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Report

To: The Shareholders of ASSI

From: Rodica Cirlan, Business Planning Manager

Date: 20/06/2023

Subject: Profit Maximization.

1. Introduction

This report will analyse economic theories considering ASSI's situation and recommend practical steps for the company's improvement. As ASSI has been experiencing growth and profitability pressure over the past years, the main shareholder Jesse Zole is dissatisfied with the decline in profit.

First, the Profit Maximisation theory will be explained and applied in light of ASSI and Jesse Zole's statement, as well as other relevant issues for the firm to improve.

Equally other appropriate economic theories such as demand and supply, business environment, business objectives, market structure in a practical environment and stakeholder issues will be discussed and evaluated, which will be considered by the company's management in decision-making. As well as view it in light of the UK retail industry.

As to be successful means having an effective strategy, which is based on a careful analysis of the business environment. ASSI and other retail companies are impacted in numerous positive and negative ways by the business environment, and because the global market is so dynamic today, organisations must be prepared to confront a variety of challenges presented by the constantly shifting business environment. The global business environment is comprised of economic, social, and political factors which require firms to be adjustable because such changes bring both challenges and opportunities to a company's diverse operations (Radim, 2021).

The report will end with a conclusion and practical recommendations for ASSI's management to assist in further growth and profitability maximisation.

2. Profit Maximisation Theory

Sloman, et al. (2019) define the profit maximising rule as that profit is at maximum when ASSI's marginal revenue is equal to the cost. Profit is deemed to be the primary concern for most businesses, including the UK retail industry. The statement of the main shareholder demonstrates the core objective of ASSI. This may be the case for minor operations under the direct control of the owner; however, large corporations face the principal-agent problem and

may also be concerned with objectives such as market share, growth and other non-profit objectives. Profit, however, remains an important objective because it provides a source of financing for future investments; it gives incentives for stakeholders, dividends for shareholders, performance-related compensation increases for employees, price reductions or enhanced products for consumers and assures the business's long-term survival and measures how effective are the management policies and permits comparisons with other forms of investment (Griffiths, 2011).

⁶ The profit-maximising theory focuses on two essential assumptions: first, owners control the day-to-day administration of the firm, so there is no principal-agent problem; and second, the primary objective of owners is to increase profits. As will be seen later see, if either of these assumptions fails to hold, the self-evident' argument for profit maximisation is compromised, as is seen in ASSI's case. Because the owners have been excluded from company operations, the agents may be allowed to decide as they choose, having a greater understanding of the firm. Thus, agents may not always agree with owners and their goals could dwarf profit (Griffiths, 2011). In the case of ASSI Jesse Zole is not the manager of the company and does not fully understand the details of the operation, therefore there is a principal-agent problem.

Advantages of profit maximisation include long-term improvement of the cash flow. In turn, this results in benefits for shareholders and offers an appealing investment opportunity. It assures as well strategic business growth - it is essential to know when to move the company to the next phase. In our case, it is the company's turn to shift to another level and revise its cost-saving strategies without compromising on the quality of the products.

The disadvantages of that include brand damage as it may negatively impact brand perception by making organisations appear profit-driven. The main shareholder of ASSI suggested increasing the prices, especially on their own products since they are exclusive to them, however as stated above it could damage the brand name and turn the customers away, they are able nowadays to shop at the competitors and find substitutes.

Profit maximisation could negatively impact customers if a business sells low-quality goods. Lowering manufacturing costs will boost revenue in the short run, but customers will notice any quality drop and leave. The same happens when the prices are inflated (American Express, 2021).

As well as the ASSI and other companies do not have to appear profit-driven, it is demonstrated that for businesses to thrive, they need to interact with the community as it is a win-win situation, the company wins its market share, and the community gets to know the brand.

Keat, (2014) suggests that management can always maximise profits in the immediate future. If, for example, a company anticipates a decline in revenue in the future year, it can maintain profitability by reducing expenses. And if ASSI's management desires to achieve this objective without an immediate impact on revenue, it can eliminate certain development initiatives.

3. Discussion and Evaluation of Market Structure, Demand and Supply, Business Environment, Business Objectives, and Stakeholder Issues. Their consideration in decision-making for ASSI.

Market structure

Market structure is the manner ⁷ markets are organised in a competitive environment including the interactions of individuals, firms and other organisations and affecting or being affected primarily by the conduct and performance of the business. The figure below represents the type of markets and their main characteristics.

Characteristics	Perfect Competition	Monopolistic Competition	Oligopoly	Monopoly
No. of Sellers/producers	very many	many	few	one
Type of product/substitutes	homogeneous (identical, standardised)/ identical substitutes	heterogeneous (differentiated)/ very similar substitutes	homogeneous (standardised or differentiated)/ close substitutes	unique/ no close substitutes
Barriers to entry	practically none	low	high	very high
Information dissemination	perfect	imperfect	imperfect	very imperfect

Kapunda (2017)

Based on the information above ASSI belongs to an oligopoly market, the same as Tesco, Sainsbury's and Aldi. Oligopoly represents a market where there are relatively few significant companies, the number is typically between 2 and 10. It means that those companies have a big market share, like ASSI.

