June 2013

ECO-01 Business Organisation

PART—A

1. Distinguish between any two of the following : 5+5

(a) Employment and Profession

Ans:

Employment	Profession
Employment commences only by entering into a service agreement (contract) with the employer.	The profession may commence on completion of a degree course, by getting a certificate of practice and become a member of concerned professional body.
An employment is an economic activity including occupation in which individuals work for their superiors with the motive of earning renumeration in return.	A profession is an economic activity that includes activities requiring special skills and knowledge in their occupation.
For example clerks, managers, peons etc	For example teachers, doctors, lawyers etc.
No capital investment is required.	Limited capital investment is required for equipment and establishment of office.
In employment, there is no risk involved. Employee gets wage or salary regularly as long as the firm continues in operation.	There is little risk present. Possibility of not getting enough fee to meet the expenditure on establishment
The main objective of employment is to earn income in the form of salary by satisfying the employer.	The main objective of a profession is to provide service.
It involves performing the work as assigned by the employer.	It involves the rendering of personalized services of specialized nature.

(b) Private limited company and Public limited company

Ans:

Private Limited Company	Public limited Company
Private Limited Company refers to the company which is not listed on a stock exchange and the shares are held privately by the members concerned.	Public Limited Company implies a company that is listed on a recognized stock exchange and whose shares are traded openly by the public.
The minimum number of members in the case of a private limited company is two and can be formed more easily.	In the case of a public limited company: the minimum number is seven
Maximum is fifty.	There is no maximum limit.

restricts the right to transfer its shares	The right of the shareholder to transfer his shares is not restricted.
prohibits any invitation to the public to subscribe for any shares or debentures of the company.	It can invite public to subscribe for its shares and debentures.

(c) Bank overdraft and Cash credit

Ans: The bank overdraft is a form of short-term credit that account holders can take advantage of without entering into a credit agreement by overdrawing their current account. Overdraft is a temporary arrangement with the bank which permits the company to overdraw from its current deposit account with the bank up to a certain limit. This means that if an outgoing payment is higher than the money still available in the account, the payment can still be made. The amount of the bank overdraft is determined by the bank or the lender. The overdraft facility is also granted against securities as in the case of cash credit. Interest is charged only on the amount actually overdrawn. Overdraft facility is offered for meeting short-term obligations of individuals or businesses. The loan duration can vary and it can be monthly, quarterly, half yearly or yearly. The process of getting a business overdraft is very straightforward and is simply a matter of discussing your needs with your bank. It can be drawn on at any time and is most useful for day-to-day practice expenses.

One advantage of the bank overdraft is that it can be used to pay short-term liabilities even if there is not enough money in the account at the time of maturity. If a company needs a short-term loan of a small amount, the bank overdraft is the most uncomplicated option, as it is not necessary to submit a separate loan application to the bank. Another biggest benefit of business overdrafts is the speed and availability with which you can access cash.

The biggest disadvantage of the bank overdraft is that it is very expensive, as banks pay very well for providing this short-term credit. The longer an account is unbalanced, the higher the interest payments. Another disadvantage is that the limit can be adjusted downwards by the bank at will depending on how often the bank overdraft is used and how well the account holder is able to balance the account again afterwards.

Cash credit refers to an arrangement on a continuing basis whereby the commercial bank allows money to be drawn as advance from time to time within a specified limit known as cash credit limit. This facility is granted against the security of goods in stock, or promissory notes bearing a second signature, or other marketable instruments like Government bonds. The company is allowed to draw whatever amount is required at different times within the limit agreed upon. The cash credit limit may be revised according to the value of securities. The money drawn can be repaid as and when possible. Interest is charged on the actual amount withdrawn. It is offered for maintaining the working capital of the business. The loan duration is generally 1 year.

(d) Joint life policy and Group insurance

Ans: Joint Life Policy: This type of assurance involves the insurance of two lives simultaneously in the same policy. The sum assured (policy money) is payable by the insurer upon the death of any one of the assured to the surviving person. If both the policy holders die at the same time, their legal heirs or nominees will be paid the assured sum. A good. Example of a joint life policy is that of a policy on the lives of a husband and wife, payable to the survivor on the death of either of the two.

Group Insurance: Under group insurance, a group of persons under the same employer are covered under a single policy. Premium is paid by the Y employer alone or by the employer and employee jointly. A group insurance policy may cover all the employees or a particular category/section of the employee of the same organisation. However, the employees are covered under this policy as long as they serve with that employer. In group insurance, the insurance contract is between the employer and the insurance company (insurer). A master policy is issued to the employer, while the each employee receives a certificate. The certificate issued to the employee stipulates the amount of coverage that person had, his beneficiary (nominee) and any other rights and privileges he may have under the plan.

The policy is taken for a fixed period, usually 20 years. If the employee (assured) dies before the expiry of the term, the nominee (beneficiary) gets a fixed annual income for the remaining part of the period and the full assured sum at the end of the term. On the other hand, if the assured survives the term, the fill assured sum is paid at the end of the term.

