

7.2_E



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Part 3

Now, an important concept is the notion of *value added*. What do I mean by value added? Well, to help you understand this idea clearly, can you look for a moment at the leaflet I have given you from the Monckton Crystal Company? As you can see, the ingredients for making glass – i.e., sand, lead oxide and other chemicals – go through several stages of production in order to be made into beautiful glass objects that customers will want to pay money for. However, looking at it another way, when a business makes raw materials into something else, it is actually ‘adding value’ to the raw materials. In fact, at each *stage* of production, value is added to the raw materials. In financial terms, we can calculate added value by comparing the cost of the raw materials and the price which the goods are actually sold for. Let’s look at an example of this. Say the company buys in some raw materials for £3,000. From these materials, the company makes 2,000 glass products which it sells for £4 each. The income from sales will be £8,000. Subtract the cost of the raw materials from the income from sales. The difference between these two figures is £5,000, and that’s the ‘value added’. Why is value added so important? Well, the point is that if companies know exactly which stages of production add the most or least value, then they can develop and improve their products and their production methods. In this way, they can maximize the benefits of the production operation to the business.

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Answers

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Now, **an important concept is** the notion of *value added*. **What do I mean by** value added? Well, to help you understand this idea clearly, can you look for a moment at the leaflet I have given you from the Monckton Crystal Company? **As you can see**, the ingredients for making glass – i.e., sand, lead oxide and other chemicals – go through several stages of production in order to be made into beautiful glass objects that customers will want to pay money for. However, **looking at it another way**, when a business makes raw materials into something else, it is actually ‘adding value’ to the raw materials. In fact, at each *stage* of production, value is added to the raw materials. **In financial terms**, we can calculate added value by comparing the cost of the raw materials and the price which the goods are actually sold for. Let’s look at an example of this. **Say** the company buys in some raw materials for £3,000. From these materials, the company makes 2,000 glass products which it sells for £4 each. The income from sales will be £8,000. Subtract the cost of the raw materials from the income from sales. The difference between these two figures is £5,000, and that’s the ‘value added’. Why is value added so important? Well, **the point is** that if companies know exactly which stages of production add the most or least value, then they can develop and improve their products and their production methods. **In this way**, they can maximize the benefits of the production operation to the business.