,959	$45,283

*Parentheses indicate a negative figure.

goods and services and the use of consumable supplies and labor in production. Cash flow from operations includes payments from customers, payments to suppliers, and other routine business expenses, including interest payments. Investing activities create cash flow when capital assets, such as land, buildings, and equipment, are purchased or sold. Financing activities involve taking out new loans or making principal payments on loans and payments on stock dividends.

Enter the total amounts for these activities for the period on the statement. Total the cash inflows and outflows for each type of activity to find the net increase or decrease in cash for the period. Add the beginning cash balance to find the amount of cash available at the end of the year.

Figure 6.2 illustrates a statement of cash flows for AgriProduction, Inc. It shows that cash inflow for the year came from the income on operations, the sale of breeding stock, and a new loan. Cash outflow was due to normal operating expenses, the purchase of capitstillidlal assets, and payments on the principal of a loan.

Figure 6.2 - Statement of Cash Flows

STATEMENT OF CASH FLOWS Name AgriProduction, Inc. For the period ending December 31, 19--	
CASH FLOWS--OPERATING ACTIVITIES	
Cash received from operations	$ 111,596
Cash paid for feed	(18,883)
Cash paid for rent	(16,000)
Cash paid for utilities	(631)
Cash paid for taxes	(3,810)
Interest expense	(15,544)
NET CASH FLOW FROM OPERATIONS	$ 56,728
CASH FLOWS--INVESTING ACTIVITIES	
Sale of capital assets (breeding stock)	$ 19,600
Purchase of capital assets (machinery)	(21,000)
NET CASH FLOW FROM INVESTMENTS	$ (1,400)
CASH FLOWS--FINANCING ACTIVITIES	
Principal payments	$ (32,200)
New loans	21,000
NET CASH FROM FINANCING ACTIVITIES	$ (11,200)
NET INCREASE/DECREASE IN CASH AND CASH EQUIVALENTS	$ 44,128
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR	$ 1,155
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR	$ 45,283

*Parentheses indicate negative figures or cash outflows.

Summary

Cash flow is the way money flows into and out of a business. A cash flow statement summarizes the projected payments and receipts for a business. A statement of cash flows for a business period arranges this information into the categories of operating, investing, and financing activities and provides a more detailed picture of where cash inflows and outflows occur. Cash flow statements can be used to measure liquidity, help a business establish and maintain a line of credit, and evaluate past financial practices to inform current decisions.

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Lesson 7:
Obtaining Business Financing

Starting and running a business can be expensive. A business might have to obtain financing to begin operations, to purchase needed inventory or equipment, or to expand.

Understanding Business Financing

Borrowing money to start or expand a business involves getting a loan. While money may be obtained from another person, it usually comes from some sort of institution, like a bank. The business will have to pay the money back at a later time, along with interest, the charge for borrowing the money. It is important to remember that interest is an expense and does not add to the worth of a business. Good financial management includes borrowing the appropriate amount needed to start or keep a business operating as well as shopping around to get the lowest interest rate possible. The amount borrowed should cover what the business plans to spend for inventory, supplies, and equipment and pay any other expenses the business will generate until money begins to flow in from its operations. A good business plan will include the forecasted cash flow for the first two months and estimated expenses; the entrepreneur can decide how much to borrow using these amounts.

The amount of money needed to start a business depends on the type of business. Some service businesses require only a minimal amount of equipment to begin operations; additional equipment may be added as the business grows. For example, an entrepreneur starting a cleaning business may need only cleaning equipment and a reliable truck or van. More equipment and vehicles may be purchased as the business expands.

Young entrepreneurs who want to start businesses that require large inventories or large capital investments may have trouble finding institutions or individuals willing to loan them money. However, they should not give up on the idea of starting a business. Successful entrepreneurs think big but may start small. For example, an entrepreneur starting a repair business could save and invest the money earned from the small repair business and expand the business or open a hardware store. Once a business has been started and financial institutions can verify a history of good business management, they will be more willing to loan money to the business.