2. Write short notes on any two of the following : 5+5

(a) Hypothecation

Ans: Hypothecation is a mode of creating charge on goods or related documents without the surrender of possession of goods. According to Prof. Herbert Hart, "Hypothecation is a legal transaction whereby goods may be made available as security for a debt without transferring either the property or the possession to the lender". Hypothecation is resorted to such cases where transfer of possession of the property from the borrower to the creditor is either impracticable or inconvenient. For example, if the borrower wants to borrow on the security of motor vehicle, which is being used as a taxi, it shall not be advisable to pledge the vehicle with the bank, as it will deprive him of his livelihood. In the case of hypothecation, an equitable charge is created on the goods for the amount of debt but the hypothecated goods actually remain in the physical possession of the borrower. The borrower who hypothecates the goods is known as 'hypothecator' and the lender is termed as 'hypothecatee'. Hypothecation is done by the borrower by executing a document called a 'letter of hypothecation' in favour of the lender. In this letter it is stated that the said goods or property are at the order and disposition of the lender until the debt is cleared. It also empowers the lender to sell the hypothecated property in the event of default or repayment by the borrower. As the hypothecated goods remain in the possession of the borrower, there is considerable scope for fraud. The same goods may be hypothecated with another person. It is a risky method no doubt. That is why this facility is granted to parties of unquestionable integrity and honesty. Even then the banker should obtain a declaration from the borrower to the effect that the goods are not hypothecated earlier with some other lender and that the borrower has a clear title to the property hypothecated. The bank should carry out regular inspection and physical verification of the hypothecated goods.

(b) Leasing

Ans: A lease is the use of an asset which belongs to some other person. In a lease contract, the possession and use of asset vests with the user called the 'lessee', whereas the ownership remains with the provider called the 'lessor'. In simple words, leasing is a system by which a person gets the right to use an asset by paying a predetermined amount of money called 'rental' periodically over a period of time.

The banks have undertaken this business in a big way. The main advantage of leasing to a business is that, although the legal title of the asset remains with the leasing company, once the first rental has been paid, the business fiml gets the physical possession of the asset to put it on operation. has complete use of the asset without having to finance its acquisition out of its own valuable resources or to seek a loan to cover the cost. In this arrangement business firm need not spare the financial resources at a time to acquire the asset or seek a loan to cover the cost.

(c) Public utility undertaking

Ans: Water, gas, electricity, transport communication, etc.,, are needed by the public in their daily life. Whenever there is any interruption in the supply of such goods or services, the normal life of people is disturbed. For example, If the electricity supply or transport services are not available, public life and activities are severely upset. these services have a great significance to the community. Hence they are termed as essential services or indispensable necessities. The business enterprises established basically to provide efficient and uninterrupted supply of the goods that are absolutely indispensable for a civilised community are referred to as public utility organisations. public utilities are the business undertakings engaged in supplying essential goods and/or services of daily necessity for the general public. The institutions which undertake certain essential services like the Supply of gas, water, electricity, urban transport, etc., are examples of public utility undertakings. All the public utility undertakings have an obligation to supply the essential goods and services to everyone in the community without any discrimination at reasonable prices.

In our day-to-day life, directly or indirectly, we require a number of essential services. In the cities you have tap-water. Similarly various means of transport help you in undertaking your journey everyday. You need electricity Tor lighting, air-conditioning, etc. Electricity is also used for running Factories, trams, railways, irrigating crops, etc. All these services are called public utility services and the organisations which provide these services are known as public utility undertakings.

All the public utility undertakings have an obligation to supply the essential goods and services to everyone in the community without any discrimination at reasonable prices.

Characteristics of public utility undertaking are:

1) Indispensability: Public utilities deal with essential services such as water, gas, light, power, transport, telephone, telegraph, postal services, etc. These services are required to meet basic needs of the community and to provide a civilised and comfortable life to every citizen irrespective of caste and creed. Therefore, these services must be made available regularly, uniformly and adequately. That is why these public utilities are indispensable in all modem societies.

2) Field of operation: The field of operation of public utility undertakings is mostly local. Such concerns fulfil the needs of the citizens, usually of a city, town or at the most of a district. Fo; example, Delhi Milk Supply Undertaking or Mother Dairy supplies milk through its booths at various localities to the people living in Delhi only.

3) Monopolistic or semi-monopolistic position: Undertakings supplying essential public services by nature assume the position of a monopoly. They do not have competitors. You can take the example of Delhi Electric Supply Company. It does not have any competitors for supplying electricity to the residents of Delhi. If another undertaking is involved in the same operation in the same town, equal

amount of money is required which is a waste. To avoid any such wasteful expenditure, monopoly is given to public utilities. However, some public utilities may have a few competitors. Take the case of milk supply in Delhi. Mother Dairy supplies the milk. But Delhi Milk Supply Undertaking or Nanak Milk Supply Company also supplies milk in Delhi. Therefore the position enjoyed by Mother Dairy is semimonopolistic.

4) Regulation and control : These undertakings enjoy a monopolistic or semi-monopolistic position. So, they are in a position to misuse it and exploit the customers. For instance they may supply poor quality goods, services may be irregular, may charge high prices, etc. The government has to ensure the quality of the products or services at reasonable prices. Public is to be assured of regular and adequate supply of services and goods without discrimination. Therefore, it is essential to regulate their working as well as the price and supply policies of public utilities. Regulatory powers of the government in respect of these undertakings are provided in Special Acts of the legislature.