As there are few firms in an oligopolistic market, the manager must consider how the decisions will likely impact the decisions of the other firms. Moreover, the actions of other firms will

significantly influence the manager's optimal decisions. The most effective decision regarding whether to increase or decrease the price depends on the manager's estimation of how other managers will react. Therefore, if the prices of the competitors are lower or higher, ASSI has to follow them in order to maintain sales, the decision should be based on the competitors' choices. Thus, if the prices are matched to the competitors, it will increase the demand, if not, the demand decreases.

Competition may be reduced with collusion, it will boost the revenue as well, another way to increase profits is merging with other companies, (Baye, 2017). However, it may be legally restricted by the authorities as in the case of Asda and Sainsbury's.

Demand and Supply

Analysing economic theories ease the process and ensures effective decision-making. Demand is the willingness and ability of customers to purchase a specified quantity of a product or service at a specified price. The supply of a product or service is the vendors' ability to provide a given quantity at a given price.

The demand and supply models are beneficial for explaining how the price and quantity sold by ASSI are determined and how external factors influence the values of these variables (Eastin and Arbogast, n.d).

If the selling price of ASSI products increases, demand will decrease. This relationship is referred to as the law of demand, and it has two causes: people cannot afford to purchase the item with their budget. Their income's purchasing power (real income) has decreased. This is known as the income impact of a price increase. ASSI's products are now more expensive compared to competitors' commodities. People, therefore, turn to alternative or substitute goods. This is referred to as the substitution effect of price increases. For instance, if the price of coffee increases, we will be unable to purchase as much as before and people will likely consume more tea, and hot chocolate, as a result. In a similar way when the price of a product decreases, demand will increase. People can afford to purchase more (income effect), and they will move to more expensive brands.

However, the price is not the only variable that affects the demand, it includes tastes, the number and price of the substitutes and complementary goods, income etc.

The general correlation between supply and price is as follows: when the price of a product increases, so does the quantity supplied. The reasons are that under a certain level of production, firms see that their expenses are rising at a rapid pace. Only if prices increase will it be profitable to produce more and cover additional expenses. The higher a product's price, the more beneficial it is to produce. Therefore, firms will be motivated to generate more of it

by shifting away from less profitable items. If a good's price maintains high, fresh suppliers will be encouraged to enter the market and total market supply increases. Other variables of supply include the cost of production, the substitutes in supply, and expectations of future price changes (Sloman and Jones, 2020).

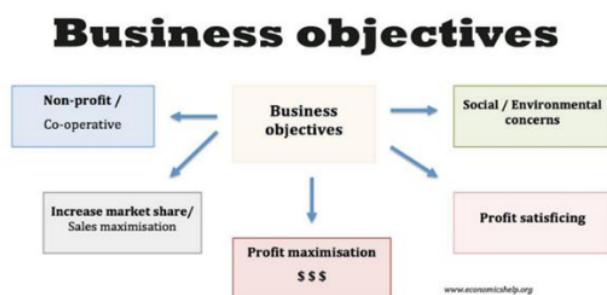
In our case, if ASSI's management decides to increase the prices, the demand will decrease and negatively affect the profit. If they decide to raise the price of elastic goods like petrol for example, it does not mean that consumers will respond positively to the rise in price, because they can turn to the competitors who do not follow the price increase.

Business Environment

A business does not operate separately within its business environment; rather, it works within a broader framework. It consists of forces that offer opportunities but also faces potential risks to the company. This includes laws, government agencies, and regulations and is capable of influencing or constraining people or organisations within society (Philip, 2019). For instance, the war between Russia and Ukraine generated higher prices for bills and higher costs of living and fuel which consequently made supermarkets increase the prices to cover the costs. ASSI must consider all these circumstances and understand that consumers now have lower incomes, meaning the inability to buy goods that are not necessary or look for cheaper alternatives.

Business Objectives

Business Objectives do not include only profit maximisation and the figure below illustrates the main ones.



The non-profit objective involves community engagement and charity partnerships. Increasing the market share is another objective, and it is long-term input in profit

maximisation, Social/environmental concerns are another business objective which implies sustainability, “greener” and planet-friendly operation.

¹⁴ The decision-making process of settling for adequate rather than ideal results is known as satisficing. Satisficing strives to be rational and reduces expenses or costs. Under a satisficing strategy, if a consumer required an instrument to process and solve a problem, they would choose the simplest, available piece of equipment, even if more effective options were available for a higher price and more effort. For instance, satisficing may involve using a single software title for ASSI as opposed to purchasing an entire software package with additional elements (Frankenfield, 2022).

