Business Theory and Practice

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1.1 Meaning of business

We use the term 'business' to convey different meanings when we use it in different circumstances or contexts. When we think of 'businesses' in a generalized way, we are, in effect, really referring to 'commercial activity.' This activity is primarily concerned with the operations involved in getting 'products':

- **From** the people/entities that produce or make or provide those products,
- **To** the people/entities that need – and will pay for – those products.

1.1.1 Business objectives

Objectives are 'goals' which an enterprise aims to achieve. Before any enterprise is started, a person or a group of people has to decide what that enterprise is going to do. For example:

- Is it going to manufacture something?
- Is it going to buy and sell?
- Is it going to provide a service?

1.1.2 Profit motive

In the private sector the specific objectives of a business are combined with the objective of making 'profit.' The goal is that the business gets a 'return on capital' in the form of profit.

1.2 Basic policies of business

After the objectives of a business have been decided it is necessary to decide in broad terms 'how' and 'where' those objectives are to be achieved. This involves laying down the basic 'policies' of the business.

1.2.1 Attitude towards objectives

Policies are really the 'attitudes' of the management of an enterprise towards achieving its set objectives. Policies, therefore, need to be 'flexible,' to be adjusted or adapted to deal with prevailing circumstances and trading conditions, with problems which might arise in attaining the objectives, or as required by the operating position of the enterprise at a particular time. Any modifications of objectives and adjustments to policy are made by the owner(s) or partners of a business, or by the board of directors if it is a company.

1.3 Planning

Planning entails deciding how the pre-determined 'objectives' of a business should be achieved in the most efficient and economical way in accordance with policy. Planning is the activity concerned with making plans. Plans are really 'routes to objectives.' Once the objectives of an enterprise have been set, planning is necessary to work out how to achieve the objectives in practice, within the framework of the policies formulated.

1.3.1 Types of planning

Planning can be broadly categorized into the following:

- **Strategic planning:** In business, top management is involved mainly with 'long-term planning' which is often called 'strategic planning.' It is concerned primarily with deciding what the objectives of the business should be in two, five, or even ten years ahead, and with the future policies of the business. Such planning is concerned mainly with the enterprise as a whole rather than with its individual departments or section.
- **Tactical planning:** This means planning how the overall strategies are to be achieved. This often entails devising and operating short-term plans, for up to a year ahead.
- **Activities or operational planning:** Other levels of management, including supervisors and foremen, are involved mainly in very short-term 'activity planning' – which is sometimes called 'operational planning.' This includes planning the day-to-day running of departments or sections and individual assignments; for example, how to meet a particular month's production quota, or deciding what each member of staff should be doing at any given time.

In practice, much depends on the size and type of a particular business, and the size of its management team. However, in general, a good deal of planning which managers are called upon to do involves making routine decisions, and is concerned with everyday matters – for example, planning the work of a team of showroom sales personnel – which will mostly be similar work week after week.

1.3.2 Flexibility in planning

Plans must be flexible so that they can quickly and easily be modified in the light of changing circumstances. For example, a business manager might have decided how his/her staff will cope while another member is on holiday, and has planned the rearrangement of the work. But the day after the implementation of the new plan, another member of staff falls ill – so he/she must modify his/her plan, and determine how the work can be rescheduled with two staff away. Much of routine planning is an automatic process, requiring little conscious thought on the part of the manager, because his/her plans and decisions will be based largely on past experience with similar – or even with identical – problems. Other planning, of perhaps a business trip or a training course, for example, might require far more conscious thought, investigation and research before decisions are reached.

1.4 Forecasting

Planning is concerned primarily with activities in the future. There has to be some guidance as to what might occur in the future. What is called forecasting is, therefore, essential if management is to be able to carry out effectively its planning function.

To forecast is to determine – as accurately as possible – the probable course of future events which might affect the enterprise and its activities. A forecast, then, is an assessment of the expected pattern of future events and the ways in which it might have effects on the operations of the enterprise or sections of it.

1.4.1 Determining the course of future events

It is not possible to anticipate or foresee the future exactly, but the more accurate the forecasting the lower will be the degree of uncertainty and the greater the possibilities of formulating reliable plans – and, in consequence, the greater will be the chances of achieving the objectives. Forecasting is, therefore, an essential accompaniment of planning. Based on the forecast, plans can be formulated to deal successfully with expected future events, and to take steps to deal with any problems which are anticipated and may arise in the future, or to avoid them before they arise.

No one can predict the state of the economy, or the possible situation of an enterprise, in ten years' time with any great degree of certainty, but the best attempt possible must be made, and many different methods can be used, depending on circumstances.

The accuracy of forecasts will frequently be influenced by certain considerations such as the extent of 'unknown' factors as opposed to those factors which can easily be predicted because they are based on past performance, accounting records or statements, experience or published information.

Also, it cannot always be assumed that 'known' factors will remain constant; for instance, future sales of a product might not be the same as past sales of it because external influences (some of which might not be predictable) might increase or decrease sales.

It is, of course, vital that the data on which forecasts are made are as accurate or valid and up to date as possible. In addition, the forecast must be clear to those who will use it on which to base plans, so that they will use it, and the information in the forecast must be relevant to the planning to be undertaken.

1.4.2 Relationship between planning and forecasting

Forecasting should be a continuous process, and forecasts should be available at regular intervals: monthly, quarterly, six-monthly or yearly, as circumstances require. This enables those members of management involved in planning to compare the latest forecasts with those on which their original plans were based, and allows them to determine whether any modifications to their plans need to be made in view of changed circumstances and in the light of experience.

2 Modern business

Various types of enterprises make up the modern, complex world of business, and which are established to produce raw materials, manufactured goods or provide services of one kind or another.

2.1 Types of enterprises

In most countries there are two distinct types of such enterprises – the public sector and the private sector.

2.1.1 The Public sector

Some organizations are controlled by the government. They make up what is called the 'private sector,' and which are run for the benefit of the population as a whole, e.g. National Health Service or research organizations, or to provide security for the nation and its citizens, like the police force or the armed forces. Some public sector enterprises are set up by the state to provide services which might not have existed previously. Other public sector enterprises might be established to take over, for a variety of reasons, by a process called 'nationalization,' a number of existing similar organizations and to combine them under one 'central authority.'

2.1.2 The Private sector

The enterprises in the 'private' sector are privately owned, either by individuals or by small or large groups of people. They are commonly referred to as 'businesses,' and are run with the aim of making profits for their owners. Some countries provide incentives to encourage their private sector to expand.

2.2 Types of businesses

There are a lot of enterprises which have a variety of objectives. Collectively they make up the modern business world. They can be broadly divided into three main categories.

2.2.1 Industrial enterprises

Enterprises in this category are of different sizes and engage in a wide variety of activities. These activities can be grouped into the following units:

- **Extractive enterprises:** They are involved in various extracting activities such as oil, coal, iron etc, which are sold to other enterprises for use as power or for use in manufacture of various related products. Activities of agriculture, fishing and factory also fall into this category.
- **Processing or refining enterprises:** These enterprises are involved in 'processing' raw materials for use in other products, for example, computer chips.

- **Manufacturing enterprises:** They are engaged in manufacturing finished products by using raw material or semi-finished products. They also manufacture products which are used in a variety of other products such as batteries.
- **Construction enterprises:** They are involved in building or construction activities, for example, contracts for buildings, bridges, roads etc.

2.2.2 Trading enterprises

Trading enterprises are commonly involved in the activities of buying and selling, i.e. distribution of raw materials, components and finished products. They range from small shops to supermarkets and hypermarkets. These are of two types:

- **Wholesalers:** They buy products from manufacturers in large quantities and sell them in small quantities to retailers. They are actually 'middlemen' between manufacturers and retailers.
- **Retailers:** They buy products in small quantities from wholesalers and sell the same in still smaller quantities to their customers. These customers may or may not be the final consumers of the products.

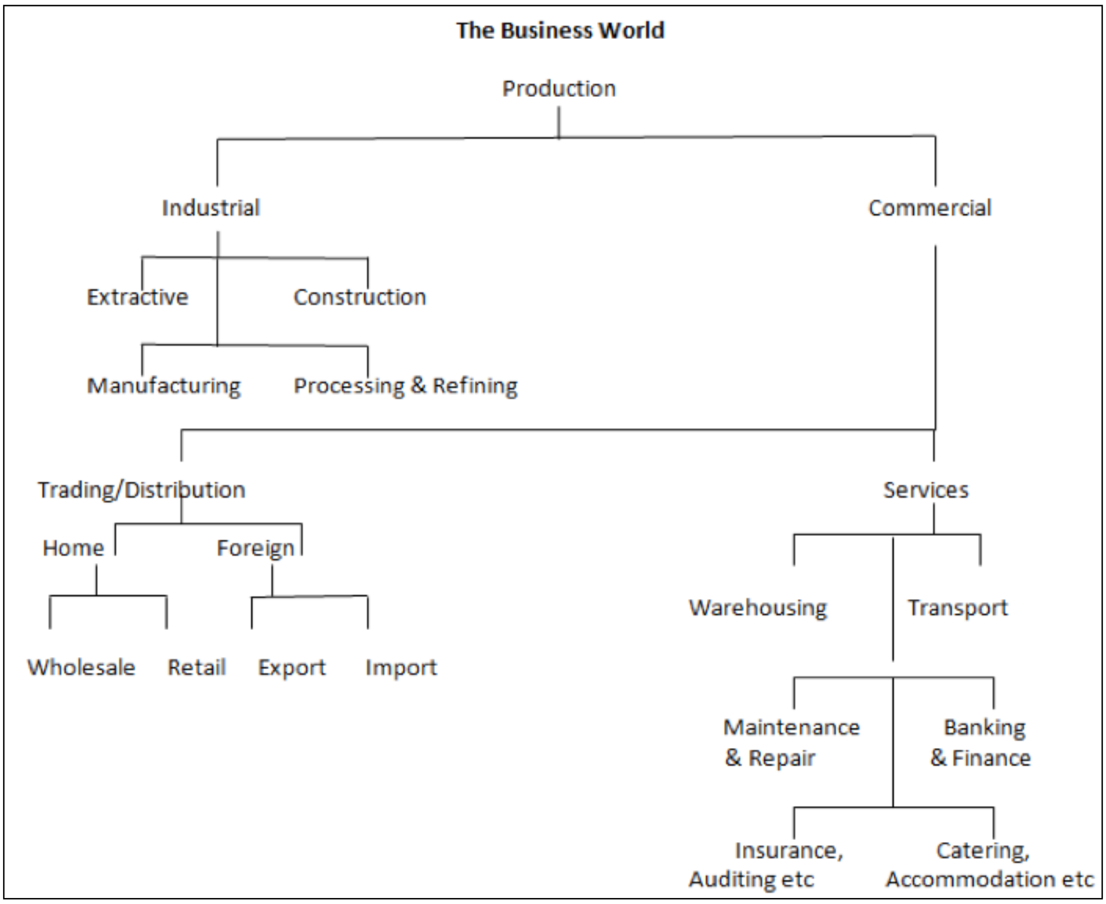
2.2.3 Service enterprises

Services provided by the enterprises involve the performance of some work or activity, the results of which might be seen by the customer. These activities include services provided by enterprises such as banks, financing companies, transport providers, insurance companies, telecommunication companies, travel agents, electricians, tailors etc. Though certain services are provided by others such as lawyers, auditors, architects also, they refer to themselves as 'professionals.'

In addition, some enterprises are multi-activity enterprises, for example, an enterprise may run a factory and sell its products directly through its own outlets. Another enterprise might sell some products and also provide maintenance service, for example, it may sell computers and photocopiers and also provide after-sales service.

2.3 The interdependence of enterprises

All types of enterprises are dependent on each other. Trading enterprises depend on industrial enterprises for the supply of raw material, semi-finished or finished products and the latter depend on the former for buying and selling their products. Both depend on the service enterprises for making their operations possible. If the few categories of enterprises don't exist, there is no place for most of the service enterprises. This interdependence can be clearly seen in the following figure:



2.4 Types of business units

In the private sector there are basically three types of business units: (a) Sole-proprietor or owner; (b) business partnerships; and (c) limited liability companies.

2.4.1 Sole Proprietorship

The most common form of business ownership is the sole proprietorship. The business is owned by one person. It is usually operated by the owner, possibly with the help of family members or a few employees. Sole proprietorship can usually operate with very limited capital resources.

❖ **Advantages:**
- This type of business is easy to set up.
- It is very flexible. The owner has the freedom to run the company as he/she likes.
- The proprietor can offer a personal service.
- He/she can keep all the profit to himself/herself.
- Finances are kept private and accounting requirements are simple – services of an accountant may not be needed.
- The business can be changed to suit local needs.

❖ **Disadvantages:**

- After normal trading hours, there still remains a lot of paperwork to be done, and only one person has to do it. One will need to work long hours to meet tight deadlines.
- It is rather difficult to raise money in order to expand the business.
- If the owner is ill, he/she may have no cover to enable the business to carry on.
- It is risky. The owner is on his/her own, with no one to share the responsibility of running the business. He/she has unlimited liability.

❖ **Examples of Sole Proprietorship:**

- Small shop owner – fruit, vegetables, groceries.
- Furniture shop owner.
- Financial advisor/Travel Agent.
- Plumbing/Electrical services.

2.4.2 Partnership firms

A partnership comprises a group of people working together in business in order to make a profit. A partnership is straightforward to set up – it involves two or more people running a business together. They share control of the business, and own it among them.

Not all partners in a particular partnership firm necessarily work in, or are involved in, the management of the business. Some might provide all or part of the capital and leave the day to day running of the business to the 'working' partners or to non-partner managers; non-working partners are commonly called 'sleeping partners.'

A partnership is also a suitable structure for a small business. Most partnerships have a Partnership Agreement. This sets out matters such as the amount of capital investment contributed by each partner, the sharing of profit (and loss) by the partners, and what to do if there is a dispute. It is a good idea to have Partnership Agreement because if something does go wrong – if there is a dispute – it will set out how the matter can be settled. A Partnership Agreement is not essential, but it does contribute towards the smooth running of a business.