5) Franchise: Public utilities operate under franchise i.e. the right to interfere with public property (land, buildings, roads, etc.) for proper functioning. For example, the railways which is a public utility undertaking, can put up barriers on roads restricting movement of traffic across railway track at level crossings. Similarly, water supply undertakings can dig pits across the roads whiIe laying water pipes, and so on. The government grants special rights as well as casts duties and responsibilities on these concerns through a charter which is called franchise. The franchise or charter contains the powers, privileges and rights granted to these undertakings as well as duties and liabilities for which these undertakings are accountable. This is done to ensure their working efficiently and satisfactorily. The franchise can be withdrawn if the undertaking does not comply with the regulations and resttictions subject to which the franchise is issued.

6) Huge capital investment: These undertakings require huge capital investment in fixed assets. Take the case of Mother Dairy which supplies milk in Delhi. For supply of milk . to its consumers it has to set up a milk plant, storage plant, and large fleet of vans1 tankers. It has also to construct depots for distribution of milk at various places in different localities of Delhi. Then, it has to monitor the distribution of milk to its consumers properly. Thus, all the public utilities invest huge amount of capital in fixed assets.

7) Risk involved: The degree of risk involved in the business carried out by the public utilities is less as compared with other industries. This is because the demand for essential goods and services is not likely to fall, rather it is likely to increase over time. For instance, the demand for water, gas, milk, electricity, etc., is not likely to fall but increase since the population is increasing continuously year after year.

8) Non-transferable demand by the consumer: The demand of the consumer is nontransferable. If a consumer is provided electricity at his house, he cannot transfer his right of using electricity to his neighbour. Every consumer is to obtain the supply separately after fulfilling the rules and regulations of the undertakings.

9) Choice of site: The promoters of public utilities do not have much choice in the selection of site for the undertaking. They have to locate their enterprise as per the permission granted to them by the concerned authorities. They have to operate as per . the prescribed local conditions and regulations.

10) Size of the undertaking: These undertakings are required to be set up on a sufficiently large scale so as to meet the demand of the public of that locality. Moreover, the size of the unit must be large enough to make it possible for the undertakings to supply the service continuously at economical rates.

(d) Underwriting

Ans: Development banks and financial institutions underwrite the issue of shares and debentures of public limited companies. Investment trusts, stock-brokers. issue houses and other similar organisations also underwrite the public issue of shares and debentures. Those who underwrite security issues are known as Underwriters. Underwriting refers to an agreement between the promoters or directors of a company on one hand, and an individual, firm or institution (known as underwriter) on the other, whereby the latter agrees to take up the whole or part of the shares or debentures issued which may not be subscribed by the public. In consideration of the undertaking given by the underwriter, the company agrees to pay a commission which is known as 'underwriting commission'. Underwriting commission is generally a percentage of the issue price of the shares or debentures underwritten.

There is a written agreement between the company and the underwriter known as the 'Underwriting Agreement' (or Contract). A contract generally contains the following:

i) The number of shares or debentures which are agreed to be underwritten.

ii)An undertaking by the underwriters to take up such of the shares or debentures as are not subscribed by the public.

iii) An undertaking by the company that the terms of issue given in the prospectus will not be changed without the consent of underwriters.

iv) The rate of commission to be paid to the underwriters and the mode of payment.

v)Authority of the underwriters to the company to allot them the balance of shares or debentures not taken up by the public.

The most important advantage of underwriting, to the promoters is that the funds required for the enterprise become available whether or not there is adequate public response to the issue of shares and debentures. Another advantage of underwriting is that the company gets the benefit of expert advice from the underwriters. The only disadvantage of underwriting is that it adds to the cost of raising finance. Any individual, partnership firm, company or financial institution may become an underwriter. They may be regarded as underwriting agencies or institutions. In India, the development banks, commercial banks, investment companies, investment trusts and stock brokers (share brokers) engage in underwriting business. Some of the well-known underwriting agencies in India are IFCI,IDBI,LIC,UTI,State Bank of India, Bank of Baroda etc...

PART-B

Attempt any three of the following questions :

3. Discuss the role of entrepreneur in business promotion. Outline the basic characteristics of an entrepreneur. 6+4

Ans: Role of an entrepreneur in business promotion:

1)Develops an idea and explores opportunities: The idea of forming n business unit is first formed in the creative mind of the entrepreneur. On the basis of the idea, he perceives opportunities for profitable investments and explores the prospects of starting a manufacturing enterprise.

2)Product analysis and market survey: He collects data on consumer preferences and needs through market research techniques and to find out the sale-ability of the proposed product. Further, he collects consumer preferences in respect of design, colour, size and shape. In addition, the entrepreneur gathers the total demand and the degree of competition for the proposed product.

3)Decides form of organisation: He decides the form of business ownership, i.e., whether it should be a sole proprietorship, a partnership firm, a company or a cooperative society.

4) Decides location: He decides location of the factory at a suitable place taking into account the available facilities of transport, power-supply, fuel, water, labour, supply of raw-materials, nearness of market, etc.

5) Collects necessary capital: He makes available sufficient amount of capital for the initiation and continuation of the business. He gives personal guarantees to the financiers who contribute capital. Otherwise, he promises to invest capital himself or arrange the necessary amounts from friends and relatives. In case of small enterprises, the promoters can provide funds from their own savings. But in case of large enterprises, funds have to be raised from various sources like general public, commercial banks, financial institutions, etc.

6)Places orders for machinery: He places orders for machinery, equipments and other requirements. He takes decision about the installation of equipment and machinery in the process of production.