Even if financing is not required to start a business, establishing a line of credit is important; a good credit history will make it possible to obtain financing if it is needed. Most businesses require the owner to buy an inventory to be sold or the equipment and supplies that are used to generate income. The inventory, equipment, and supplies must be bought, and in most cases paid for, before they are sold or used. If the business is unable to purchase the items needed, the business will not survive. Sometimes businesses go through periods of cash flow problems when more money is paid out in expenses than is received as income. A business may then find it necessary to borrow money for short periods of time until more money can be earned. Building a good credit history makes it easier to obtain financing in both of these situations. Using credit wisely and only when needed means that a business has to pay less interest, which creates fewer expenses and more profit. Establishing a good personal credit history and maintaining a good business credit history will not only make it easier to borrow money but will also make it possible to obtain the lowest possible interest rate, because more institutions will be willing to loan the business or individual money.

Sources of Financing

Many of the same financial institutions that lend to individuals also lend money to businesses. The amount, length, purpose, repayment method, and type of collateral necessary to secure the loan will vary with each source. The best place to secure money for a business is the financial institution the entrepreneur has used in the past. Establishing a good personal credit history with a financial institution helps in securing a business loan from the same institution. Some sources of credit that a business may consider are listed below:

Commercial banks - Commercial banks will generally offer short- and long-term loans that require a single payment or periodic payments of interest and principal. Commercial banks will generally loan money for real estate, inventory, or capital assets.

Savings and loans - Savings and loan institutions are primarily set up for long-term use for real estate.

They mostly lend money for housing but may also loan money to purchase commercial real estate.

Insurance companies - Some insurance companies will allow individuals to borrow against the cash surrender value of their life insurance policy to make purchases. Most policies do not have a significant loan value until they are at least eight to ten years old. Insurance companies make short- and long-term loans.

Small Business Administration (SBA) - This government agency primarily guarantees a certain percentage of short- and long-term loans made by private lenders to entrepreneurs and small businesses meeting certain qualifications.

Farm Credit agencies - The government originally financed the lending institutions that make up the farm credit system, but now they are cooperatives owned by the people who borrow money from them. Farm Credit agencies make short- and long-term loans for production or service agribusinesses. The money may be used to purchase land or assets or for operating funds.

Manufacturers and retailers - Manufacturers and retailers provide short- and long-term credit. In many cases, the manufacturer or retailer from whom a business purchases inventory for resale or the supplies needed to run a business offers credit to that business. Such credit is not only convenient but also helps the business pay for inventory or supplies when money is available. Certain merchants or dealers may also give a discount on the merchandise being purchased if the money is paid in a designated period of time. In some cases, the manufacturer or retailer may sell merchandise on consignment. When merchandise is sold on consignment, it does not have to be paid for until it is sold by the business. If the merchandise is not sold, it can be returned.

Farm Services Agency/Agricultural Stabilization and Conservation Service - In 1995, the Farmers Home Administration reorganized to only handle housing loans, and now this government agency handles government and government-guaranteed farm loans. These loans are made to persons with experience in agricultural production, who will be the owners or operators of an agricultural production facility when the loan is closed. Through this agency, agricultural producers who cannot obtain credit elsewhere can secure a loan. Loans can be secured for farm ownership, soil and water conservation improvements, operating expenses, and emergency purposes.

Venture capital can also be used to fund a new business. Venture capital is money that can be invested in the ownership of a business. Acquiring venture capital may involve selling stock on the open market to investors or taking on partners.

Personal sources of financing can be very useful when setting up a new business, particularly if sufficient funding is not available from these other sources. The capital could come from loans on life insurance policies, personal trusts, or savings plans that were established with a present employer. Money could also be borrowed from family members or friends.

Information Needed for Loans

Some of the information required by a financial institution providing a business loan is the same as that needed for a personal loan. If an individual obtains a personal loan for a car, the financial institution will first check to see if the individual has a good credit history. To be sure that if the individual fails to repay the loan, the bank can get its money back; the bank makes the car collateral for the loan. If the individual cannot pay the financial institution for some reason, the bank repossesses the car from the individual and sells it.

The same principle applies to business loans. The financial institution will check to see if an individual or business has a good credit history. It will try to determine if the assets being put up as collateral are enough to repay the loan if the individual or business borrowing the money cannot repay it and if the individual borrowing the money will have sufficient cash flow from personal and business income to repay the interest and principal of the loan.

If the business has already been established, the financial institution will look at its history, such as past income and expenses, in addition to the information listed above. The bank will not be as concerned with what the business says it can do in the future as with what it has done in the past.

If the business is just being started, the financial institution will look at the history and the business idea or business plan of the individuals requesting the loan in addition to their credit history, assets, and cash flow. For example, it may examine the

entrepreneur's experience and training in trying to determine if they will be successful in running a business. The institution will also examine the feasibility of the business idea.