Therefore, it focuses on reducing expenditure, which is relevant in ASSI's case, as it increases the profit in the long run.

Stakeholder Issues

ASSI must consider internal and external stakeholders, as now, building sustainable value for society rather than just profits for shareholders has become a necessity.

- Shareholders: Despite stakeholder capitalism, shareholders still possess power. They vote on corporate goals and affect stock market value and investment.
- Employee absence can impact plans, corporate management, and production. Employee review websites, which could limit an organization's ability to recruit and retain top talent.
- Customers: The desires and opinions of customers determine a company's sales. Consumer trends and behaviours significantly impact the success of brands. On social media, customers can promote or criticise businesses.
- Suppliers: All parts of the supply chain depend on the business being supplied. Each link's purpose depends on the chain's communications, operational processes, transport, and payments.
- ¹² • Regulators: Regulators and government agencies may hold companies responsible, tax them, and even stop them from trading if they violate legal and ethical standards, examples of regulators are HMRC, Competition and Markets Authority.
- NGOs: Raising public awareness can compel corporations to improve labour conditions, lessen their environmental effect, or reconcile with the community.
- Local communities: Goodwill for the local community attracts consumers and employees and supports growth. If commercial activity harms the community, it is challenging to continue it.

4. Conclusion

This report covered the profit maximisation concept as the main business objective, its advantages, and disadvantages, in the context of the shareholder's statement. It was concluded that it does not have to be the only objective of the firm as in conjunction with other objectives it creates value to the customer, therefore generating long-term profit and business survival. Increasing the prices of goods nowadays when people's income is lower because of the higher bills, and higher cost of living in general, will only turn the customers away. In our case, if ASSI's management decides to increase the prices, the demand will decrease and negatively affect the profit.

¹ The other economic theories such as demand and supply, business environment, business objectives, market structure and stakeholder issues were discussed and evaluated, and those aspects aid efficient decision-making.

Due to the small number of firms in an oligopolistic market, the manager must consider how the decisions will likely affect the other firms' decisions. The optimal decision regarding whether to increase or decrease the price depends on the manager's estimation of the reactions of other managers.

ASSI must now consider both internal and external stakeholders, as creating sustainable value for society, as opposed to just profits for shareholders, has become a requirement.

5. Recommendations

To increase the profit, the company does not need to concentrate on profit maximisation solely. Therefore, the following steps are recommended to pursue:

1. The non-profit objective involves community engagement and charity partnerships. Thus, ASSI has to partner with charities and donate goods, and organise regular campaigns, for instance, if a customer buys a certain product 5% of the revenue could be donated to a nominated charity. This will enhance the brand's name and have an input in long-run profit maximisation for ASSI.
2. ASSI has to ensure "greener" and planet-friendly operations, which include logistics and recycling. The company has to use less plastic in their packaging and produce goods made of recycled items. ASSI must promote recycling and give vouchers to customers who bring recyclable items back to the store. Then use those vouchers in-store when purchasing for more than £20, which will boost revenue as well.
3. Cost structure management is a major step in ensuring profitability. Under a satisficing strategy, if a consumer required an instrument to process and solve a problem, they would choose the simplest, and the most affordable. So ASSI has to choose the

simplest package when changing its software in order to speed up the processes but ensure it has the same effects.

4. Besides that, ASSI has to increase the production of the items that sell better than others to improve cash flows.
5. Reduce the number of employees and revise their working hours and job scope, train them to be able to cover each other and provide excellent customer service.
6. Negotiate a lower price for the goods with the manufacturer when increasing the quantity demanded (bulk buying).
7. Open smaller versions of their stores in prime locations, as it will reduce fixed costs. It has to be without too many parking spaces, fuel forecourts and restaurants. For example, Sainsbury's opened their local stores.
8. Implement a loyalty card system, it will attract customers to come back to ASSI and assist in analysing consumers' behaviour and their needs. ¹⁵ Tesco and Sainsbury's have a Club Card and Nectar Card, respectively.
9. Merge with the suppliers, as it will ensure lower prices for the products, therefore a higher margin.
10. ASSI must shift away from less profitable items and supply more of the ones with a higher margin.
11. ASSI must create an essential, more affordable line with lower prices to meet customers' needs, and considering the high cost of leaving nowadays, therefore it will attract customers with lower incomes.
12. Advertising should continue until the increased profit from increased sales just covers the final pound spent on advertising, as it is essential in an oligopolistic market in order to increase revenue (Samuelson, 2015).
13. To organise a quick and easy check-out experience for customers, as technology generates demand, therefore profit.
14. ASSI needs leading indications of possible changes in stakeholder attitudes and to understand how various stakeholders affect its company. Reports that include the analysis of all stakeholder groups must be provided to the company before attitude changes affect sales, and share value (Alva,2021).
15. Match the prices to the competitors' prices for example Tesco matches the prices with Aldi.
16. Rent out the spaces that are not in use.
17. Sell unused inventory.

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