7) Recruitment of labour: As an entrepreneur he makes an estimate of skilled and unskilled workers of different categories required for various departments. Accordingly, the entrepreneur arranges their recruitment.

8) Designs internal organisation structure: He designs internal organisation structure for his proposed concern. This involves breaking up of the total work of the enterprise into major functions like production, marketing, finance, personnel, purchase, engineering, etc. and the dividing of each of them into sections. He stipulates the functions of different departments and their inter-relationships.

9) Fulfils formalities and launches enterprise: Every type of business has some procedural formalities while starting a new enterprise. The formalities are different for different types of business organisations. Unless you fulfil them, you cannot simply launch an enterprise.

Characteristics of an Entrepreneur are:

i. Independence: Many entrepreneurs who started their businesses resisted being pigeonholed or following routine habits. In fact, entrepreneurs become frustrated when they have to follow someone else's direction. They have to be the boss. They like to be in control. They find it difficult to work under the direction of others.

ii. Hard Work: Willingness to work-and work hard-is an outstanding trait of entrepreneurs. A successful entrepreneur described his early experiences that they worked endless, twelve hour days and sometimes seven days a week.

iii. Desire-to Achieve Goals: They have a strong desire to overcome problems and setting up successful business ventures which eventually give adequate profits. They considered profit as measure of their achievement and performance rather than making money alone.

iv. Foresight arid Dynamic Outlook: Basically, these people have wide knowledge about business environment i.e., market, consumer attitude, technological development, etc. Further, they ore dynamic in forecasting business uncertainties and risks, accordingly, they take quick and sound decisions.

v. Open-mindedness: They are intelligent in predicting changes in business environment. However, they never resist changes because they know that they cannot stop it. Therefore, they are habituated to open-mindedness even though sometimes they lose crores of' rupees due to changes in consumer tastes which ultimately forced them to change their technology, etc.

vi. Optimistic Outlook: They are generally inclined to believe that present problems are of it temporary nature and conditions will be more favourable in due course. Entrepreneurs are always eager to achieve their goals in the best possible manner, to get outstanding results which they can be proud of.

vii. Working Relationship : The success of a business mostly depends upon its workers first rind then their links with other business undertakings. Most of the successful business entrepreneurs have had harmonious relationships with others. This builds up their reputation in the market.

viii. Good Organisers : They are good at bringing together different types of resources needed for starting a business and making it operationally efficient. They can convince people about the prospects of business, get their cooperation, raise funds, procure machinery, arrange supply of materials, select right type of employees and coordinate various activities relating to the business.

ix. Innovative Aptitude: Most of the successful entrepreneurs have innovative aptitude. They spend part of their income on research and innovative activities so that they offer suitable products to meet the demands of consumers. Some of our industrialists like Tata, Birla, Kirloskar, etc. have established their own research centres.

4. State the various methods of raising long term funds for a business organization and explain the merits and demerits of any one of these methods. 3, 4, 3

Ans: Long-term finance may be raised by companies from, one or more of the following sources:

i) Capital market which consists of individual investors, financial institutions and investment companies
ii) Special financial institutions consisting of development banks and institutional ' investors.'

iii)Leasing companies

iv)Foreign sources

v)Retained profits

Merits of Retained Profits:

i. Increased stock value: Amongst the many advantages of retained profits is increased stock value. as retained profits are a part of the corporate balance sheet, it raises your company’s total balance sheet. This is an advantageous effect that the stockholder equity has, which in turn presents an impressive image of your enterprise, ultimately attracting more investment.

ii. Retained earnings are an easy source of financing : Market conditions and business profitability are highly volatile, which means that they can change course anytime. Hence, when your business keeps its retained profits, it builds a safety net by providing liquidity for low revenue situations. During any emergency condition, your business would have funds to keep operations on and make basic payments.
iii. Funding for growth: The advantages of retained profit also stretch towards supporting the growth of the business. Reserving the company's profits allows your company the space to do more developmental activities and research. The retained profits can be invested into elements or assets that drive growth. These profits can be carried on, and the reserve can be increased by it for future investments.

Demerits of retained profits:

I. Chances of holding the retained earnings

Though retained profits can be a good thing for the business, if these retained profits do not create more money or do not bring in extra benefits, the stakeholders might ask for more dividends. Along with this, the directors of the company have the power to restrict the value of the dividend, and they might set it too high, which would again mean that the business would be left with very minimum retained profits. Hence, chances of holding on to the retained profits are slim and have to be wisely thought out.

II .Improper utilization of funds

Retained profits can be a great source of financing without taking on any liability. However, this plan can only be successful when the profits are used according to a plan where all the expenses and investments that would be made are clearly mentioned with the expected impacts. Retained profits ultimately are the extra money the business earned. So, in the absence of a well-strategized plan, these earnings can be misused very easily. Overspending on unnecessary supplies and investing just for the sake of locking the money but not getting any returns gives departments and projects budget raises without any major need.

III. Over-capitalization

Disadvantages of retained profits include over-capitalization. Over-capitalization is a term that refers to a business state where the assets of the company are lesser in value in comparison to its capital.