In most cases, a financial institution will not lend the total amount needed to start a business, so the entrepreneur will most likely need to invest personal income as well as the money from the loan. Financial institutions will generally loan only as much money as they can recap by selling the asset being purchased if the loan cannot be repaid. Most business loans require a substantial personal investment by the individuals starting the business.

Determining Credit Worthiness

Lenders typically look at four factors when deciding whether to grant a loan. These factors are often referred to as the "Four C's"--character, capacity, capital, and collateral.

Character - Character refers to the credit history of the entrepreneur applying for a loan. Lenders examine the applicant's financial worth, how much he or she owes, whether bills are paid on time, and any past history of problems repaying credit. They also look at the stability of his or her lifestyle or past business operations.

Capacity - Lenders want to know whether the applicant will be able to repay the loan. Specifically, lenders want to know whether the business will have the ability to operate effectively in the future and generate enough revenue to pay back the loan and meet other business expenses. A lender will examine the applicant's business operations, resources, and expenses to try to determine his or her capacity to repay a loan over time.

Capital - Lenders examine the cash flow of the entrepreneur to determine whether he or she has the capital available to meet his or her financial obligations. They look at whether money will be available to pay off the principal and interest when payments are due.

Collateral - Lenders want to be sure the applicant has assets that can be offered as security for the loan. Should the individual fail to make loan payments, the collateral is forfeited to the lender to satisfy the loan.

Franchises

A way to enter business without developing an entirely new business operation is to purchase a franchise. A franchise is an agreement that grants the right to operate a business, such as a fast-food restaurant, in the name of a recognized company. The franchisee, or person purchasing the franchise, hopes to reduce his or her risk by purchasing a business that has been shown to be successful. The franchisor, or owner of the existing business, provides all of the business planning needed to operate the business, including information about starting up the business, management, and day-to-day operations.

Buying a franchise may make it easier to obtain financing. Franchisors often assist franchisees by helping to arrange loans from lenders. Their influence makes it more likely that a loan will be approved. A disadvantage to starting a franchise is that the initial franchise fee and on-going royalty fees can often be expensive.

Summary

Money is required in order to start and run a business. This money is generally obtained through loans from a person or financial institution. Different sources of financing may be used, including commercial banks, savings and loans, the Small Business Administration, manufacturers and retailers, and the Farm Services Agency. In order to receive financing, an individual must supply the institution with such information as a credit history, assets, and cash flow data.

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Lesson 8:
Making Business Decisions

Sometimes business plans do not work out, and adjustments must be made. Being able to make decisions and adjust a business plan is an important part of starting and operating a business.

Making Decisions

What should be done if sales are not as high as expected? No single answer to this question exists, and every possible answer will not be applicable to every type of business. In some cases, the answer may be to cut expenses so that the projected profit goal can be achieved. For other businesses, increasing advertising may generate enough extra sales to offset the expense and make the projected profit goal. Some businesses may need to change locations or add a product or service to attract customers to the business or the answer to the problem may be a combination of solutions.

Many things can go wrong when starting and operating a business. It is important to be able to make decisions and deal with problems as they occur. Problems should never be ignored, but neither should an owner or manager overreact, since the problem may be temporary and abrupt changes could worsen the situation. All available facts about a problem need to be collected, and a solution determined through a logical decision-making process. Making decisions and solving problems is a part of doing business.

Steps in Making Decisions

The decision-making process is a logical process with seven main steps. The steps of the process are listed below.

1. Identify the problem.

2. Gather and consider all facts relating to the problem.

3. Determine objectives. The objectives should allow the decision maker to reach the goal of solving the problem. If the problem is decreased sales, an objective might be to extend store hours to try to increase sales.

4. Identify several possible solutions to the problem. If no solution can be determined, gather more facts concerning the problem.

5. Choose the logical solution from the alternatives and implement it. Choosing a solution from several alternatives is the hardest part of decision-making, but making a logical choice is possible if all the facts have been gathered.

6. Monitor the situation to see if the problem is solved. Unfortunately, the proposed solution may not solve the problem, so the results of implementing the solution need to be checked. If the problem still exists, make small adjustments and monitor the situation to see if they correct the problem.

7. If the chosen solution does not correct the problem, repeat the process. Reexamine the facts surrounding the problem. Consider any insights gained from the first attempt to solve the problem that may guide the decision-making process. Select and implement an alternative solution.