- **Advantages:**
  - More capital is available than in a sole proprietorship business.
  - The workload is usually shared.
  - There are likely to be more skills available – one partner may be a technical expert, another good salesperson, another financial expert, and so on.
  - There is cover for holidays and sickness.

- **Disadvantages:**
  - There is a danger of disagreement among partners. If some of the partners are dishonest or incompetent, the others could be left with large debts and a big mess to clean up.
  - Death, retirement etc of any of the partners threatens to break up the business.
  - All partners have unlimited liability. If the business fails, or if one partner is successfully sued, then all the partners are responsible for all debts. In addition, if one partner fails to pay income tax, for example, the other partners may have to pay it for him/her as well as their own. (It depends on the relevant laws and regulations applicable in a particular country.)

- **Examples of Partnership:**
  - Accountancy firms
  - Legal firms
  - Groups of doctors, builders etc.

2.4.3 Limited Liability Companies

The capital and ownership of a limited liability company are divided into 'shares.' The quantity and value of shares in a particular company are generally a matter of convenience or commercial viability, and there is no fixed rule: for example, a company with a share capital of $50,000 could have 100 shares of $500 each, or 1000 shares of $50 each. The shareholders elect a 'board of directors' to run the business on their behalf and to protect their interests. In many cases, especially in small companies, the directors are themselves the shareholders.

A limited liability company is a business:

- Owned by shareholders;
- Run by directors; and
- Set up as a body that is separate from its owners (shareholders).

A limited liability company is different from a sole proprietorship or partnership business. The sole proprietor or partner **is** the business; if the business goes 'bust' then so does the owner. The shareholder owner of a limited liability company **stands apart** from the business, which is a body in its own right. If the company goes 'bust,' the shareholder is protected by limited liability, and does not lose all his/her money – just the money invested in the shares of the company.

2.4.4 Types of limited companies

There are two types of limited companies:

- **Private limited company:** Most small or medium-sized businesses which decide to incorporate become private limited companies. They are often family businesses with the shares held by the members of the family. Private companies cannot offer their shares for sale to the public at large, and so they may find it difficult to raise capital.
- **Public limited company:** Public limited companies are larger than private companies. They can offer their shares for sale on Stock Market in order to raise capital, but not all public limited companies do this.

❖ **Advantages:**

- Public limited companies have more capital available than partnerships do.
- A public limited company has a legal position as a company in its own right, not just as a group of partners.
- The owners (shareholders) have a limited liability.
- The death or retirement of a shareholder does not affect the existence of a company.
- The transfer of shares from one person to another does not necessarily affect the management of the company, as it does a partnership.

❖ **Disadvantages:**

- This type of company is expensive to set up. Legal and accounting fees can be especially costly.
- In private limited companies, shares cannot normally be bought or sold to the public. The director has to approve the buyer. This may limit the capital.
- Accounts must be kept accurately. The company is legally obliged to publish and register its accounts annually. A public limited company must also have a full audit every year. The requirements for a public limited company in this area are much stricter than those for a private limited company.
- The business is less flexible than the other types of ownership.

❖ **Examples of limited companies:**

- Marks and Spencer
- Microsoft Corporation
- Larsen and Toubro

2.5 Who controls limited companies?

Shareholders own a limited company and appoint directors to control the management of the company and plan for its future.

- In case of a *private limited company*, the shareholders often are the directors, and so the shareholders can be said to control the company. One of the directors is the managing director.
- In the case of a *public limited company*, the shareholders can only speak and vote at company meetings (often only once a year), and it is the directors who control the company.
- All companies have to register with the government agency concerned. A company will also need the following documents:
  - ✓ **The Memorandum of Association:** This outlines what a company can do.
  - ✓ **The Articles of Association:** This is the internal 'rulebook' for the directors.

2.6 The Board of directors

A company is managed by a Board of Directors – commonly referred to as the 'Board' – which generally comprises between 2 and 12 directors. They are elected by the shareholders – the owners – of a business in order to run the business of the company. The directors may also own shares.

However, in a large company there might be hundreds or thousands of shareholders. It is impracticable to consult anybody or everybody, and so the directors only run the business. Shareholders are mainly interested in the results or profits achieved by the company.

2.6.1 Duties and Responsibilities of the Board

A Board of Directors has responsibilities, some of which are towards its 'shareholders' (which include its shareholders, employees, customers, suppliers etc.) Other responsibilities are imposed by law. However, the Board has the following main responsibilities:

- The Board is the trustee of the funds invested by the shareholders, and is responsible for ensuring the proper utilization of these funds.
- The Board is responsible for making policies in order to achieve the company's objective, and for ensuring their implementation. It is also responsible for making changes necessary as per circumstances.
- The Board must keep itself informed about financial matters, and ensure that sufficient 'working capital' is available. It also approves 'capital expenditure,' such as for the purchase of plant, machinery, land, buildings etc.
- It is the responsibility of the Board to appoint top executives, to ensure effective management, and provide leadership as a whole.
- It is responsible for ensuring that the company operates as per the legal/statutory requirements of the country in which it is located.

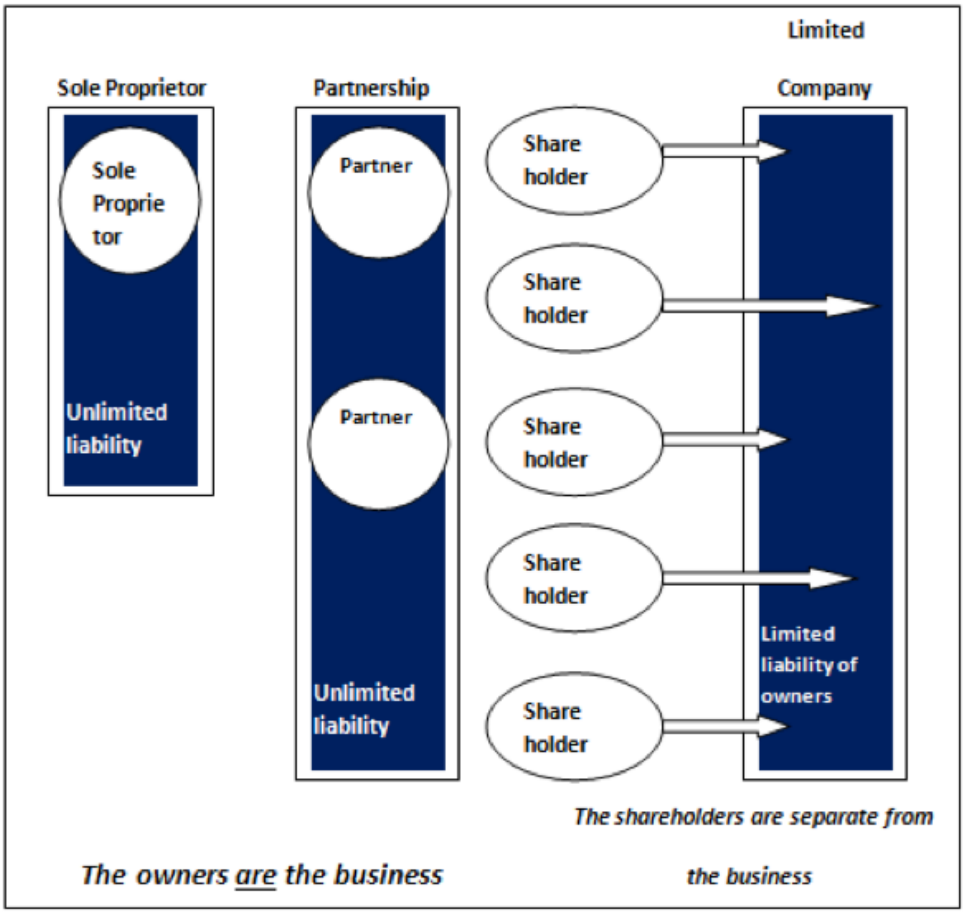
2.6.2 Structure of the Board of Directors

- **The Managing Director:** The Managing Director has a dual role. He is both a director and the Chief Executive Officer (CEO). He is involved in the day to day running of the company, and is a 'bridge' between the Board and other members of the management team. However, when the chief executive of a company is not a director, he/she is frequently referred to as the 'General Manager.'
- **Executive Directors:** These officials work full-time for the company and are responsible for the smooth running of their respective departments. Their views are taken seriously in Board meetings also.
- **Non-executive Directors:** These officials are part-time directors and are not involved in the day to day running of the company. They are often appointed for their expertise or contacts, for example, lawyers, bankers, financial advisors, ex-ministers etc.
- **The Chairman:** The Chairman of the Board (often nowadays called the Chairperson) is a director elected to the post – theoretically by the other directors and not by the shareholders. He/she chairs the meetings of the Board. He/she is not likely to hold an executive position. However, in smaller companies the Chairperson holds the position of Managing Director also and as such has an executive function. Chairperson of a large company often represents the company at various events such as press conferences, meetings with other companies etc.
- **Structure of modern management:** Generally the following structure is followed in several companies:

The Shareholders	They collectively own the company, provide capital, and elect directors, but might not participate in management.
The Board of Directors	Appointed by the shareholders to represent their interests.
Chief Executive Officer	Most often the Managing Director, but need to be a director.
Senior Executive Officers	Department managers, some of whom may be directors
Middle Management	Junior/Section/department managers (sometimes including their assistants
Supervisors	Including foremen and Junior Managers

2.6.3 Types of business ownership:

The following figure displays the types of business ownership:



2.7 Channels of distribution

A channel of distribution is the route through which goods move from the manufacturers or producers to the ultimate consumers. The types of distribution channels are:

Manufacturer/producer → Wholesaler → Retailer → Consumer

2.7.1 The Wholesale business

Wholesalers act as 'middle men' between manufacturers or producers and retail business which sell mainly to consumers. Wholesalers buy products from the manufacturer/producer in bulk quantity, and sell in smaller quantities to retailers at profit. They often give 'trade discount' to retailers when they buy in large quantities.

2.7.2 Retail business

Retailers buy products from the wholesalers and then sell the same in smaller quantities to consumers, keeping some profit for themselves in the bargain. Retailers could be small shops or large supermarket chains.

2.8 Types of trading enterprises

Specific types of large retail units might vary from country to country. However, the following are the main types of retail units found in modern day commerce:

2.8.1 Cooperative enterprises

A business formed by a group of people to get services or products more effectively and economically than they could get individually is called a cooperative. Members of the cooperative own, finance, and operate the business for mutual benefit. The term 'cooperative' refers to the two types of activities:

- ✓ A retail cooperative society – which sells goods or services to public;
- ✓ Cooperative – a group of people joining together to produce goods or to provide a service.

- **Other cooperative organizations:**
  - ✓ **Trading cooperatives:** Groups of individuals, who do not have the resources in terms of capital and time to carry out their own promotion, selling and distribution may join together to store and distribute their products. They may also set up cooperative ventures to purchase machinery and equipment.
  - ✓ **Workers' cooperatives:** A workers' cooperative may often be found where the management of a business is not succeeding and a shut-down is proposed. The 'workers' step in, with the consent of the management, and take over the ownership and running of the business with the aim of 'making a go of it' and at the same time safeguarding their jobs.

- **Advantages:**
  - ✓ This type of business offers competitive prices.
  - ✓ The dividend on purchases and the interest on shares make their goods even cheaper.
  - ✓ A range of services (for example, the Co-op Bank) are offered to the members.

- **Disadvantages:**
  - ✓ There is a danger of poor planning, management and financial control.
  - ✓ Few people have faith in cooperatives.
  - ✓ Cooperatives can only offer a limited range of goods. Famous brands are not usually stocked.

- **Examples of cooperatives:**
  - ✓ Vineyards
  - ✓ The Cooperative Society

2.8.2 Franchises

A franchise is defined as *"authorization granted to an individual or group by a company to sell its goods or services in a particular way."*

The two people involved in the deal are:

- **The franchisor**, the person who has developed a certain line of business, such as clothes retailing, hamburgers, and has made the trading name well-known.
- **The franchisee**, the person who buys the right to trade under the well-known trading name.

In return for an initial high fee the person setting up (the franchisee) receives full advice and in some cases the necessary equipment. As business trades, a 'royalty' percentage is paid to the franchisor.

- **Advantages:**
  - ✓ The franchisor offers marketing and staffing.
  - ✓ You are entering into a business which has been tried and tested in the market.
  - ✓ You are more likely to be able to raise finance from a bank for a franchise.

- **Disadvantages:**
  - ✓ The initial cost of going into the franchise – the payment to the franchisor is high.
  - ✓ A portion of your takings also goes to the franchisor.
  - ✓ You are less independent in that you cannot develop the business as you wish – you cannot change the method of doing business.

- **Examples of franchises:**
  - ✓ Burger King
  - ✓ Pizza Hut
  - ✓ Kentucky Fried Chicken
  - ✓ McDonald
  - ✓ Domino's

2.8.3 Chain stores/multiple shops

These are owned by large companies and have a number of branches within a country – and often in other countries. All the branches usually trade under the same name so that they are easily recognizable by the consumers. There is generally 'centralized' management of all stores and buying is done centrally, though each unit has a 'local' management team. Examples are: IKEA, Splash, Nike, Toyota, and Jaguar.

2.8.4 Do-it-yourself (DIY) businesses

A lot of people themselves perform work on their houses, gardens, motor vehicles, etc. For these people the range of products which can be sold on the DIY principle vary from nails, screws etc to tools, wall paper, doors, tiles, electrical equipment, kitchen equipment, and much more. Many items may be sold in 'kit form' for assembly by the purchaser, for example, furniture.

2.8.5 Mail-order businesses

Low value items of jewelry, dress, shoes, small household gadgets etc can be delivered to customers rather easily by post/courier. This has led to 'mail order' business. The supplier advertises through newspapers, magazines, TV etc and the customers can order items by mail.