5. "Advertisement is a waste". Comment on this statement. 10

Ans: Though advertising is one of the most frequently used medium of promotion of goods and services, it attracts lot of criticism. The opponents of advertising say that the expenditure on advertising is a social waste as it adds to the cost, multiplies the needs of people and undermines social values. The proponents, however, argue that advertising is very useful as it increases the reach, brings the pay unit cost of production down and adds to the growth of the economy. It is therefore, important to examine the major criticisms against advertising and see the extent to which these are true. This is taken up as follows:

1. Adds to Cost: The opponents of advertising argue that advertising unnecessarily adds to the cost of product, which is ultimately passed on to the buyers in the form of high prices. An advertisement on TV,

for a few seconds, for example, costs the marketers several lakhs of rupees. Similarly, an advertisement in print media say in a newspaper or a magazine costs the marketers a large amount of money. The money spent adds to the cost, which is an important factor in fixation of the price of a product. True, advertisement of a product costs lot of money but it helps to increase the demand for the product as large number of potential buyers come to know about the availability of the products, its features etc. and are persuaded to buy it. The increased demand leads to higher production, which brings with it the economies of scale. As a result, the per unit cost of production comes down as the total cost is divided by larger number of units. Thus, the expenditure on advertisement adds to the total cost but the per unit cost comes down which in fact lessens the burden of consumers rather than adding to it.

2. Undermines Social Values: Another important criticism of advertising is that it undermines social values and promotes materialism. It breeds discontent among people as they come to know about new products and feel dissatisfied with their present state of affairs. Some advertisements show new life styles, which don't find social approval. This criticism is not entirely true. Advertisement in fact helps buyers by informing them about the new products, which may be improvement over the existing products. If the buyers are not informed about these products, they may be using inefficient products. Further, the job of an advertisement is to inform. The final choice to buy or not to buy anyway rests with the buyers. They will buy if the advertised product satisfies some of their needs. They may be motivated to work harder to be able to purchase these products.

3. Confuses the Buyers: Another criticism against advertisement is that so many products are being advertised which makes similar claims that the buyer gets confused as to which one is true and which one should be relied upon. For example, we may note similar claims of whiteness or stain removing abilities in competing brands of detergent powder or claims of whiteness of tooth or 'feelings of freshness' in competing brands of toothpaste that it is sometimes confusing to us as to which one to buy. The supporters of advertisement, however, argue that we are all rational human beings who make our decisions for purchase of products on factors such as price, style, size, etc. Thus, the buyers can clear their confusion by analysing the information provided on the advertisements and other sources before taking a decision to purchase a product. However, this criticism cannot be completely overruled.

4. Encourages Sale of Inferior Products: Advertising does not distinguish between superior and inferior products and persuades people to purchase even the inferior products. In fact, superiority and inferiority depends on the quality, which is a relative concept. The desired level of quality will depend on the economic status and preferences of the target customers. Advertisements sell products of a given quality and the buyers will buy if it suits their requirements. No advertisement should however, make false claim about the quality of a product. If a firm makes a false claims it can be prosecuted for the same.

5. Some Advertisements are in Bad Taste: Another criticism against advertising is that some advertisements are in bad taste. These show something which in not approved by some people say advertisements showing women dancing when not required or running after a man because he is wearing a particular suit or using a particular perfume are certainly not good. Some advertisements distort the relationship like employer employee and are quite offensive.

6.Advertising leads to monopoly: Small competitors find it difficult to enter the market due to advertising. This is because large firms create hurdles in their way.

7.Advertising causes undesirable social effects: Certain social effects can be. there due to advertising like it influences the materialistic values and life styles of people in society, certain sex and, horror appeals are used in order to draw the consumers attention, it creates frustration and disappointment when a person cannot purchase and enjoy a particular product.

8. Advertising results in inefficient resource allocation: Advertisements are intended not so much for the benefit of consumers. They are mainly directed to influence the consumer demand to fit whatever has been produced. In other words, advertisements are aimed mainly to change the tastes of people so that they will buy whatever is manufactured. This leads to distortion in consumption expenditure and increases the producers market power. Thus, advertising indirectly determines what people should consume. In this process productive resources i.e., land, labour and capital, may not be used in the best interest of the society.

9. Advertising may act against the freedom of press: Mass media earn huge income from advertisements. If the media are dependent on income from advertisements sponsored by few large business firms, it may be difficult to disseminate information in public interest when it is unfavourable to those big business firms. Big sponsoring firms can threaten the media owners by refusing their advertisements and dictate what media have to do. Thus, the financial dependence of media on advertisements may act against the freedom of press.

6. Discuss the factors influencing the choice of channels of distribution. 10

Ans: The following factors generally influence the choice of the channel of distribution:

1) Distribution policy

2)Characteristics of the product

3) The target customers in view

4)Supply characteristics

5)Types of middlemen in the field

6) Channel competition

7) Potential volume of sales

8) Costs of distribution

9) Profits expected in the long-run

1)Distribution policy: Where the manufacturer is interested in distributing his products through all possible outlets, it is desirable to use more than one channel to reach the target customers. This is known as intensive distribution policy. The purpose in this case is to make the product available as near to the consumers as possible. Consumer goods of frequent use like pens, pencils, paper, soap, hair nil, etc., are distributed through a large number of wholesalers and retail traders. If goods are meant for customers who are very particular about their quality and usefulness, manufacturers adopt a selective distribution policy.