The decision-making process involves trial and error. If the first effort to solve a problem does not lead to a correct solution, each new attempt should come closer and closer to a final solution to the problem. The decision-making process is illustrated in the following example.

Ashley has owned and operated a small hardware store for three years. She has kept daily sales and expense records since she started her business. Ashley reviews sales records and notices that for the first week in November she has had a 15 percent sales decrease compared to the same week last year. She is very concerned, so she decides to gather facts to determine why sales have been so much less than the previous year.

Ashley knows that she had increased sales by an average of 5 percent over last year up until the first week of November. After checking her expenses from last year, she notices that she this year has spent only half the amount on advertising she spent last year.

Ashley comes up with three possible solutions to her problem. The three possibilities are to run a special advertisement in the paper, extend the hours the business is open, or cut back on some part-time help to lower expenses until sales get better. After

carefully considering the facts and the possible solutions, she decides to spend some money on advertising.

At the end of the second week in November, she again checks her sales, and while they have increased, the increase is only 2 percent over the same week last year, rather than her 5 percent average. Ashley is still very concerned and decides she needs to examine the facts again. As she is looking at last year's sales figures, Gus, a local repairman and a good customer, comes into the store. Gus starts talking about how the weather is so much better than last year. Suddenly, Ashley thinks of some facts she had not considered.

Ashley checks the notes she made last year about sales in November. She finds that the first snows had fallen in the first and second weeks of November last year and that she sold out of snow shovels, salt, scrapers, and sleds and had to reorder. Ashley now knows that the sales losses will be recovered when the first snow falls. She has already purchased more shovels, salt, scrapers, and sleds than last year. Ashley decides to add a note next to each daily sales figure describing the weather conditions for that particular day.

Many times the first attempt to solve a problem may not work. Good record keeping includes records or notes on anything that affects the operations of a business. The more information a business owner has to work with, the better the decision.

The Importance of a Business Budget

A business budget consists of two basic parts. The first part of the budget is the expected income for the period, and the second part plans for the expenditures of that income. The figures used on the budget are based mainly on past experience. A budget is a very simple but important part of operating a business that helps the business owner take control of finances and reach desired goals. Budgets should be done monthly.

As a planning tool, a budget helps a business set priorities and then allows the owner or manager to monitor progress toward established goals. For example, a business might have a goal of expanding. The owner of the business might use a budget to ensure that expenses are less than income so that a profit that can be used for expansion is realized. A budget can help the owner or manager of a business formulate intelligent business decisions.

In some cases a business may be running well, but changes would improve it. The objectives and goals of a business may change over time, and decisions need to be made and plans implemented to accommodate those changes. A budget may help to indicate where changes can be made to improve the business.

A budget is only a guide to reaching goals and so needs to remain flexible. Sometimes events do not occur as planned, and budgets may need to be changed to eliminate problems. A flexible business budget can be adapted into a contingency plan by turning budget figures into objectives that will guide a business to adjust spending to reach a desired goal.

Finally, budgets allow businesses to judge how changes have affected them. A budget shows how income and expenses are altered by business decisions and the effect the changes have on projected returns. The manager of a business can use the budget to determine the effectiveness of his or her decisions.

Summary

Making decisions is just another part of operating a business. Even with the best plans, decisions must be made and implemented to meet changing situations. If an owner or manager follows a logical decision-making process, however, changes may be more easily made. Budgets aid in the decision-making process by allowing a business to see how changes will affect or have affected the income and expenses of a business.

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GLOSSARY

A

advertising: A promotional message that a sponsor pays to have placed in different media such as newspapers and radio.

amortized loan: Loan payed off in installments over time.

approach: The way in which the salesperson solicits a purchase from the customer in a presentation.

asset: A resource or property owned by a business.

average product: Total output produced divided by the total number of units of input.

B

balance sheet: A financial statement showing a business's assets, liabilities, and net worth as of a specific date.

basis: The difference between the local cash price and the price of an expiring futures contract.

bonds: Certificates of debt that promise payment of interest on specified dates and payment of the original investment upon maturity.

business plan: A detailed proposal that describes all aspects of a new business.