2.8.6 Internet shopping

In modern times there are a number of shopping sites available on the Internet. A wide range of products from dresses to watches, household appliances to cars can be purchased online. Payment is made through Credit Card/Debit Card on the payment portal of these sites. There are a lot of such sites, for example, amazon.com, e-bay.com, netstore24×7.com etc. This facility has opened vast opportunities for buyers to browse on the Internet, compare quality and prices from the comfort of home.

2.8.7 Door-to-door selling

This is a 'direct selling' method through which manufacturers, wholesalers, and even some retailers employ sales people to call on householders at their homes to try to persuade them to buy the products they are selling. This method is quite popular in areas where the markets are at a distance from the households.

2.9 Own brands and private labels

Customers usually rely on the brand names of organizations because they are sure of the quality and price. Some large wholesalers and retailers sell products of other organizations under their 'own' brand names. For example, a large supermarket chain may sell its 'own' labeled cans of vegetables along with the normal branded cans of the same manufacturer. Thus customers have a choice. Another example is that of garment sellers. They may get the garments produced somewhere but sell them under their 'own' brand name, for example, Marks and Spencer.

3 Financing of businesses

Every new business requires capital. Generally it is in the form of money or the potential availability of money e.g. loan, bank overdraft etc. This is one type of asset while there may be other forms of assets such as land, buildings, stocks of raw materials, goods for sale etc. Initially money is required to pay for all the expenditure in order to run the business so that it can generate income.

3.1 Commonly used terms

- **Capital expenditure and fixed assets:** Money is exchanged for other assets of similar value. These assets are intended to be retained for some time such as land, buildings, machinery, office fixtures and equipment etc. Such assets are called 'fixed assets.'
- **Revenue expenditure and current assets:** It includes money spent on purchase of raw materials or semi-finished products for production or goods for resale. Such assets are termed as 'current assets.' Revenue expenditure also includes such expenses as rent, salaries, transport, electricity, water, telephone etc.

3.1.1 Fixed assets and current assets

- **Fixed assets:** A business enterprise requires a large number of items in order to carry out its activities, and which are retained for some time. Depending on the type and size of the enterprise, they might range from desks and chairs, other office equipment, to factory buildings, machinery, motor vehicles etc.
- **Current assets:** The total value of such assets is constantly changing as per the day-to-day operations of the enterprise. They include stocks of goods, raw materials, bank balance, debts owing to the enterprise etc. In some countries current assets are called 'circulating assets' or 'floating assets.'

3.1.2 Liabilities

This is money which an enterprise owes to others, that is, they are the 'debts' of the enterprise. These liabilities may include materials and/or services provided by suppliers but not yet paid for; or goods or services paid for by the customers but not yet provided to them. They also include bank overdrafts and loans received from banks and other financial institutions. Liabilities can be classified into three groups:

- **Capital,** which is raised to start the business or to enhance it.
- **Long-term liabilities,** which extend over long periods. They include mortgages or land and buildings, and loan for purchase of expensive machinery.
- **Current liabilities,** which fluctuate continually. They include money owed to trade creditors and bank overdrafts.

3.1.3 Debtors and creditors

- **Debtors:** This term refers to people and organizations who owe money to the enterprise. They are mainly customers who have been supplied with goods or services 'on credit,' and have not paid at the time of sale. The other debtors are those who have been paid in advance for goods or services not yet received. They are commonly referred to as 'trade debtors.' These types of transactions are sometimes referred to as 'book debts,' and are therefore classed as current assets.
- **Creditors:** This term refers to people and organizations an enterprise owes money to. They may be suppliers who have supplied goods or services on credit, and have not been paid at the time of supply. They might be customers who have paid in advance for goods or services. They are commonly referred to as 'trade creditors.'

3.2 Meaning of capital

Whatever its size, a business requires initial capital to start its operations. Initial capital requirements vary from business to business. Money is needed to acquire the necessary fixed assets as well as the current assets. Sufficient capital – called 'working capital' – is also required to meet the various requirements such as rent, salaries, electricity, telephone, publicity etc until such time when income from sale of goods or services is generated.

3.2.1 Funds forecast

Initial capital requirements are based on a 'funds forecast,' which is generally a part of the 'business plan.' Such a document could be a simple statement in the case of a sole-proprietor business but it can be quite complicated in the case of a medium-size manufacturing enterprise.

3.3 Raising the capital

Capital – at the initial stage or even at the expansion stage – can be raised in a number of ways. As the 'borrowing costs' are quite high because of interest rates, it is necessary that the management considers all the options before making a final choice.

The initial capital requirements of a sole-proprietor and partnership businesses are generally met by the introduction of cash or other assets such as land, buildings, tools, raw materials or goods for sale. Further requirements may be met by interest-free loans from friends or relatives. Moreover, in some countries government or semi-government agencies come forward to finance the business at low interest or interest-free loans.

In some countries banks offer assistance by way of over-draft or easy loan schemes. A small business might also finance its activities by obtaining goods on credit from suppliers, and then paying for them after generating income from the sale of goods.

3.3.1 Ordinary shares and preference shares

Obtaining finance for a limited company is more complicated than for a small business. People who invest in limited companies are not interested in the day-to-day running of business but in the 'return' on capital invested. So when such people wish to invest in limited companies, they buy shares of these companies and are interested in 'returns' on their investment – called 'dividends.' The companies usually issue 'ordinary shares' which have a 'nominal' or stated value, but they might be issued at a discount, i.e. below the nominal value or at a 'premium,' i.e. above the nominal value. At the end of a business year, the Board of Directors of the company decides to distribute dividends depending on the profits made. Most ordinary shares give the share-holders 'voting rights' to vote at general meetings.

Some companies sometimes issue 'preferential shares.' Their holders receive a fixed rate of dividend before any profits are shared among ordinary shareholders. This fixed rate may be 5% or 10% or any other dividend. Preference shares are usually cumulative. It means that if in any year the profit is insufficient to pay the full fixed amount, the balance shortfall is added to the dividend in the subsequent year and is paid in full.

Here is an example how the share value is calculated:

> Let us assume that a company has an issued share capital of $500,000 made up of:
> 20,000 5% shares of $4 each = $80,000

+ 420,000 ordinary shares of $1 each = $420,000

At the end of a profitable financial year the company's net profit, after having made the necessary reserves, amount to $80,000, which the directors recommend should be distributed to its shareholders.

The dividend payable for preference shares @ 5% of $4 = $0.20 (or $0.04 for each $1 invested)

Total amount payable to preference shareholders = 5% of $80,000 = $4000

Amount remaining for distribution to ordinary shareholders = $80,000 – $4000 = $76,000

$76,000 ÷ 420000 = $5.52 per ordinary share

So a particular shareholder will be paid that sum for each ordinary share. If he/she holds 500 shares, they will be paid $2760.

3.4 Raising additional finance

In the course of business there may be a necessity of raising additional finance. It may be done in various ways.

3.4.1 Bank loans and overdrafts

A 'loan' refers to money which is borrowed with the intention that it will be repaid at a later date. The most common sources of loans for business purposes are banks and other financial institutions.

- **Term of loan:** The bank (or the financial institution) might agree to lend the sum of money over a period of one year, or two or three years, or longer. The period of the loan may be short-term (one or two years) or long-term depending on the business plan of the enterprise. For short-term, banks may allow overdraft facility to their customers.
- **Security or collateral:** To reduce the risk of losing money, a bank will usually require the borrower to make a 'pledge' that in the event of all or part of the sum loaned and not being repaid as agreed, the bank may seize – through due process of law – some property of the borrower; that is called 'security' or 'collateral.' Rarely will a bank loan be made without suitable security or collateral. Instead of asking for security, or in addition to security, the bank might require another person of standing (perhaps a director or another executive of the business) to 'guarantee' the loan. This means that in the event of the business not being able to repay the loan, the guarantor can also be pursued by the bank to pay all or part of the loan not repaid by the borrower.
- **Interest:** A bank charges its customers for the services it provides to them. Hence the bank charges a certain rate of interest, which is usually presented as a percentage, such as 10% or 15% of the sum borrowed. Sometimes the rate of interest is 'fixed' during the term of the loan; sometimes it is 'variable,' which means that it might 'fluctuate,' that is it might rise or fall.

3.4.2 Mortgages

A mortgage involves the advance of a loan to a person (or more than one person jointly e.g. partners) or to an enterprise – called the 'borrower' or 'mortgagor,' by another enterprise such as a bank or a financial institution, building society or insurance company – called the 'lender' or 'mortgagee.'

The money loaned and used by the borrower to acquire an asset, frequently a 'property' or 'real estate,' such as land or a commercial building or a factory becomes the 'security' or 'collateral' for the sum loaned. Usually a mortgage is a long-term loan, often up to 25 years. The borrower undertakes not only to repay over a period of time by 'installments' the sum borrowed – which is called the 'principal sum' – but also to pay 'interest' which is the mortgagee's 'return' on the sum loaned. The rate of interest payable might be 'fixed' for the term of the mortgage or might be 'variable.'

3.4.3 Debentures

An alternative which many companies resort to is the issue of 'debentures,' which are documents acknowledging loans and giving the lenders a 'charge' against the company's assets. Each debenture states the sum borrowed, the rate of interest to be paid thereon, and the terms upon which the sum borrowed is to be repaid, as well as particulars of the assets mortgaged or charged as security for the loans. If the sums borrowed are not repaid (or re-negotiated by the due date) the lenders can take possession of the assets concerned, from the proceeds of the sale of which they can reimburse themselves. It is important to note that debentures are 'loans' to the company and not additional capital.

3.4.4 Leasing, Contract Hire/Rental

The facility for an enterprise to lease, hire or rent might be an important consideration in the acquisition of relatively expensive items such as plant and equipment, motor vehicles, computer systems etc, particularly if they depreciate in value fairly rapidly. Generally an agreement is made between the customer and a financial institution (perhaps a bank) under which the customer makes regular payment – which usually combine elements of capital repayment and interest – and leases, hires or rents the items from the finance house.

- **Sale and Lease Back:** Certain fixed assets might be sold to an investment company under an agreement which allows the enterprise to lease back the assets from the investment company at an agreed rate for a specified period. The leasing/rental payments will be met out of revenue income.

3.4.5 Hire purchase

On payment of a deposit, the customer takes delivery and may make use of the item(s) involved, but does not become the owner of the item(s). The customer enters into an agreement to pay the balance of the purchase price plus interest and service charges by regular installments.

4 Starting a business

The first matter to be decided when considering the establishment of a new business is its objectives: what it is going to do, and what it is hoped the new business will achieve. Once the objectives are clear, basic policies can be laid down to decide how those objectives will be achieved. It is important that adequate thought be given to objectives and basic policies and, if necessary, that full investigations and research be undertaken before final decisions are reached.

4.1 Business plans

Plans are 'routes to objectives,' and they have to be made in advance to show the best ways in which the objectives of a business will be achieved in practice. Plans are particularly important before a new business is established, and they should be set out in what is called a 'business plan.'

The modern business world is composed of a huge range of kinds and sizes of businesses, engaged in very many different types of activities, and therefore there can be no set format for a business plan. However, these are the general guidelines of what needs to be included:

- ❖ What are the objectives the business will be:
  - Is it going to make or produce products – if so what?
  - Is it going to buy and sell products – if so what?
  - Is it going to provide a service – if so what?

In other words, the very 'nature' of the business has to be determined.

- ❖ What 'activities' the business will be involved in to achieve its agreed objectives; what actions will have to be taken, and in what manner those activities will be carried out.
- ❖ Who will 'run' or manage the business, and/or work in it. The owner of the business might work alone, or have family members to assist, or might have to employ one or more employees, or work with a 'partner.' The experience, training, knowledge and skills of the owners/partners and/or employees should be determined and listed.
- ❖ From where the business will operate – its location – and the premises it will require.
- ❖ What market is there for the products the business is going to make, produce, buy and sell or provide?
- ❖ What 'competition' will have to be faced; that is, what other businesses there are making or producing or buying and selling or providing the same or similar products, especially in the same locality or vicinity.
- ❖ A 'funds forecast' dealing with financial matters has to be prepared. These include how much money will be needed to establish the business, to buy machinery and equipment, to buy stocks of goods or materials or components, to rent or buy premises, to pay for expenses, to attract customers, and to keep the business 'running' until it earns sufficient income from its activities. Also, how much, if any, money is already available, how much will have to be raised from other sources, and what those sources are likely to be.
- ❖ A 'profits forecast' – an indication of how much profit the business is expected to gain, year by year – is to be prepared.

4.1.1 Initial capital

The initial capital requirement might not, in some cases, be large or have to be entirely in the form of actual money. For example, a new business person might already own land or building from where to operate the business, or stocks of goods or raw materials, or machinery or equipment. Nevertheless, whatever the type of business some money will be needed, and not necessarily only at the time at which the new business is started or formed – it might be weeks or months after that time before sufficient income or revenue is received to enable the business to 'pay its way.'

4.1.2 Reserve capital

Before start-up, money will probably be required for some time after the business has commenced operations. That applies not only because of foreseen or budgeted factors, but possibly also due to unexpected 'external' factors over which the business person has no control. For example, any factors which decrease sales will have an adverse effect on the financial position of a business. Some can be anticipated in advance, and planned for, but others cannot be, and the consequences for business which has no reserves of capital to 'fall back upon' can be severe. Examples of such factors include:

- Poor health of the owner or a key employee;
- Loss of key personnel;
- Strikes by workers in other industries such as transport, resulting in business running 'out of stocks' of goods;
- Political upheavals or natural disasters;
- Tax increases;
- Other government actions such as the 'fixing' at short notice of the price of certain basic commodities like petrol, diesel etc.;
- Unexpected competition.