2)Characteristics of the product: The nature of the product influences the choice of channel. For example, perishable products like eggs, milk, etc., are supplied either directly or through the short channels. In the case of heavy and bulky products (e.g., cement, steel) where distribution and handling costs are higher, short channels are preferred. Sophisticated electrical and electronics equipment which require careful handling are also generally distributed directly or through short channels. On the other hand, long channels are found in the case of light-weight and small-size items like dress material, readymade garments, pocket calculators, stationery, toothpaste, toothbrush, etc. Similarly, simple mechanical products like electronic toys, time-clocks, etc., are supplied through long channels for intensive distribution.

3)Characteristics of target customers; If the number of customers is large and geographical area is extensive, long and multiple channels are necessary for intensive distribution of goods. This is also suitable where the consumers are in the habit of making frequent purchases of small quantities at irregular intervals. Short channels and direct selling are possible in the case of few customers who purchase large quantities at regular intervals and they are concentrated in a small area.

4)Supply characteristics: Goods produced by a small number of producers concentrated in one region are generally distributed through short channels. Long channels are suitable if a large number of producers in different regions produce and supply the goods.

5)Types of middlemen: Availability of suitable middlemen in the channel of distribution is another factor in the selection of the channel. This is because different functions like standardisation, grading, packing, branding, storage, after sale servicing, etc., are expected to be performed by middlemen. Efficiency of distribution depends upon the size, location and financial position of middlemen. If the middlemen in a specific channel are dependable and efficient that channel may be preferred by producers.

6)Channel competition: There are different situations in which manufacturers compete with each other for availing the services of particular wholesalers. Similarly, wholesalers often compete with each other to deal with particular retailers or carrying particular brands of products. Sometimes producers use the same channel which is used by their competing producers. If any producer arranges exclusive distribution through a particular wholesaler, other producers also do the same. Thus, selection of a channel may depend on the competition prevailing in the distribution system.

7)Potential volume of sales: The choice of the channel depends upon the target volume of business. The ability to reach target customers and the volume of sales varies between different channels. One outlet may not be adequate for achieving the target in which case more channels need to be used. Of course, the competitive situation must be taken into account while examining the potential volume of sale through different channels.

8)Cost of distribution: The various functions carried out in the channel of distribution add to the cost of distribution. While choosing a channel, the distribution costs of each channel should be calculated and its impact on the consumer price should be analysed. A channel which is less expensive is normally preferred. Sometimes, a channel which is convenient to the customers is preferred even if it is more expensive. In such cases the choice is based on the convenience of the customers rather than the cost of distribution.

9)Long-run effect on profit: Direct distribution, short channels, and long channels have different implications with regard to the profits in the short-run and long-run. If demand for a product is high, reaching the maximum number of customers through more than one channel may be profitable. But the demand may decline in course of time if competing products appear in the market. It may not be economical then to use long channels. So, while choosing a channel one should keep in mind the future market implications as well.

7. Define business risk. What are the various types of business risks ? How do you manage them ? 2+4+4

Ans: The term is used to refer to (a) an insured object such as a home or a car, (b) a peril such as fire or earthquake, (c) the probability of an event which may cause loss, (d) the loss itself, (e) the hazardous condition, (f) the variation in the outcome that could such as fire or earthquake, (c) the probability of an event which may cause loss, (d) the loss itself, (e) the hazardous condition, (f) the variation in the outcome that could occur over a specified period in a given situation, etc. 'Business risk' may be defined as the uncertainty of occurrence of economic loss in the event of any business activity.

Types of business risk:

Pure and Speculative risks

The occurance of perils like fuel windstorm, explosion, flood, earthquake, riot, etc., generally cause losses only. Their occurance never result into gains. The uncertainty concerning their occurance may be termed as pure risks. Thus, Pure risks are those risks in which tlie occurance of events causes losses only. For instance, car drivers always face the risk of accidents. If an accidence occurs, the driver may suffer physical and financial losses. If the accident did not occur, there would not be any gain. Thus, in the case of a pure risk, there is loss when it occurs, otherwise , there is no loss or gain. On the other hand speculative risks involve events which may produce either gains or losses. For instance, expansion of operations in a new market (area] may lead to higher profits or loss of invested funds. Most business decisions relating marketing, production, finance, etc., are taken with the idea of making gains, but there are possibilities of incurring losses also. Thus, all business enterprises face both pure risks as well as speculative risks. Many pure risks can be handled through insurance, while most of the speculative risks are not generally handled through insurance. So business enterprises must find their own ways of handling specualtive risks.

Static and Dynamic Risks

Risks can also be classified as dynamic risks and static risks. Dynamic risks are related to uncertainties caused by an ever-changing business environmental factors such as consumer wants, technology, competition, governmental policies, firms internal organisation, etc. On the other hand static risks are those which occur even if there are no changes in the business environment. Normally static risks are closely related to pure risks such as fire, flood, windstorm, etc., whereas dynamic risks are more closely associated with speculative risks. Most of the static risks can be handled through insurance while most of the dynamic risks may not be handled by insurance.

Risk Classified by Loss Severity

Risks may also be classified as follows into three groups on the basis of the extent of loss and its importance on the financial position of the business firm:

Class 1: Those losses which do not disturb a firms basic finances.

Class 2: Those losses which would require borrowing or selling firms property.

Class 3: Those losses which might bankrupt the firm. Class 1 risks cause small losses, Class 2 risks cause much bigger losses, and the firm may not survive with the occurrence of Class 3 risks. Therefore, Class 1 and 2 risks can be handled by various internal methods but Class 3 risks are beyond internal capabilities of the business firms.