C

call option: The right to purchase a futures contract at a designated strike price.

cash flow: The way money flows into and out of a business.

cash flow statement: A financial statement that summarizes either projected receipts or past cash flows for a business.

cash market: Market in which an actual cash transaction takes place and commodities are exchanged.

close-ended question: Question that generally provides information through a very short answer.

commodities market: Market in which cash commodities and contracts for future delivery are traded; also referred to as a *futures market.*

common stock: Stock that is secondary to preferred stock in payment of dividends.

compound interest: Interest that is calculated not only on the principal of a loan but also on accrued interest payments.

constant substitution: Type of substitution in which one resource can be substituted for another at the same rate for each additional unit of input.

constructive criticism: Criticism that identifies a problem and gives instructions for solving it.

contract: A legal agreement that creates an obligation binding the parties involved.

cooperative: A special type of business system characterized by the absence of the profit motive.

copy: The main message of an advertisement.

corporation: A separate legal entity owned by people who hold shares of stock in the business.

cost of production: Monetary outlay for the fixed and variable input factors needed to obtain output.

credit: The transfer of money on the promise of repayment at some future date.

credit history: A record of how an individual has managed finances in the past.

current asset: Asset that can or will be used or sold within one year.

current liability: A liability that is payable within one year.

D

demand: The amount buyers are willing and able to purchase at different prices at a given time and place.

demand curve: A graphic illustration of a demand schedule.

demand schedule: A set of prices and the corresponding quantities of an item that would be purchased at each price at a given time and place.

depreciation: The loss of value each year due to wear, age, or obsolescence.

diminishing: Decreasing.

direct sales: Sales made by the salesperson directly to the final consumer at the consumer's home or business.

E

elastic: Type of elasticity in which the change in price is less than the relative change in quantity available.

elasticity: A measure of how sensitive the market is to change in price or quantity.

entrepreneur: A person who organizes and manages a business.

equilibrium price: Point at which supply and demand are equal.

F

fixed asset: Asset that will not be used or sold and converted into cash within one year; also referred to as a *noncurrent asset.*

fixed cost: Cost incurred regardless of the level of production or use.

franchise: An agreement that grants the right to operate a business in the name of a recognized company.

free enterprise system: An economic system in which goods and services are produced and traded through a complicated system of prices and markets by private individuals and businesses.

futures contract: A legally binding agreement made on a futures exchange to buy or sell a commodity.

G

goal: A statement of what an individual wants to accomplish either personally or financially.

grain reserves: Stores of grain used by the government as an inflation-fighting tool.

H

headline: A line of print in an advertisement that is designed to catch the reader's attention.

hedging: A means of managing price or market risk by taking a position in the futures market that is the opposite of that held in the cash market.

hidden objections: Objections made by the customer to disguise true objections; also called *smokescreens.*

I

income statement: A financial statement that is a summary of a business's income and expenses for a specific period.

inelastic: A type of elasticity in which the change in price is greater than the relative change in quantity.

input: A factor of production or a basic resource; may be fixed or variable in nature.

interest: Money paid on money that is invested or borrowed.

L

Law of Demand: Economic law that states that when the price of a product increases with no change in factors other than price, less of the product will be purchased.

Law of Supply: Economic law that states that when the price of a product is lowered with no change in factors other than price, less of the product will be supplied.

liability: A debt owed by a business.

liquidity: The capacity of a business to generate cash to meet anticipated and unanticipated cash demands as they occur without disruption of operations or a loss of value.

long hedge: Buying a futures contract to offset the risk of a price increase on a future cash commodity purchase.

long-term credit: Money borrowed for more than one year; also known as *noncurrent credit.*

long-term liability: Liability that is not payable within one year; also called a *noncurrent liability.*

M

marginal: The change or difference between two factors.

marginal cost: The change in total cost, or total variable cost, due to a one-unit change in output.

marginal input cost: The change in total cost, or total variable cost, due to a one-unit change in input.

marginal product: The change in output resulting from each additional unit of input; also known as *marginal yield.*

marginal revenue: The change in total return due to a one-unit change in output.

marginal revenue product: The change in total revenue due to a one-unit change in input.

Maslow's Hierarchy of Needs: System for classifying needs developed by the psychologist Abraham Maslow that identifies levels of needs and how needs motivate people to act.

mutual fund: Diversified investment that is professionally managed.