4.1.3 Link between capital and ownership of a business

Frequently there is a necessary link between capital and the ownership of a business. For example, a person might have a good idea for a new business, and might be confident of making a success of it, but might lack sufficient initial and operating capital to get it 'off the ground.' If other sources (e.g. banks, which are very conservative about new ideas) fail, then the only option left might be to seek a partner, either in forming a business partnership firm, or who is prepared to purchase a reasonable proportion of the shares in a limited company. Perhaps two or more such people will have to be found.

4.1.4 Avoiding problems in partnership

It might be felt that a business partnership firm, run under a mutually acceptable partnership agreement in writing, might be a better solution, and in some cases it might well be – provided the partners get on well together and trust each other. However, in many cases a partner might wish to sell his 'share' in a firm, or withdraw the capital he invested in it. When a partner withdraws from a firm (or a new partner is admitted) the original firm ceases to exist. A new firm might be formed immediately by the remaining partner(s) – with or without the admission of one or more new partners – but there might still be problems and complications, particularly with replacing the capital withdrawn by the existing partner.

Where capital and control of a business are concerned, there is always the possibility of conflict arising. Wherever possible, likely problems should be anticipated in advance, and comprehensive 'partnership agreement' should be drawn up by an experienced lawyer, to cover all eventualities, and should be signed by all parties involved. In most countries there is usually a legal statute to govern many matters concerning business partnerships in the absence of a formal partnership agreement.

4.2 Assessing market potential

Sometimes there is a 'ready-made' market. For example, people in a small town or village might not at present be able to obtain easily certain products which are readily available in larger towns or cities, although they are willing and able to buy those products. What the business person then has to decide is whether the number of potential customers warrants the expense of establishing a business, and that might depend on whether there is likely to be a continuing – and preferably increasing – demand for what they hope to sell.

In other cases a 'demand' for products has to be created. Potential customers might not be aware of the benefits to them of possessing or using certain products, they might not be aware that a particular product even exists, or that it is superior in any way to similar products with which they are already familiar.

4.2.1 Meaning of market

The common usage of market means a place where goods are bought and/or sold. A market need not necessarily mean a place of exchange. The word market is commonly used and may mean or aim in any of the following:

- Market may mean a place where buying and selling take place;
- Buyers and sellers come together for transaction;
- An organization through which exchange of goods takes place;
- The act of buying and selling of goods (to satisfy human wants);
- An area of operation of commercial demand for commodities.

4.2.2 Market research

It is necessary to 'research' the market before a new business is established, and at various times when circumstances, e.g. falling sales, dictate. Basically the process of market research seeks to provide answers to these kinds of questions:

- What is the size of the demand for the products the business can supply?
- How does demand vary from area to area, and are there any common factors to account for the variations, e.g. are sales higher in towns than in countryside, or are the products purchased by higher income groups residing in suburban areas?
- What kinds of outlets are there in each area: are they mainly retail shops, department stores, offices, factories etc.?
- What share of the market has the business currently secured and how does it compare with the shares of the largest competitors, and how can the business' share be increased in a profitable way?

Not all these questions are applicable to all businesses or to all types of products. Nevertheless, the answers obtained to the listed questions can provide very valuable – and often surprising information – for management, and can form the basis for planning and meaningful decision-making.

4.2.3 Competition

The potential market for the products or range of products which a particular business hopes to manufacture and/or sell is very often limited or restricted by other – competitive – businesses making and/or selling the same or similar products. It must be assumed that there is likely to be only a limited number of customers for certain types of products in a specific area. That number might be fairly 'static,' or might increase gradually as standards of living and incomes increase, or might decline due to economic factors, government intervention etc. In other cases, in say a 'tourist' area, the numbers of potential customers might fluctuate widely at different times or 'seasons' of the year.

Whatever the situation, it can often be dangerous to contemplate starting a new business in an area in which there are already a number of established businesses selling the same or similar products, or providing the same services. In order to compete successfully with established businesses, the new ones must be able to offer customers something special or new, or be able to give faster or more efficient service to customers, or be able to ensure sufficient savings for customers, e.g. by charging far lower prices. The 'launch' of the new business might be supported by extensive advertising, publicity and sales promotion campaigns, all of which are, of course, designed to attract the maximum number of customers to the new business as soon as possible.

The key factor, then, in the establishment of a new business is to try to find an 'area' (not necessarily a physical one) in which there is market potential which is not adequately being catered for at present. That might mean the location of a business in a town, or a part of a town or city, in which there is little or no existing competition, or the manufacture (or import from another country) of a product or a range of products for which a demand exists – or can be created – but which is not currently available to potential customers.

4.2.4 Location of businesses

Location of businesses depends on various factors given below:

- **The type of business:** Many businesses depend for much of their trade on 'passers-by,' that is, people walking or driving past the premises from which the business operates, e.g. shops and stores selling electrical appliances, clothing, footwear, books, jewelry etc. The majority of businesses which depend in full or in part on 'passing trade' need to be situated at ground level in busy streets or arcades or malls along which large numbers of people pass every day. Businesses which do not depend on 'passing trade' can often be located on upper floors of buildings, or away from the hustle and bustle – and expense – of main thoroughfares or shopping precincts, e.g. insurance brokers, accountants, lawyers and other 'professionals,' artisans such as tailors, hairdressers, and technicians such as those who repair electrical appliances, watches, televisions, and so on. Wholesale businesses, which do not depend on 'passing trade', might be located in quieter areas.
- **The market:** in addition to existing or potential competition, the 'market' can be looked at from two aspects:
  - ✓ **The natures of products sold/service provided:** When considering the 'nature' of products, their qualities and prices must be taken account of.
  - ✓ **The class of customers/clients whom it is hoped to attract:** The class – or financial status – of the majority of people who frequent an area should be carefully researched before deciding whether there is a market in that area for the types of products it is hoped to sell.

- **Special facilities or needs:** Some businesses have special needs, or require special facilities, which might dictate the areas in which they have to be located, or limit the choice of areas. Some businesses rely on good access by road and/or rail for transport delivering or collecting their products. Others might need to be located near to an airport. Some businesses – like hypermarkets – might need parking facilities for customers.

4.3 Purchasing existing businesses

There can be advantages in an individual, a group of people or an enterprise buying an existing business rather than starting a new one, and possibly to compete with the existing one.

4.3.1 Reasons

There are many reasons why such action might be taken:

- It could be that the business is for sale just at the time that a person or a group of people is considering establishing the same or similar type of business in the same general area.
- An established business may want to 'diversify' its activities – to broaden the range of its activities – either by venturing into a different type of activity or might want to use the business it is buying as a 'branch.'
- In other cases, the only way to secure the use of particular premises is to buy the business currently operating from it.

4.3.2 Price and negotiation

The price, which the owner(s) of a business might initially ask is generally not the final sum which will be accepted for it; that will have to be arrived at, usually, after negotiation. It is important to try to establish as closely as possible the true value or worth of a business, both to the current owner(s) and to the prospective purchaser(s). Generally the overall value of a particular business will be a combination of two main features:

- The agreed value of unencumbered assets, less the value of its current liabilities;
- Its particular ability to earn profits for its owner(s), and to keep on doing so.

4.3.3 Renting of premises

A business might operate from 'rented' or 'leased' premises and it is then important that the 'lease' – the document which sets out the terms of renting or leasing of the premises – be studied carefully, preferably by a lawyer. The wording of some leases can be – often deliberately – vague, and so it will be well worth the little expense of a lawyer before signing a lease or accepting the transfer of one.

5 Business organization

5.1 Delegation of responsibility

Delegation of responsibility is essential in any enterprise. No one person can be responsible for, and control, every little aspect and activity, except perhaps in very small businesses. Even a sole-proprietor might have to delegate some responsibility – for bookkeeping, for instance – to another person. Delegation is:

- A process of assigning various degrees of decision making authority to subordinates;
- A process by which a sole-proprietor/manager assigns some of the tasks to subordinates on selective basis and allows them to exercise authority on his/her behalf to perform the assigned task;
- A primary formal mechanism by which a network of authority relationship is established;
- Conferring authority from one executive of the organizational unit to another to accomplish a particular assignment.

5.1.1 Process of delegation

The following stages and steps are to be carried out in sequence:

- Sizing up workload;
- Assigning work appropriately;
- Granting authority;
- Creating accountability.

5.1.2 Features of responsibility

Responsibility has these features:

- Obligation to perform assigned work satisfactorily;
- Acceptance of assigned work leading to becoming responsible;
- Cannot be transferred or delegated further;
- Acceptance of responsibility leading to becoming accountable to superior;
- Flows from lower to higher levels.

5.1.3 Effective delegation

Effective delegation can be achieved by making use of the following guidelines:

- Establishing objectives;
- Evaluating competence of subordinates;
- Defining responsibility and authority clearly;
- Motivating subordinates;
- Establishing communication channels;
- Imparting proper training;
- Exercising supportive supervision;
- Determining standards of performance;
- Incorporating a feedback system.

5.2 Expansion of business

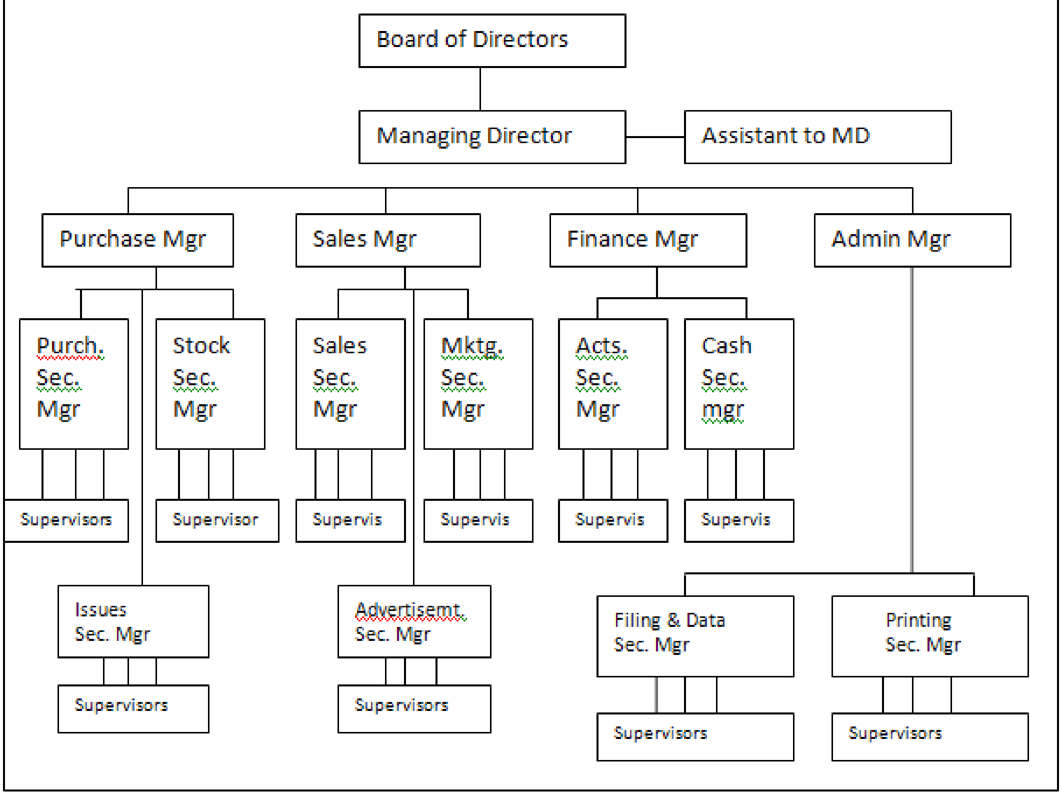
If the business continues to expand, each of the owners/managers will probably need assistants. Thus, over a period of time, 'sections' – containing groups of people engaged in related or similar work – will come into being; the sizes of the sections will vary, and even at this stage they might be called 'departments.'

Although people working in each section will be performing related tasks, it is likely that gradually different people will 'specialize' in different activities, depending on their abilities and aptitudes and the necessity for specialization or the division of labour within a particular section. Should the business continue to expand, specialist sections will themselves have grown into large sections. Some originally small 'sections' will have grown into full 'departments' comprising a number of sections. By this stage, the owner of the small business will no doubt have formed it into a company, of which he/she might be managing director, if they have not relinquished their managerial control – in which case there will probably be a salaried managing director or general manager, responsible for the overall control and coordination of the activities of the new large business.

5.2.1 Organizational structure

The organizational 'make-up' – or structure – of the company can be illustrated in what is known as an 'organization chart.' An organization chart shows how responsibility is delegated from top management to lower levels of management.

Fig. 5/1 **Sample Organization Chart of a Company**



The organization chart shows responsibility and authority being delegated 'downwards,' but at the same time the personnel shown lower in the chart are accountable for their actions, decisions etc to the executive in the next box 'upwards.'

5.2.2 Planning the organizational structure

The organizational structure of an enterprise, or a department of it, should be planned for the greatest effectiveness. Opportunities for changes in organizational structure might be limited in an established business – although they might arise from time to time, due to diversification or amalgamation for example – but a planned organizational structure must not be overlooked in the establishment of a new business.

The steps in setting up of an effective organizational structure are:

- The activities which will be necessary to achieve the objectives of the business must be established.
- The various related activities should be grouped together into departments.
- The necessity to lay down the extent and the limits of authority and the duties of all those who will hold managerial positions and the authority to delegate must be provided.
- To ensure effective coordination of all parts of the enterprise, effective procedures and systems of communication must be devised and installed.

5.2.3 Spans of control

By this term is meant the number of people reporting directly to one supervisor or manager. The number of subordinates who can be effectively supervised directly by one supervisor or manager can vary greatly from one section or one department to another. A question often asked is: *"How many people can a supervisor or manager control?"* The answer to this question is not simple because different factors and/or circumstances are involved in different cases. For example:

- Not all managers and supervisors have the same talents or abilities, and some managers and supervisors find it difficult to cope with a large number of subordinates.
- The nature of the work being performed is a significant factor. If the work is relatively simple and if most employees are performing the same work, large numbers can be supervised relatively easily. On the other hand, fewer people can be supervised effectively by one person if their work is complex.
- The experience and reliability of the workforce is another factor. Fewer new, little trained people can be effectively supervised by one person than can trained people who have been performing the same work for the enterprise for some time.
- The amount of time available for supervision is a vital consideration – particularly in cases in which a manager might frequently have to be away from his/her post during the course of their duties.