Objective and Subjective Risks

Objective risk is the measure of the degree of variation in the proportion of actual from the expected events. This proportion declines at the number of observed events increase. Hence, the objective risk as a proportion declines when larger and larger number of events are involved. Subjective risk may be defined as the uncertainty of an event as seen or perceived by an individual. This perception depends on the attitudes of the concern individuals towards risk. Among people, there are 'risk lovers' who prefer a situation with a great deal of uncertainty, and also 'risk haters' or 'risk averters' who do not like to face risks.

Risk management involves five basic steps:

i) Risk identification is the first step and also the most difficult function. Failure to identify all the loss exposers of the firm means you will not be in a position to deal with those risks.

ii) After identifying the risks, next step is to assess the intensity of financial loss associated with each of those risks. We have to determine two aspects: I) probability of the occurrence of each of the perils or risk identified in the first stage, and II) extent of financial loss to the firm, if that peril occur. With this assessment, we can identify the relatively more serious risks and pay more attention to them.

iii) Third step is to decide on various tools of risk management and decide upon the best combination of the tools to be used. There are six tools for risk management :

I)assumption(or retension)

II) loss prevention

III)avoidance

IV)transfer(insurance)

V)separation

VI)combination

I) Risk assumption or retention: This is a common way of handling risks. Business enterprises assume or retain risks consciously (intentionally) or unconsciously (unintentionally). Under conscious assumption, one is aware of the risk to which his/her business is exposed, but essentially does nothing to avoid I I it. A manager of a business who consciously assumes risk is doing something about it by the very act of being aware of those perils and hazards which may cause oss. Being aware of risk, he may knowingly or unknowingly make adjustments in operations which will help to alleviate the impact of that risk. Awareness of risk itself is a significant achievement in better management. In the case of unconscious risk assumption, risk is not recognised. As you are not even aware of the existence of some risk, losses stemming from it can cause disastrous surprises to your business.

II) Loss Prevention: Another method of handling risk is to take appropriate measures to prevent the occurrence of a peril or minimise its financial impact on business. This approach is known as loss prevention. For example, by using fire resistant building material, you can prevent the occurrence of fire in the building. Loss prevention may not totally eliminate the risk, but can reduce its probability in terms of frequency as well as severity.

III) Avoidance: Avoiding situations which have the potential to cause loss, is another approach. For instance, a firm can avoid the risk of loss due to bad debts by simply stopping credit sales.

IV) Transfer: Transferring the risk to another party is a very widely followed approach to handle risks. Insurance is the most common method of transferring pure risks such as fire, windstorm, flood, riot, theft, etc. Business enterprises normally transfer the pure risks to the insurance company and devote their full efforts to their normal business.

V) Separation: Fifth method of risk control is separation of the firm's exposers to loss instead of concentrating them at one location where all of them might be involved in the same loss.

VI) For example, when a firm keeps its entire raw material in one warehouse, the entire raw material may be damaged if fire occur in that warehouse. Therefore, the firm may decide to store the raw material in ten separate warehouses. If fire occur in one warehouse, materials stored in that warehouse are damaged and the remaining nine warehouses are safe. This methods is also a kind of loss prevention.

VII) Combination: Strategies like diversification of products, law of large numbers, formation of more companies with unrelated lines of business, etc., come under this method. For example, if a firm is engaged in more products, the losses incurred in one product may be upset by the gains in another product. Similarly, if there are more companies, the losses incurred by one company may be upset by the gains by the other companies. Insurance companies work on this combination principle where a sufficiently large number of similar objects are combined to make the loss predictable within narrow limits.

While managing risks, one need not just rely on any one method, instead may rely on some combination of various methods.

iv)After taking a decision regarding the combination of risk management tools, the next step is the implementation of the decision made. For instance, if you have decided in the previous stage to transfer the risk, you have to get the insurance policy at this stage.

v) Last step is to evaluate the effectiveness of the risk management tools we have implemented. The result of the decisions made in the four stages must be evaluated to determine their effectiveness and change the strategy, if required.

8. (a) Explain the characteristics of a government company. (5)

Ans: According to the Indian Companies Act. a government company is a company in which 51 per cent or more of the total paid-up capital is held by the central government or any state government 01. by many state governments or partly central government and partly by one or more state governments. Any company which is subsidiary of such a company is also considered a government company. Thus a government company is an enterprise wherein government is a predominant shareholder having the bulk of controlling interests, Government company is registered under Indian Companies Act. k of controlling interests, Government company is registered under Indian Companies Act. When the government applied to the Registrar of Joint Stock Companies for setting up a new company, it has to follow all the rules and procedures as are applicable to private persons.