N

net income: Increase in capital resulting from profit-making activities.

net loss: Decrease in capital resulting from profit-making activities.

net return: Financial return after all costs have been paid; also referred to as *profit.*

net worth: The net ownership a sole proprietor, partnership, corporation, or cooperative has in a business.

noncash expense: An expense in which cash is not actually spent by the business.

nonconstructive criticism: Criticism that identifies the problem, but does not suggest a solution.

nonverbal communication: Any method other than the spoken or written word that is used in the communication process to convey a message from sender to receiver.

O

objective: A step necessary to achieve a goal.

open-ended question: A question that requires an extensive answer.

opportunity cost: The return on the best alternative not selected.

opposite position: Offsetting a position in the commodities market.

option: A contract that gives its owner the right to buy or sell a futures contract at a certain price for a certain period of time.

output: Unit of production, resulting from the combination of variable and fixed inputs.

P

partnership: A business association of two or more persons who have agreed to combine their financial assets, labor, property, and skills.

personal selling: Component of a promotional campaign that requires the person selling a product or service to perform the tasks of advertising, public relations, and sales promotion.

point of maximum profit: The point at which marginal cost equals marginal revenue and marginal input cost equals marginal revenue product.

preferred stock: Stock that takes precedence in the payment of dividends.

premium: Price paid for an option.

price controls: Limits placed on prices by the government during shortages to prevent inflation as well as windfall profits by producers.

price determination: General principles of supply and demand used to determine price.

price discovery: The process by which an estimate of supply and demand and market clearing price is reached.

principal: The amount of money loaned.

principle of diminishing economic returns: Economic law stating that at some point marginal economic returns decrease with each additional unit of input.

principle of diminishing physical returns: Economic law stating that at some point in time the marginal product decreases with each additional unit of input.

processing sales: Market in which a salesperson sells either services or inputs like raw materials or processing equipment to a manufacturer to produce a saleable product.

production: Process of combining inputs to yield output.

public relations: Component of a promotional campaign that involves performing various activities designed to create a positive image to promote goodwill toward a business.

put option: The right to sell a futures contract at a specific strike price.

R

realized hedge price: The difference between the amount of the cash market transaction and the amount of the futures market transaction.

resume: A written summary of an individual's qualifications for employment.

retail sales: A market in which a product is sold directly to the final consumer.

revenue: Income received by the business.

S

sales promotion: Component of a promotional campaign that includes the use of coupons, rebates, contests and sweepstakes, and visual merchandising.

secured loan: A loan in which an asset is put up for collateral.

service business: A business that offers services to consumers.

short hedge: Selling a futures contract to offset the risk of a decline in prices on a future cash commodity sale.

short-term credit: Money borrowed for a term of less than a year; also known as *current credit.*

signature: The symbol of the business; also referred to as a *logo.*

simple interest: Interest that is paid only on the principal of a loan.

sole proprietorship: Arrangement in which the business is owned by one person.

solvency: Capital structure of a business in which the sale of all assets would generate sufficient cash to pay off all liabilities.

speculator: An investor who purchases or sells futures contracts to make a profit but has no desire to actually obtain a commodity.

statement of cash flows: Financial statement that shows in what areas cash inflows and outflows occur in a business.

stock market: Market in which shares of stock are bought and sold.

stockholder: Individual or another company that purchases shares of stock in a business.

stock: Share of ownership in a company.

strike price: The guaranteed price at which an option can be bought.

substitution: Replacing one input with another in an attempt to maximize profit.

supply: The amount of product or commodity producers are willing and able to provide at different prices at a given time and place.

supply curve: A graph illustrating a supply schedule.

supply schedule: A listing of the amount of a product that the industry is willing to offer for sale at different prices.

T

total cost: The sum of the cost of fixed and variable inputs at any given level of production.

total product: Total output or yield.

total return: Total of all receipts from a project before expenses are deducted.

total revenue: Total income.

U

unit elastic: Measure of elasticity in which the change in price is equal to the relative change in quantity available.

unsecured loan: A loan that is based on a good credit history and does not require collateral; also known as signature loan.

V

valid objection: Statement made by a customer that is true or at least true based on the customer's knowledge.

variable cost: Cost that changes in response to the production level or the amount of use.

variable substitution: Type of substitution in which one resource can be substituted for part of another at a different rate for each additional unit of input.

verbal communication: Any form of communication that consists of either spoken or written words.

W

wholesale sales: A market in which the wholesaler purchases a product in bulk with the intention of dividing it into smaller portions to sell to retailers or directly to the final consumers.

work ethics: Principles of right conduct as accepted by a profession or by the business world in general.