Adjustments in spans of control might have to be made from time to time as circumstances and/or personnel (both supervisory and managerial, and subordinates) change. Too wide span results in lack of control, while too narrow a span involves wasted personnel and an 'over-supervised' workforce.

5.3 Types of organizational structure

There are various types of organizational structure:

5.3.1 Line Organization

This is the simplest form of organization and can be very efficient, particularly in small and medium-size enterprises. Line organization is illustrated in Fig. 5/1, and is so called because there is a clear 'line' of responsibility and authority right through the management structure from the Board of Directors to the lowest level of supervision, and below. Line organization is simple and direct. The 'chain of command' is direct, and so decisions can actually be made quickly and implemented rapidly, while because of the directness of the control, the coordination of the activities of all the people employed in a department is simplified.

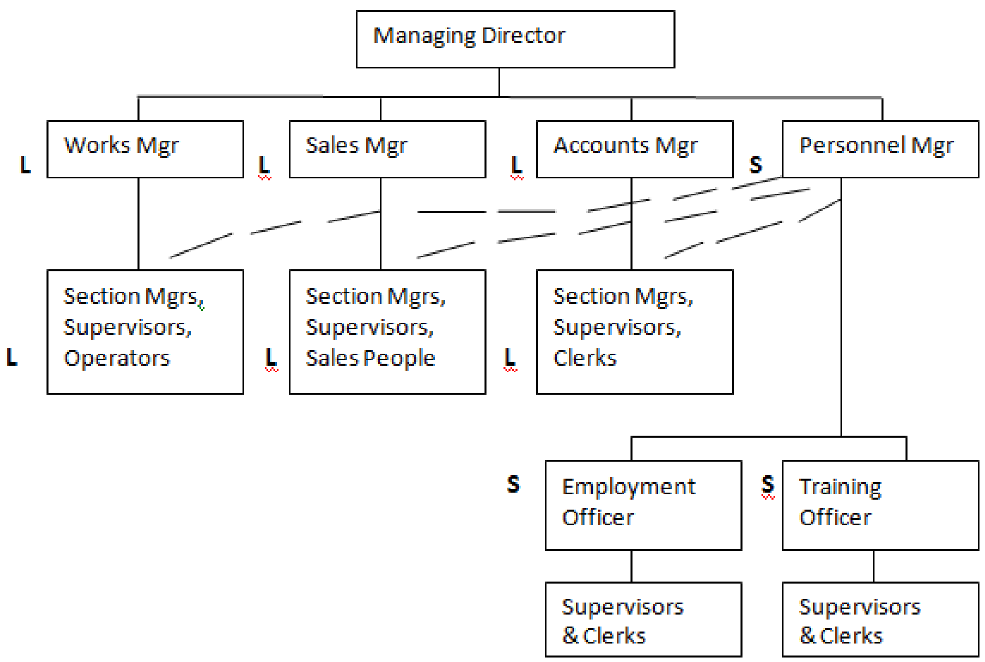
5.3.2 Functional Organization

This is the type of organization in which it is the 'function' (the type of activity) which determines the areas of authority and responsibility. An expert or 'specialist' is placed in charge of each function, and will have direct control of that function wherever it is undertaken within the enterprise. For example, the HR/Personnel manager will have authority over employees in whichever department they might work, or the office manager might have authority over clerical and secretarial staff working in any department. This means that line managers, in whose departments the relevant function is being carried out (and who are responsible for all matters relating to their staff) find their authority reduced with regard to functional activity, and to discipline and to employee relationships. As the functional specialists are not involved in the day to day running of the enterprise (which is the province of the line manager) they are free to concentrate on their particular functions wherever they occur, which do produce many benefits for the enterprise. However, this form of organization makes control difficult, as there are no clear lines of authority and it is similarly difficult to establish when things do not go right. Furthermore, staff as well as supervisors and junior managers become confused at being subject to the authority of more than one supervisor.

5.3.3 Line and Staff Organization

This is the combination of line and functional organizations and is an organizational structure commonly used successfully. It is important to note that the word 'staff' in this case refers not to the workforce of an enterprise or a section of it, but to specialists who act mainly as 'advisors' and who have no executive authority outside their own departments.

Fig. 5/2 Sample Line and Staff Organization



L – Line relationship; Responsibility authority shown by: ________________

S – Staff Relationship; Staff-advisory relationship shown by: - - - - - - - - - - - - - -

In such a structure:

- The 'line managers' control the 'primary functions,' such as marketing and production, which are directly concerned with achieving the objectives of the business.
- The 'staff managers' are generally involved with 'secondary functions' which assist the smooth and efficient running of the primary functions.

It is clear from Fig 5/2 that the HR/Personnel manager is directly responsible for his/her own department and has full authority over its staff. However, although his/her department provides services for the line managers and supervisors with regard to recruitment of personnel, personnel records, and personnel welfare, they have no authority over the personnel in those other departments.

The 'composite' form of organization ensures that the lines of responsibility and authority are still clear for all (managers, supervisors and staff alike) to see, and understand. The line managers keep full control of their respective departments or sections, while having expert advice and assistance available in many subsidiary areas. The relationships between the line managers and the staff managers must be clearly defined, and cooperation between them must be encouraged.

5.4 Communication in business

Communication is a vital tool of management in business. In fact, communication in management can be defined as *"passing on a message from one party to another in such a manner that both parties understand its identical meaning."* If these messages are not passed on and understood in exactly the same manner, there might be disagreements, mistakes, and disputes.

We can say that:

- If there is no communication, no work can be done in an enterprise.
- No information can be given or received.
- There will be no contact between the members of management.
- There will be no contact between the managers and subordinates.
- There will be no contact between the enterprise and its customers or suppliers.

5.4.1 Internal communication

Effective internal communication ensures that every member of management and every other employee will receive precise and accurate information, to ensure that every person working for the business knows exactly what he or she is expected to do, when and where; for what and for whom, and to whom, they are responsible, etc. Misunderstandings and misinterpretations – which can result in wastage of time, effort, labour or money and/or loss of profit, can therefore be greatly reduced or even eliminated.

In a business enterprise communication has to be of the following two types:

- **Vertical communication:** In an enterprise communication must operate in both directions – 'upwards' as well as 'downwards.' That's why it is called 'vertical' – up and down – communication. When information and instructions are passed on from managers to subordinates, there is 'downward' communication. On the other hand, when subordinates have some problems, complaints or suggestions, there is communication 'upwards' – from subordinates to managers. This vertical communication makes it possible for instructions and information to reach the subordinates, and subordinates' feedback to reach the management. This system ensures that the subordinates are able to perform their duties effectively, and the managers are able to address the issue raised by their subordinates. This is possible with two-way communication. 'Lines of communication' between the management and subordinates should be established. This will ensure that information reaches the subordinates quickly, and any change of plan depending on the observations of subordinates can be made quickly and implemented efficiently.

- **Horizontal communication:** There must be horizontal – sideways – communication in an enterprise. This means that information must flow between the personnel of similar status in various departments, for example, between the Marketing Manger and the Production Manager. This type of communication can be effective only if the members of different departments cooperate with each other. When effective horizontal communication exists in an enterprise, it increases the efficiency of the enterprise. Sometimes there may be difficulties in ensuring effective horizontal communication because of personal attitudes, jealousy etc. Some department or section managers may not pass on the correct and timely information to managers of other departments and sections. The top management must ensure that this type of attitude is checked.
- Horizontal communication is concerned with flow of information from one department to another. It is not the flow of instructions. For example, a member of the marketing department may inform the production department about the customers' complaints regarding the poor quality of products. This means that he is only providing the information he has received, and not giving any instructions about the product. The manager of one department must not communicate directly with a subordinate in another department without the knowledge of the subordinate's manager. When all such limits of responsibility and authority are clear to everyone, horizontal communication will increase effectively.

5.4.2 External communication

Without external communication a business would be isolated from its potential and existing clients/customers and its suppliers. Effective and efficient two-way external communication is important in maintaining good public relations by:

- Ensuring that customers or clients are satisfied with the standard of the goods or services provided and that what is being produced or provided is what they require.
- Ensuring that any consumer complaints are speedily and satisfactorily dealt with.
- Ensuring that consumers are kept apprised of new and/or improved products or services (involving advertising and publicity).

Up to date information is also necessary about activities by competitors, new technological development, buying trends, changes in fashions or in consumer preferences, etc. Communication might also have to be maintained with training establishments, trade associations, government departments, professional firms, banks and financial institutions, and with a wide range of other people and/or organizations.

6 Budgeting and pricing policy

6.1 Importance of budgeting

Plans which are prepared in advance to show how the financial and material resources will be required and be used by an enterprise during a specified period are called 'budgets.' A major failing of far too many businesses – and in particular smaller ones – is that their managements do not prepare or use budgets. The point is that a budget is a plan, and all responsible planning is far better than no planning at all.

6.1.1 Benefits of budgeting

Some of the benefits which can be gained from budgeting include:

- The people who are responsible for preparing the budgets have to consider all aspects of expenditure estimated to be incurred by the business and compare it with the income estimated to be generated during the period concerned. In doing so, areas of wastage or excessive spending might be identified, as might areas in which income might be being lost or in which potential is not being fully exploited. The opportunity for remedial action to be taken is therefore provided.
- The comparison between budgeted figures and actual results might also reveal areas of the enterprise's operations which require management's attention and action.
- The existence of budgets makes all employees, including managers and supervisors, aware of the need to conserve the resources of the business.
- The preparation of the 'master budget' for the entire enterprise requires that all sections and departments of it cooperate fully with each other, e.g. production and sales, and are aware of each other's areas of responsibility.

6.1.2 Budget preparation

The responsibility of preparing budget depends largely on its size, its organizational structure, and on its range of activities. The owner/manager or the partners of a small business might prepare its budget. A large organization is likely to set up a 'budget committee' to take charge of all matters relating to budgeting.

It is helpful if the budgeting system and procedures, as well as the responsibilities of the people producing budgets, are set down in writing. The people responsible for producing budgets should not work in 'isolation,' particularly when a large department is concerned. Supervisors in charge of sections, and in some cases even individual employees, should be consulted. After all, those intimately involved with certain tasks or groups of tasks are most likely to be able to make reliable estimates.

6.1.3 Sales budgets

These are based on sales forecasts and on the estimated revenue there from. The two main methods used are:

- Using statistics showing volumes of past sales, and identifying factors which influence increases or decreases in certain periods;
- Obtaining the opinions of experienced sales personnel, both individuals and groups of sales people and those in managerial positions.

6.1.4 Production and purchasing budgets

In non-manufacturing enterprises there will be really 'purchasing budgets' or 'stock control budgets.' Whatever the activities of a particular enterprise, those executives who are responsible for ensuring that the products are available when required for sale, must base their budgets on the sales forecasts – hence the need for close interdepartmental cooperation in preparing them – and in fulfilling them.

An important matter concerns the 'stock levels' maintained by the enterprise, whether they are for goods produced by it (and the materials/components used in their manufacture) or are purchased by it for sale.

Only if forecasting and budgeting can be done as accurately as possible, and if there is good interdepartmental cooperation, can problems be anticipated and, wherever possible, solved in advance.

6.1.5 Cash budgets

The term 'cash' refers to both money in hand and money 'at bank,' There is little benefit in a business budgeting for production and sales if at some stage during the budget period it runs out of cash without the means for financing the production or selling activities.

It is therefore essential to budget for cash, so that any likely shortfall of cash will be anticipated, and plans can be made in advance to overcome the problem. It might be necessary to arrange for short-term finance, such as a bank overdraft or a bank loan, which will have to be agreed upon in advance by the bank manager concerned. Alternatively, more long-term finance might be required by such methods as a share issue or debentures.

Example of cash budget

1. Income from credit sales (i.e. debtors) estimated to be:

Jan	Feb	March	April	May	June
$21,000	$27,300	$52,500	$73,500	$84,000	$162,750

2. Expenditure estimated to be:

Jan	Feb	March	April	May	June
$26,250	$28,350	$72,450	$81,900	$103,950	$108,150

3. Cash at bank on 1st January: $8,400

Based on these figures, the following cash budget could be prepared in advance:

	Jan ($)	Feb ($)	March ($)	April ($)	May ($)	June ($)
Cash balance at start of month	8,400	3,150	2,100	-	-	-
Cash shortfall at start of month	-	-	-	-17,850	-26,250	-46,200
Estimated income during month	21,000 29,400	27,300 30,450	52,500 54,600	73,500 55,650	84,000 57,750	162,550 116,550
Estimated expenditure in month	26,250	28,350	72,450	81,900	103,950	108,150
Estimated balance at end of month	3,150	2,100	-	-	-	8,400
Cash shortfall at end of month			-17,850	-26,250	-46,200	

6.1.6 Master budget

Many other budgets can be prepared for various sections of an enterprise. Examples include budgets for selling expenses, distribution expenses, administration expenses, manufacturing expenses, capital utilization, manpower, direct materials, direct labour, and others.

Once the various budgets have been prepared, they are collated and incorporated into a 'master budget,' which is a 'blue print' for the enterprise for the coming period.

Example of budget for Sales & Marketing Department

Budget for the year 1st January 20…To 31st December 20… **Department: Sales & Marketing** **Prepared by:** **Approved by:**		
Expenditure area	**For year ($)**	**For a 4 week period**
SPECIFIC:		
Salaries, Commissions & Allowances	104,000	8,000
Advertising & Display material	26,780	2,060
Telephone & Postage	3,900	300
Transport	2,600	200
Printing	8,320	640
General Expenses	2,600	200
Others	650	50
PROPORTIONAL:		
Rent & Rates	6,500	500
Insurance	1,079	83
Directors' Fees & Audit	3,900	300
TOTALS	**160,329**	**12,333**

6.2 Budgetary control

The approval of the master budget is not the end of the budgetary process. It is, in fact, merely the beginning. The whole purpose of budgeting is the establishment of 'standards' against which actual results, whether in the form of income, expenditure, production or sales, can be compared.