Characteristics of a Government company are:

i) Created under Indian Companies Act : Government company is a corporate body created under the Indian Companies Act, 1956, like any other joint stock company in the private sector. With regard to registration, memorandum, articles, meetings, capital structure, accounts, audit, etc., it is governed by the provisions of the Companies Act. But the government has the authority to exclude or modify certain provisions of the Companies Act by special notifications duly approved by the legislature.

ii) It is a corporate body: A government company is a legal entity. It is an 'artificial person' which exists in the eyes of law. Like a living being it can file a suit in a court of law br be sued, can enter into contract and acquire property in its own name.

iii) Scope for private participation in the capital : A government company may be , wholly or partly owned by the government. In any case, the share of the government is not less than 51%. In case it is partly owned by the government, the private persons (individuals as well as corporate bodies) can also participate in the capital. Thus, there is scope for the private sector to participate in the capital.

iv) Managed by a Board of Directors : It is managed by the Board of Directors. All the directors or the majority of them, depending on the extent of private participation, are appointed by the government. While constituting the Board the government may give representation to various interests like technocrats, labor, consumers, foreign . collaborators, etc.

v) Enjoys financial independence : Government company can use and reuse the revenue derived from [he sale of its goods and services. If necessary, it can borrow money from the financial institutions and the general public.

vi) Independent staffing : Its employees are not civil servants. They are appointed by the company on its own terms and conditions. It regulates its personnel policies according to its Articles of Association.

vii) Independent accounting and auditing system : It is exempted from the accounting and audit laws and procedures applicable to government departments. Its accounting practices are more akin to those of commercial enterprises and its auditors are chartered accountants appointed by the government on the advice of the CAG.

viii) Annual reports : Its annual reports and accounts along with the audit reports are to be presented to the legislature, as per the Companies Act.

(b) Why is government's direct participation in business considered necessary ?

Ans: The government controls the private enterprises on one hand and directly participate in the business on the other. Government today is engaged in various types of business undertakings. There are several types of services which are provided by government organisations such as electricity, water, postal, telecommunications, transport services, ztc. Besides these organisations, there are many manufacturing industries owned and inanaged by govcmment. They produce steel, locomotives, machine tools, watches, railway coaches. telephone equipment, and so on. Government undertakings are also involved in the supply of consumer goods like milk (through government milk schemes), bread (Modem Bakeries), cloth (National Textile Corporation), etc.

The reasons for the direct participation of government in business and industry may be divided into three categories:

i) basic reasons

ii) ideological reasons

iii) specific reasons.

i) Basic reasons: The government of India was rightly convinced that political independence without economic independence would not have much meaning. It was, therefore, decided to industrialise the country in a big way as early as possible.

The government felt that if the private sector was to take the initiative. it would take an unduly long time to achieve this objective of rapid industrialisation. It was so because the private enterprises lacked adequate entrepreneurship and resources to start large scale ventures.

The government encouraged private enterprises to set up new industries, but also, went into industry in a big way.

It was decided to establish steel plants. fertilizer factories and other units necessary for industrial and agricultural growth. The following is a list of some major enterprises and power projects set up by the government within a decade of Independence- Steel Plants at Rourkela, Bhilai and Durgapur, Indian Telephone Industries.

The intention of the government was to have economic self-reliance in as many areas and as early as possible.

ii) Ideological reasons: Apart from the economic and social consideration, the government had strong ideological commitment to the philosophy of public ownership of the means of production.

iii) Specific reasons: There are many other reasons for the government to participate in business. These are specific to a particular decision. Some of these are listed below.

* Air Transport Business: Till 1953, there were many private air companies in the country. Most of these were financially unsound and had no money to invest in modem and costly aeroplanes, The air transport is of strategic importance to the country. The government, therefore, nationalised nine air companies and created Indian Airlines Corporation and Air India International Corporation in 1953.

* Insurance Business: Today, the whole of insurance business is with the government. The life insurance business is operated through the Life Insurance Corporation of India and other types of insurance business through the General Insurance Corporation of India and its four subsidiary companies.

The government went into the life insurance business in 1956 nationalising scores of private companies which were not fulfilling the main objective of the life insurance business, namely, i) effective mobilisation of the people's savings, ii) spreading the message of insurance as far and as wide as possible, and iii) using the insurance funds for economic development.

* Commercial Banks: The government today is in the banking business in a big way. Over 90% of commercial banking is in the hands of the government. The government rightly wanted the banking system to serve the developmental needs of the economy in conformity with national policy and objectives. It also wanted the banks to have new criteria for advancing loans in order to benefit the weaker sections of the society.

* Coal Industry: The coking coal mines were nationalised in 1971. It was done because coking coal which is essential for production of iron and steel has very limited reserves in the country. The private sector was mining this fast depleting and scarce natural resources in a very wasteful manner. Other coal mines were also nationalised in 1973. The reasons for this were: i) the private sector owners did not have the necessary funds required for increasing the coal production, ii) the coal which is a scarce natural resource was being mined in a very unscientific way, and iii) the private coal miners were greatly exploiting the labour employed in the mines.

* Oil Industry: In the 1970's the foreign oil companies Burmah Shell, Caltex and Esso were nationalised. Here the objective was that the government should have control over a critical and strategically important resource like oil.

* Various Other Types of Business: There is yet another important reason for the government going into business of various types. Over one hundred cotton textile mills and dozens of engineering and other enterprises have been taken over by the government since Independence. This is done because the government cannot afford to lose production capacity which exists in the units which become sick and which the private sector wants to close down.

From the above, we can conclude the reasons for participation of Government as:

i) The government's role in business in India is greatly justified by economic and social reasons.

ii) Had the government not initiated a large number of industrial activities, the Indian economy would never have got the sound base and self-reliance which it has today.

iii) A large number of enterprises have been forced on the government when they became sick and they could not be allowed to be closed down due to social and economic reasons.

iv) There is an element of ideology in the role which the government has in business today. Had the ideology not been there, the government would have disengaged itself from at least some of its business activities after completing its role as path finder or initiator.

v) The government continues to be in business in a big way because of ideological as well as economic and social considerations.