6.2.1 Budget review statements

Once a budget has been allocated for the relevant period, the manager/supervisor is responsible for controlling the department, section or processes by keeping the various costs within the limits imposed by that budget. It is therefore essential that there is an effective method of checking that performances and/or expenditure do comply with the allocated, approved budget. A good method of exercising budgetary control involves preparing regular budget review statements every month (or every four weeks for more accurate comparison between periods.) Such statements will enable a manager to spot quickly whether the business or the department or section of it under his/her control is over-spending or under-spending in any area, and allow the reasons for the variances to be quickly investigated – and for the necessary corrective action to be taken quickly.

Example of a Budget Review Statement (Section only)

Budget Review Statement
For Period: 1.8.20… To: 29.8.20…
Department: Sales & Marketing

Expenditure Area	**Period**		**Variance**		**Remarks**
	Budget ($)	**Actual ($)**	**This Period ($)**	**Year to Date**	
Salaries, Commissions & Allowances	8,000	9,500	1,500	1,800	Sales exceeded forecasts
Advertising & Displays	2,060	2,060		32	
Telephone & Postage	300	350	50	75	Increase in rates
Prepared by: Checked by:					

6.2.2 Variances

A 'variance' shows the difference between the amounts budgeted to be spent on a particular 'expenditure head' during a particular period, and the amount which was actually spent. Variances can be classified into the following:

- **Adverse variances:** These occur when the actual expenditure is greater than the amount budgeted to be spent; and
- **Favourable variances:** These occur when the actual expenditure is lower than the amount budgeted to be spent.

However, the words 'adverse' and 'favourable' used in the context of budgeting do not necessarily have the same meaning in ordinary usage. Only after a particular variance has been fully investigated, can it be decided whether it is a 'good' or a 'bad' result. For example, under-spending on advertising might appear to be a 'saving' for a business, but if the result is a drop or decline in sales, the result is a bad one, and the variance is 'adverse.' On the other hand, if the variance is caused by a change to a different media which has produced improved sales at a lower cost, the result is clearly a good one, and the variance is 'favourable.'

In addition, such budgetary control – comparing forecasts or estimates with actual performance – provides valuable data for subsequent forecasts.

6.3 Standards in business

Controlling is the function of management which checks whether what was planned to happen actually does happen and, if necessary, ensures that corrective action is taken. All operations or processes must be checked or inspected, and performances must be measured against targets set in the plans, and against set 'standards.'

A business will set its own standards for the various types of work to be performed and for its end products, although in some countries there might be laws to ensure that various products meet certain quality or safety standards, and of course often consumers will indicate the standards they expect. Standards apply in virtually all organizations, whether industrial, trading, distributive, service or governmental. And standards must be flexible so that they can be amended in the light of circumstances, for instance, changes in consumer demand, rising costs, new technology etc.

The following types of standards can be used:

- **Ideal standards:** They are set at the maximum level of efficiency. They are in effect standards of 'perfection' and as such can rarely be achieved, and then only for short periods.
- **Attainable standards:** They are set at levels which it is considered are capable of being attained with reasonable effort.

Much depends on the type of work being performed and on the caliber of employees, on the work environment and work climate, on management's attitude towards its workforce, and on the managerial skills of individual managers, supervisors and foremen. Reasonable, understanding and fair management is most likely to result in attainable standards actually being achieved on a regular basis.

6.4 Pricing Policy

A good price policy is of great importance to the producers, wholesalers, retailers and the consumers. If the prices are too high, only a few buyers purchase and if the prices are low, several buyers purchase. Thus market may be reduced or increased. Therefore, a sound pricing policy must be adopted to have maximum sales.

6.4.1 Pricing Objectives

Before determining the price itself, the management must decide the objectives of pricing. The main goals of pricing may be classified as follows:

- **Pricing for target return:** Business needs capital for various types of activities. When a businessman invests in a business, he calculates the possible return on his investment. A certain rate of interest on investment is aimed. Then the price is fixed accordingly. The target of a business organization is fixed in terms of investment. For example, a company may set the target of 10% or 15% return on investment. This target may be a long term or short term. Wholesalers and retailers may follow the short term, usually a year. They charge a certain percentage over and above the price at which they purchased, which is enough to meet operational costs and some profit. This target may be revised from time to time. The objective of pricing is also known as pricing for profit.
- **Market share:** The target share of the market and the expected sales are the most important consideration in pricing the products. Sometimes a company may lower the prices, in comparison to the competitors' products, with the intention to increase its market share. By reducing the price customers get the benefit. The management can compare the present market share with the past market share and can know well whether the market share is going up or coming down. When the price is lowered, the profit may come down but the sales will increase as more customers may buy the product. This way the company will also not lose but rather gain ultimately.
- **To meet or prevent competition:** The pricing objective may be to meet or prevent competition. While fixing the price, the price of similar products, produced by the same company, will have to be considered. At the time of introduction of new products to the market, a low price is likely to attract customers, and can establish a good market share. The low price policy discourages the competitors.

- **Profit maximization:** Business is run with the idea of earning profit at the maximum. The aim should be to maximize profits on total output, rather than on every item.
- **Stabilize price:** It is a long term objective and aims at preventing frequent changes in price. It also prevents price war among the competitors. When the price changes often, customers start losing confidence in the product. The prices are determined in such a way that they do not fall below a particular level and also do not go up beyond a certain level. The aim is to live and let live. The companies remain satisfied with small profits during periods of short supply of products.
- **Customers' ability to pay:** The prices that are charged quite often differ from person to person, according to his ability to pay. For example, several doctors charge fees for their services according to the paying ability of the patient.

6.4.2 Procedure for price determination

Every business organization follows its own policy in determining the prices of its products. However, the following steps may generally be followed:

- **Determining demand for the product:** There is a relation between the price charged and the resulting demand i.e. normally higher the price, lower the demand. First it is to be determined whether there is a price which the market expects, and second, to estimate the sales volume at different prices. Comparison of the prices of rival products is a good guide in pricing products. In certain cases, business enterprises conduct regular surveys of buyers, retailers, and wholesalers etc. to determine the expected price.
- **Predict and analyze the competitive reaction:** The competitors can influence the price. To predict the reactions of the competitors, it is necessary to collect information about their product, cost, market share etc.
- **Establish expected market share:** A business enterprise must decide the share of the market at the expected price. Low priced products may get a large share of the market, and a high priced product may get a small share of the market. Share of the market is also decided by factors such as existing production capacity, cost of plant extension etc.
- **Select pricing strategy:** One strategy is to charge high initial price of the product, at the time of introduction of the product in the market. Manufacturers aim at profit maximization in the shortest period, when the market conditions are also favourable. The price is brought down when competitors enter the market. The other strategy is to keep a low introductory price to get a large market share. Here the aim is to catch the major share of the market.
- **Setting the price:** After studying and analyzing the above factors different companies may decide the prices of their products. They may also revise their prices from time to time keeping in mind the demand and market share for their products.

7 Credit control and discounts

7.1 Introduction

In the modern world of commerce, an increasingly high proportion of sales are made 'on credit,' that is, the customer does not pay for the goods or services received at the time of receiving them. Such sales are called 'credit sales.' Vendors are said to 'extend credit' to their customers or clients.

7.2 Importance of allowing credit

Many companies benefit if they allow credit facility to buyers. First of all, the number of customers increases – thus increasing the volume of sales. Those who could not afford to buy certain products for lack of the availability of cash are now able to do so because of credit facility. This is particularly beneficial to sellers of high value items like cars, TV, fridge etc.

The wholesalers and retailers – who themselves get credit from manufacturers/distributors – are able to recover at least a larger part of the cost of goods before they have to pay because of the volume of sales.

7.3 Effect of allowing credit on demand

When people are able to buy increased number of products because of credit facility, it leads to larger demand for a variety of products. This often happens with regard to certain items like laptops, iPads, TVs, automobiles, and many more such items. Large demand for a product leads to increased sales.

7.4 Forms of credit

Given below are some of the most common forms of credit used in modern business:

7.4.1 Monthly account

A customer might be allowed to purchase goods and/or services without paying at the time of receipt, but the total value of what was received must be paid at the end of the month concerned, or within a certain period in the following month. This form of credit is very commonly allowed to 'known' customers, and it is also used in many countries by service and utility organizations to charge customers for telephone calls, electricity, gas, water, etc.

7.4.2 Fixed periods of credit

The customer must pay for the goods or services received on a fixed period after the date on which they were received. "30 days' credit" is very common. In some cases "60 days' credit," "90 days' credit" or even "120 days' of credit" might be allowed.

7.4.3 Budget accounts

This form of credit is used particularly by some chains of clothing stores. Basically, a customer must make a regular monthly payment of an agreed amount, in exchange for which he might purchase on credit goods worth, say, 20 times the monthly payment.

7.4.4 Credit cards

These are issued by banks and credit card companies like American Express and Diners Club. Most business enterprises accept these cards in lieu of cash payment.

7.4.5 Debit cards

Debit cards issued by banks to their account holders are accepted by business enterprises in lieu of cash. Since the volume of a transaction undertaken with the card is immediately 'debited' to – that is, paid out from – the customer's bank account, it is not a true form of credit. However, the use of a debit card avoids the customer having to carry cash for making purchases.

7.5 Dangers in allowing credit

Despite the advantages of credit, a business enterprise must never overlook the fact that the unwise allowing of credit or 'extended' credit can be damaging to that business for the following reasons:

- An organization or a person to whom credit has been allowed might not pay in due course for the goods or services provided.
- Most businesses have to operate on the basis that sufficient income will be received, on a more or less continuous 'cycle,' to meet all the expenses they must incur (and to produce a profit). If, because lengthy credit periods have been allowed, a business must pay its own expenses well before receiving payment for goods/services sold, it could find itself with cash-flow problems and with a shortage of working capital.

7.6 Principles of credit control

It is necessary that before allowing credit to its customers a business house should decide its credit policy. A credit limit needs to be set for each customer regarding the maximum amount, and the period of time. However, if the creditworthiness of a customer increases over a period of time, his/her credit limits may also be increased.

After the decision on credit limits has been taken, the sales personnel of a business must have up to date knowledge regarding the credit limits set for each customer, and must comply with them. Whenever a customer is nearing the credit limit the accounts department must inform the sales personnel of the situation. The sales personnel must obtain the approval of the management before allowing credit facility to a new customer.

A check on the creditworthiness of a new customer is necessary. As far as the existing customers are concerned, it can be based on their payment history. More caution is needed in respect of new customers before they can be allowed to buy on credit. This could be done by getting a bank reference from the customer, and also trade references – which means the business houses which have extended and are still extending credit to this customer.

7.7 Discounts

A discount is a reduction in the price of an item or service. Commonly, but not always, it is stated as a percentage, for example, 5%, 10%, 25% etc.

Discounts are offered for a number of different reasons, and in a number of different circumstances. Some of the most common are given below:

7.7.1 Trade discount

In many countries manufacturers recommend the prices at which their products should be sold to consumers – the 'recommended retail price' (RRP) or the 'maximum retail price' (MRP). Generally manufacturers, producers, suppliers etc allow a reduction from the RRP (or MRP) to customers buying from them in large quantity for resale, and who will sell the items – probably in smaller quantities – to their customers. This type of reduction is generally called the 'trade discount.'

The size of trade discounts allowed might vary from one manufacturer to another and between one wholesaler and another. However, trade discount is allowed to enable a trade distributor to meet its distribution expenses and after having met them – to achieve a net profit from its trading activities.

7.7.2 Quantity discount

This is offered to encourage a customer to purchase at one time a larger quantity of a particular item than he might otherwise purchase at that time.

Frequently – but not always – quantity discount is offered on a 'sliding scale;' the percentage discount increases as the quantity purchased increases. For example, a particular item might normally sell at $25. However, a customer (whether a wholesaler, a retailer or a consumer) might, for example, be offered:

- 2½% discount if 10 of the item are purchased at one time;
- 5% if 20 of the item are purchased at one time;
- 10% if 50 or more of the item are purchased at one time.

Quantity discount must not be confused with trade discount. They are allowed for two quite different reasons:

- Trade discount is allowed only to those who are buying for resale.
- Quantity discount might be offered even by a retailer to a customer to encourage him/her to buy a larger quantity at one time.

7.7.3 Cash discount

This is offered to persuade a customer to buy at once and/or to pay in cash at once. Cash discount can be offered in many different circumstances and members of a sales team must know exactly what those circumstances are, and what discount, if any, they may offer. A common use of this type of discount is in retail outlets.

In some cases businesses might also offer a cash discount to persuade a customer to pay in currency notes or by cheque instead of by credit card (the seller might have to wait for some time for the payment if it is made by credit card).

7.7.4 Regular custom discount

It is offered to induce a customer to continue to purchase regularly from the vendor concerned, and to dissuade him from buying from competitors. Generally a fixed percentage discount, say 5% or 10%, is allowed from the value of every purchase made by the customer concerned.

7.7.5 Prompt payment discount

It is offered to persuade a customer who has been sold goods on credit to settle the debt earlier than agreed.

8 Management of personnel

8.1 Human resource

The 'human resource' of an organization is composed of all the efforts, skills or capabilities of all the people who work for that organization. Some organizations may call this 'human resource' as 'staff' or 'workforce' or 'personnel' or 'employees,' but the basic meaning remains the same. All those who work for an organization are workers. However, the organizations may call those who do manual work as 'workers' and describe others who do non-manual work as 'staff.' The executives of an organization are supposed to manage its human resource in the most effective manner so that personnel work well in the best interests of the organization, and in their own interest, too. For this purpose, it is essential that good personnel relations are established with the entire workforce.

8.2 Recruitment of personnel

The term 'recruitment' refers to the first stages in the process of filling of vacancies in an organization. These vacancies may arise on account of the following:

- **Creation of a new position:** It may be necessary because of increase in the work load of existing employees or the general expansion of the organization. First, HR department will have to analyze whether it is not possible for the existing workers to share additional work.
- **Resignation/termination of an existing employee:** First HR department will have to decide whether it is necessary to fill this vacancy. It may be possible to distribute the work of this employee among the existing ones. It may be an opportunity to re-design the work allotment to various existing employees.

8.2.1 Internal recruitment

A vacancy may be filled by a person who is already working in the organization in another position, section, or department. This may provide an opportunity for transfer or promotion to an existing employee who might be interested in this position. The advantages of such internal transfer or promotion are:

- Employees are aware that hard work may be rewarded through promotion. This leads to greater job satisfaction among the employees.
- The skills and potential of internal candidates are already known to the manager, and so it may be easy to transfer/promote such an employee without going through the whole process of recruitment.
- Employees who have already been promoted have a good knowledge about the work and the organization. Hence the induction and training period for such employees may be shorter than for new comers.

However, there might be certain disadvantages of internal recruitment such as:

- The organization will lose the opportunity of getting employees – particularly at managerial level – who might bring with them new ideas and innovations.
- Other employees – who are not considered – may develop feelings of jealousy and resentment and may not cooperate with this employee.

In order to overcome these disadvantages the management must ensure that:

- Details of vacancies are circulated to all;
- Selection is to be made in a fair and impartial way;
- Selection should be based on merit and performance.

8.2.2 External recruitment

This involves the filling of a vacancy from a source outside the organization. These sources may include the following:

- Local schools
- Colleges, technical colleges and universities
- Employment agencies

- Recruitment consultants
- Advertisements in newspapers
- Posting on recruitment websites

8.3 Recruitment process

Before a decision about recruitment is made, it is necessary to ensure that the various aspects of a potential recruitment have been considered. For this purpose, various steps will have to be taken.

8.3.1 Job analysis

Job analysis is the process by means of which a description is developed of the present methods and procedures of doing a job, physical conditions in which the job is done, relation of the job to other jobs and other conditions of employment. Job analysis is intended to reveal what is actually done as opposed to what should be done. Therefore, if an employee is found doing some activity not required of that job, it should still form part of the job analysis.

The nature of job changes over a period of time. New developments take place. New personnel are employed. All this necessitates that jobs are reviewed and analyzed to suit the changed circumstances.

Any job comprises a number of tasks. Some of these require special skill, knowledge, and training. Other tasks might be easier. In order to describe a job it is necessary first to analyze it. This is done to find out the following things about the job:

- What different tasks are to be performed – whether it is single task or a small number of multiple tasks?
- How the different tasks are to be performed. It means the procedures to perform these tasks in the best possible way.
- What qualifications (education, training, skills etc.) and personal qualities (good eyesight, good hearing, pleasant voice etc.) should be possessed by the candidate.
- For what and to whom the candidate will be responsible.

The purpose of job analysis is not to describe an ideal but show the management how at the moment the constituent parts of its business are being carried out. Job analysis enables the HR department to compare different jobs. This will provide information about the status of various jobs as well as for job evaluation and in training. The information concerning the job can be obtained from a number of sources such as observation of workers, interviews, questionnaire responses, bulletins etc., knowledge of the materials of work and actual performance of work. It has been found that questionnaire is well suited for clerical workers and interviewing is suited for shop-floor workers. Working conditions and hazards are better described when viewed by the analyst.

8.3.2 Job description

The results of job analysis are set down in job description. It defines a particular job. Writing job descriptions for production workers, clerical people and first line supervisors is a fairly established practice. The two types of job descriptions differ from each other in the following manner:

- The lower level job descriptions are generally written by the HR department, but the managerial job descriptions are written by the incumbent executive himself and/or his superior.
- The lower level job descriptions are written for wage and salary administration and so centre directly on tangible duties and day-to-day assignments i.e. the tasks to be performed. On the other hand, descriptions for higher level jobs are more closely related to organization planning and so naturally are descriptions of intangible relationships, overall responsibilities and lines of authority i.e. the results to be achieved by the person.

A job description describes a particular job. It states the purpose of a job and its relation with other jobs and people. A job description contains the following:

- Job title, section or department, and details of the workgroup.
- Objectives of the job, for example, for the post of supervisor of customer service section: "*To ensure that the complaints and queries of customers are promptly attended to.*"
- List of duties.
- Responsibilities – for what and to whom the person will be responsible.
- Information about the relationship with people connected with the job – both inside and outside the organization.
- Information about the work environment – private office or open-plan office.
- Details about hours of work, paid holidays, sick leave etc.
- Details about salary, overtime, bonus, and such other benefits.

Job description gives detailed information about the job, and even enables a candidate to make a decision whether he/she wants to take up the job. It also prepares him/her to perform duties with full understanding and without any doubts.

8.3.3 Employee specifications

Employee specification gives details about the personal qualities desirable for a candidate to possess. It helps the organization to decide whether a particular candidate is suitable for the job. It seeks the following details:

- Physical qualities – age, general health etc.
- Mental qualities – alertness, patience etc.
- Skills – IT applications, technical knowledge etc. (as per the type of job).
- Qualifications – education, experience, training etc.
- Personality – reliable, honest, hardworking, pleasant etc.

Through employee specifications the HR department is able to decide whether the candidate is fit – physically, mentally, skill and qualification wise – for the job he/she has applied for. It will also show the candidate's ability to work as a productive member of the team.

8.3.4 Attracting suitable applicants

After the relevant job analysis, job description and employee specification have been completed, the HR department is ready to take steps to attract suitable candidates to apply for the job. For this purpose, the advertisement has to be posted with all relevant details as given below:

- Full name of the organization, its physical address, and the nature of its activities;
- Job title and its objectives;
- Details of important tasks involved;
- Important personal qualities required;
- Information on salary and other benefits;
- Information on how to apply, and what documents are to be attached with the application.

8.4 Selection

Once the applications have been received, the information about the applicants is compared with the requirements for the position applications have been called for. The applicants, who fulfill the criteria, are short-listed and invited to attend a personal interview.

8.4.1 Employment interviews

- **System of interviews:** An interview is a face-to-face meeting and discussion between an applicant and the employer's representative. Depending on the type of post, interview can be conducted by a single manager – usually HR manager – or HR manager and the manager of the department for which interviews are being conducted. For managerial positions there is a panel of interviewers including HR manager, Departmental manager, one of the top managers, and an internal/external interview specialist.
- **Aim of interviews:** The aims of an employment interview are the following:
  - To confirm the information already provided by the applicant;
  - To enable interviewers to compare in detail each applicant's personal characteristics with those provided in the application form;
  - To enable interviewers to assess the applicant's behaviour, mannerisms, alertness etc.;
  - To enable the applicants to seek relevant information about the job and the organization as a whole;
  - To enable the interviewers to short-list the most suitable candidates from among those who attended the interview.

- **Conduct of employment interviews:** In order to ensure that the interview process is successful, it is necessary to have proper planning and preparation for the same. The following planning and preparation helps the interviewers:
  - Each interviewer should go through the job description and employee specification before conducting the interview.

- Each interviewer should make notes about the relevant details of the applicants, and should also make a note of the additional information he/she wants to gather. Different interviewers on the panel may have a different order of important information they would like to seek.
- All the interviewers should decide the order of topics to be covered during the interview so that duplication of questions from different interviewers may be avoided. However, there should be scope for flexibility depending on the varying personalities and skills of candidates.

- **Conducting interviews for best results:**
  - Interviewers must understand that some candidates may be shy or nervous at the beginning of the interview. They need to be made comfortable by starting the interview with general conversation such as the time taken to reach the venue of the interview, their mode of transport, their place of residence etc. As a matter of fact, this process should start from the time they report for the interview. They need to be greeted in a friendly way by the secretary or the receptionist, and if they have to wait for some time in the case of several candidates attending the interview, by offering them a glass of water or a cup of tea/coffee etc.
  - The room in which the interview is conducted should be comfortable and quiet i.e. away from computer printers, telephones ringing. This will ensure that there is no disturbance during the interview process.
  - The interviewers should greet them pleasantly by standing up and shaking hands, or by making some friendly and pleasant comments etc.
  - For best results candidates should be encouraged to talk and give information without frequent interruptions. The interviewers need to talk less. The focus should be on the candidate speaking.
  - If a candidate gives a wrong answer to a specific question, the interviewer should never point out the mistake. Rather supplementary questions may be asked, or the topic may be changed.
  - Some interviewers are in the habit of 'showing off' in front of other panel members and start a lecture on a certain topic. This is absolutely unacceptable. It is the candidate who is being interviewed and not the interviewer.
  - Before the interview is brought to a close, the interviewer should be certain that all relevant questions have been asked. At this stage, the candidate should be given an opportunity to seek information about the job and the organization, and clear and precise answers are to be given.
  - Finally, the candidate should be told when he/she can expect to learn the result of the interview, and should leave the interview room in a pleasant and positive frame of mind.

8.4.2 Selection tests

For some posts certain tests might be used to supplement – but not to replace – the interview. Some tests are fairly straightforward, such as:

- **Work tests:** They are designed to check if a candidate is as skillful as he/she has claimed. For example, a secretary may be asked to type a letter, or a driver to drive a motor vehicle, or a fork-lift operator to drive and maneuver a vehicle.
- **Aptitude tests:** They are designed to show skill of doing simple tasks.
- **Intelligence tests:** They are designed to test reasoning ability.
- **Personality tests:** They are designed to indicate the possession or lack of certain character traits.

8.4.3 Appointment

After the selection has been made, the most suitable candidate (or candidates if there are more vacancies) should preferably be informed by telephone, and then a written confirmation is to be sent. This letter should contain all the relevant details such as post, date of joining, and the official to whom the candidate should report. The appointment letter should contain, or be accompanied by particulars of the 'terms and conditions of employment,' such as hours of work, starting salary, other benefits, and perhaps even a copy of the relevant job description.

The decision to appoint must be communicated as early as possible because a candidate might have accepted appointment elsewhere if there is a long time gap between the interview and the offer of appointment. Moreover, if the candidate, who is number one on the list, is not available, there is time to offer the post to the candidate next on the selected list.

8.4.4 Dealing with unsuccessful candidates

Candidates who have been unsuccessful at the interview should be informed accordingly as early as possible by tactfully worded letters, which would ease disappointment and avoid upsetting the recipients.

However, although a candidate was not found the most suitable for a particular job, it might be that the person concerned could be suitable for a similar or another post in future. It is, therefore, useful to retain on the file applications (along with relevant interview notes etc.) of those candidates, so that if suitable vacancies arise in the future, the relevant candidates can be contacted.

8.4.5 The trial or probationary period

It is quite common for people to be offered a post on condition that they will work an initial 'trial' or 'probationary' period. This period might be one month, three months or even longer, depending on the seniority of the post or on the amount of training necessary so that the work can be performed to the required standard.

The probationary period allows the employer to assess whether the candidate selected is actually suitable in real-life work situation. At the same time, this period allows the new employee time in which to decide whether he/she will be happy working for the organization.

At the end of the probationary period the new employee might be called for a talk with the departmental or HR manager during which reports on progress made can be discussed. If both the parties are satisfied, the employee is 'confirmed' in the post, otherwise he/she needs to be informed and the employment can be terminated.

8.5 Induction, training and development

8.5.1 Meaning and purpose of induction

The process of induction is meant to induct a new employee into the new social setting of his/her work. The new employee is introduced to his/her job situation and informed about the rules, working conditions, privileges and activities and other particulars pertaining to the organization.

It is important to give the new employee a good impression on the first day of work. However, the induction programme should not end there. It is also important to have a systematic induction programme, spread over several days, to cover all the ground in the shortest effective time.

Most of the information is likely to be contained in a handbook which is distributed to all employees, and in the case of rank and file workers, the induction programme may consist of brief explanation by a member of the HR department or the supervisor under whom the employee will work.

In the case of supervisory and management employees, induction training may be more elaborate. Some organizations show movies explaining their activities. Others arrange for lectures and presentations on the organization and its practices. In some organizations the new recruits spend anywhere from a day to several months in each department to gain first-hand experience in various types of work.

8.5.2 Effective induction programme

In some organizations, the induction programme is divided into phases. In the first phase, the induction is generally done by a member of the HR department who informs the new employee particulars relating to the organization. In the second phase, induction is done by the supervisor of the department in which the new employee is going to work. He/she informs the new comer about his/her job, duties, responsibilities, importance of his/her job in relation to other jobs etc. Further, he/she is introduced to the rest of the work team.

The induction programme should be drawn up in consultation with all those involved. Depending on the size and complexity of the business, this may include:

- Senior management
- Supervisors or line managers
- HR officials
- Health and Safety managers
- Employee or trade union representatives

8.5.3 What induction programme involves

Induction usually involves the new employees meeting and listening to different people talk about various aspects of the business. Other methods include written information, audio-visual aids and group discussion.

The following items are generally covered in the induction programme:

- Introduction to the business/department and its personnel/management structure
- Layout of buildings (factory/offices)
- Terms and conditions of employment
- Relevant personnel policies, such as training, promotion, health and safety
- Business rules and procedures
- Arrangement for employee involvement and communication
- Welfare and employee benefits and facilities

8.5.4 Follow-up

An informal 'follow-up' talk between the section/department manager and the new employee during the first few weeks could be advantageous as it would remove any doubts and misunderstandings the employee may have. It will also ensure that the manager concerned is able to spot any errors or deficiencies in the new employee's work and correct them immediately. He/she may also give practical help and advice. This is likely to result in establishing a good working relationship between the manager and the new employee – thus ensuring efficiency and productivity of the new employee for the benefit of the organization.

8.6 Training and development

After the candidates have been selected for various jobs, and induction programme has been completed, there is need for the management to provide for their training and development. This is because the efficiency of an organization depends greatly on the training and development of personnel. Particularly these days, when the process and techniques of management have become quite complicated, there is a great need in management for arranging training and development of its personnel.

Generally, the terms 'training' and 'development' are used as though they are synonymous. However, there are differences in the contexts and techniques of employee training and development. Training is the act of increasing the knowledge and skills of an employee for doing a particular job. It imparts specific skills for specific purposes. It is mainly job-oriented. Training is given to both old and new employees throughout their stay in the organization. In contrast, development includes the process by which managers and executives acquire not only skills and competency in their present jobs but also capacities for future managerial positions.

8.7 Employee counseling

Situations which can lead to disciplinary action may be avoided by taking certain steps. This involves having a talk with the employee concerned, trying to find a solution to the problem which is creating such a situation. This process of settling problems without resorting to disciplinary action is referred to as employee counseling.

8.7.1 Nature of problems

Some problems are related to work while others are of personal nature. Generally a manager or supervisor is concerned with the employee's work-related problems, but sometimes he/she may have to deal with an employee's personal problem also because that may have been the cause of starting a work-related problem.

8.7.2 Solving the problems

- Solution to a problem can be found only through a joint discussion between the manager and his/her subordinate. This needs to be a two-way process. Sometimes a manager or supervisor arranges a counseling session, but sometimes it is initiated by the employee when he/she needs to share some problem.
- It is important that the manager or supervisor keeps the information related to an employee's counseling session confidential from other employees.
- Every problem that needs to be addressed through counseling is individual in nature. Hence for each problem the manager or supervisor has to adopt a flexible approach and not try to fix every problem with the same solution.

8.7.3 Process of successful counseling

A counseling session is likely to be successful if the following points are considered:

- The subject for discussion should be introduced in a discrete manner and not done openly.
- The reasons for the discussion should be explained to the employee in a sympathetic manner so that he/she has confidence to discuss the matter further.
- Questions should be asked in a gentle manner so that the subordinate is able to appreciate how the manager or supervisor is trying to help him/her.
- Quite often all the questions related to the problem may not be addressed in one session. A few more sessions may be necessary in order to get all the facts right. Hence a lot of patience is to be exercised.

After the problem has been ascertained, an effort has to be made by both the parties to find a solution acceptable to both. When this happens, it is possible to have a high level of employee motivation. This is also very effective in controlling employee behaviour.

8.8 Equal Opportunity Policy

Equality in the workplace means that there is fair treatment for each individual. Everyone is supposed to have equal access to job opportunities, promotion and other benefits. It also means that there should be a system of equal pay for similar work in the organization.

There should be no discrimination on the basis of gender, race, religion or physical disability. Today a large number of organizations have a policy referring to discrimination on the above-mentioned grounds. A good equal opportunity policy includes age, marital status, gender, HIV and AIDS. The policy should state clearly a commitment to equality in the areas of recruitment, promotion, training, performance appraisal and pay, transfers, terms and conditions, disciplinary procedures and dismissal, rules against harassment etc.

Policies alone are not enough. There must be a commitment to put them into practice by specific measures, and this should be the responsibility of HR management. The policy should be publicized to all staff and job applicants.

An important part of implementing equal opportunity policy is monitoring its effectiveness. In the case of gender, race or disability, there are usually arrangements to collect statistics to ensure that these people are represented in the workforce.

8.9 Remuneration

The term 'remuneration' refers to wages, salaries, overtime payments, bonuses, commissions and any other 'financial rewards' paid to employees in return for the work they perform for their employers. It is also referred to as 'pay.'

8.9.1 Remuneration policy

Top management usually decides remuneration policy in consultation with HR manager, and if necessary, with trade union and staff association. A remuneration policy might also be affected by the following factors:

- Strength of the trade union or staff association;
- Economic climate of the country;
- Availability of labour in a particular area;
- Government policies, etc.

8.9.2 Systems of remuneration

Different employees of the same organization might be remunerated by different systems, according to the type of work they perform. The following are the most common systems of remuneration:

- **Time rates:** Under this system, payment of an agreed amount is made for agreed period of 'working time.' Time rates are mainly used when output cannot be directly related to the wage or labour cost, or when the emphasis is on the quality of work to be performed rather than on quantity alone. If the same employee works for additional hours, he/she is likely to be paid extra for the time worked in excess of the agreed number of hours at an 'overtime rate.' This overtime rate may vary from organization to organization or from one department to another.
  Other employees might be paid monthly. They include managerial and supervisory staff, clerical and secretarial staff, professional and specialist staff etc.
- **Piece work rates:** Under this system, payment is made according to the 'output,' that is, the 'quantity' of an 'acceptable quality' of an item produced.
- **Bonus:** Bonus is a reward for output or achievement above previously agreed levels. Some schemes are based on an individual's output, while others are based on the output of the group. This is usually paid at the end of the work year.
- **Incentives:** They are usually given to employees for a variety of factors such as good timekeeping, increased productivity, reducing operational costs or wastage, or involving in innovative activities.
- **Commissions or target bonuses:** The system of paying commissions generally applies to sales people, and is based on the values of sales achieved above a certain pre-determined 'target.' Some are paid on an individual salesperson's achievement, while others are based on the performance of a group, and shared out proportionately.
- **Allowances:** Depending on the nature of their work, some employees might be paid allowances, for example:
  - Cost of transport;
  - Cost of expenses incurred on entertaining existing or potential customers or clients;
  - Cost of buying and maintaining clothing and accessories;

- o Travel allowances.
- **Standard employee benefits:** In addition to salary, bonus and allowances, employees are normally provided with certain benefits. They could be of different types:
  - o **Annual paid holiday:** This is the most common benefit applicable to employees who are eligible for a certain number of holidays (or vacation) on an annual basis. During this period their normal salaries are paid to them. In some countries, the duration of this period is laid down by government rules, while in other places different organizations decide this. This paid holiday period is usually not less than 30 days for every year worked. Most organizations pay salaries in lieu of the vacation period if the management and the employee mutually agree to this.
  - o **Sickness pay:** This is also a common benefit. An employee who falls ill or sustains injury, whether in the workplace or outside, gets a recovery period "off" work during which he/she will continue to receive pay. The minimum period is laid down by law. However, some organizations may allow longer periods.

    Generally female employees are allowed a period of 'maternity' leave (before and after the birth of a child) as per government rules of the country. In some countries, fathers of newly born babies might also be allowed a period of time "off."

- **Additional (or fringe) benefits:** Some categories of employees might receive certain additional benefits which are commonly referred to as 'fringe benefits' or 'perks,' for example:
  - Company-owned motor vehicle for personal use;
  - Rent-free residential accommodation;
  - Shares of the organization;
  - Cost of meals (or on subsidized rates) in the organization's canteen;
  - Interest-free salary advance;
  - Loans;
  - Pension or superannuation funds;
  - Medical or health insurance;
  - Group life assurance;
  - Flexible working hours;
  - Working from home or other locations.

9 Stock Control and Stores Management

9.1 Introduction – Why stocks are held

Every organization finds it necessary to hold 'stocks' or 'inventory' of various items and materials. That is because it would be particularly impossible to operate with only one of each item to be sold or used in manufacturing or engineering or used in office work. A 'reserve' or 'inventory' of each item used frequently is, therefore, maintained so that as items are used they can be replaced from the stocks 'held in reserve.'

9.1.1 Stocks

The range of items (stocks) which might be held in stores is huge. The variety and quantity of items held in the stores of a particular organization will depend on its size and on its range of activities. For example, the stores of the Armed Forces may need to have a lot of items in stock.

9.1.2 Importance of store management

The success of stores management depends on its efficient management for the following reasons:

- All the possessions of an organization are called its 'assets.'

- The items in the store cost money. If through bad stores management there are too many held in the store or if the wrong items are being held, money will be 'tied up' – money which might be required to pay for other needed items.
- If poor stores management leads to shortages of needed items, there will be hold ups and interruptions. This will create problems for the organization. For example, if a particular spare part is needed to put a car back in operation, it will not be possible to do so.
- If items in the store are lost, stolen or damaged in any way, the organization loses money.
- It costs money to run the stores – on building maintenance, salaries of stores personnel, equipment, cooling, lighting, power, etc. The organization must receive a 'return' from its expenditure, in terms of efficiency.

9.2 What is involved in store management

Store management covers the actual handling of the items received into, held in and issued from the store. The work involves:

- Receiving items and material, including the inspection of them;
- Storing the various stock items in the most appropriate manner, binning and/or racking them by the best methods, and placing them in such a way that any item or material in the store can be located quickly and easily when it is required;
- Ensuring the safety of all items and materials while in store – that is, protecting them from pilfering, theft, damage and deterioration;
- Ensuring, when necessary for sending them out to another location, that items are so packed that they will not be damaged or caused to deteriorate while in transit to their destinations.

9.2.1 What is involved in stock control (inventory control)

"Stock Control" comprises mainly the clerical and administrative functions of stores work. It involves:

- Ensuring that the right types and qualities of items needed for use are always available when required;
- Ensuring that stock is issued in the correct sequence of FIFO (First In First Out), so that 'older' stock is not allowed to deteriorate by being kept too long in the store, for instance, because it has been hidden from view by more recently received stock;
- Maintaining records showing the 'movement' of items into and out of the store, controlling and monitoring those movements and maintaining full records of the items in the store;
- Ensuring that the correct 'stock levels' of the various items are set and are maintained, that orders and re-orders are made (or requested to be made) in good time, and that what is ordered is received;

- Checking, counting or otherwise measuring stock to ensure that records are accurate and that no losses are occurring due to pilfering, theft, damage or poor storage;
- Pricing and valuing the items in the store.

9.3 Relationship between stores and other departments

The function of the stores department is to provide a 'service' to the rest of the organization of which it is part. The 'service' provided by the stores department is essential to all other parts of the organization because it is basically intended:

> *"to ensure that all other sections or departments of the organization are furnished, when required, with the correct items, in the correct quantities and of the correct qualities."*

The standard of service provided by the stores department will affect the efficiency of the entire organization.

The stores department cannot be expected to provide the best service unless it receives adequate information from other departments. Furthermore, it must work closely in cooperation and coordination with those other departments.

9.4 Stock verification

The object of stock verification is to ensure that:

- All materials in stock tally with the description and specification as shown in the stock records.
- Physical balance agrees with the balance as per records.
- Excesses and deficiencies found during the verification are properly investigated, explained and accounted for.

9.4.1 Responsibility for stock verification

The stock verification will be carried out by representative of the accounts department.

9.4.2 Frequency of verification

Perpetual verification/count of stores and spares will be carried out through the year. Annual programme of verification will be prepared before the commencement of the year and got approved from the competent authority. The programme will be evenly distributed throughout the year. No item of stock will be left out of verification except for valid reasons and all such items will be taken up in earlier half for the next year's programme. Exclusion of items from a year's programme will be got approved from the competent authority.

9.4.3 Guidelines

Following guidelines are usually observed for stock verification:

- Usually one day's notice will be given to the storekeeper with regard to the stores verification.
- Normally all items in stores will be verified physically measuring, counting, etc. There may, however, be some exceptions to the general rule e.g. packages of electrical material liable to damage or certain items of ball bearing etc which have to be preserved in the manufacturer's original packing. In such case, the stock verifier will obtain a certificate from the stores officer that the quantities shown on the packages are correct.
- Stock verifier will not enter the book balances in the count sheet or the stores ledger before completion of verification of the items in question.
- He will obtain a certificate that all available stores have been presented for verification.
- Presence of storekeeper or his representative is required during stock verification. The representative of stores shall sign in token of his acceptance of verification results.
- Large discrepancies found during verification will be investigated in accordance with the prescribed procedure.

- In addition to the physical verification of stock, verifier will also look into the following:
    - o Case of errors classification i.e. items which have not been classified correctly in accordance with the codification list;
    - o Adequacy of security arrangements;
    - o Items declared surplus but not moved for one year thereafter;
    - o Unauthorized or unaccounted for stock, if any, where unaccounted material is found, proper investigation will be made to ascertain how the material found its way to the store
- Discrepancies during stock verification: The stores officer will explain the discrepancies found as shown on the count sheet within a specified period (usually one month) of receipt of each sheet from the stock verifier. While explaining the differences, following will be kept in view:
    - o Where the accounting unit is in number, there should not be any large discrepancy except where cross items are taken.
    - o In explaining the excess against one item by clubbing it with shortage against another item, only similar items are taken.
    - o With regard to weight, errors larger than 2 percent of the total transactions cannot be allowed.
- Any shrinkage of an item must be within permissible limits.

9.5 Inventory control

The objective of any inventory management system is to keep down the capital investment in inventories to the barest minimum.

9.5.1 Codification of inventory items

The stores will maintain numerical accounts for material stocked in the stores. A register will be maintained of the Index Cards which are current. Following are some guidelines for maintenance of cards:

- The cards will contain a complete record of transactions i.e. numerical account of the quantities received/issued and the closing balance, the stocking limits and the optimum order quantity.
- Normally there will be only one card for a particular material. However, more than one card can be opened for different qualities of the material.
- Normally the numerical balance on the cards will be reconciled with the corresponding price ledger balance at the end of a specified period (usually a quarter).
- For each entry on the card, there will be a corresponding voucher.
- An indent will be raised when the stock does not touch or goes below the re-order point. Consumption will be watched so that necessary changes in the stocking limit can be made.

9.5.2 Lead Time, Lead Time Usage and Safety Stocks

Lead time is the time taken in procurement of an item from the time an indent is prepared to the time the material becomes physically available for issue. To take into account the fluctuation in lead time or consumption, safety lock has to be added. It is quite possible that lead time goes up/down or the consumption varies. So it is necessary to work out the safety lock i.e. the quantity that should be added to lead time usage so as to satisfy all reasonable demands without going out of stock.

9.6 Concept of purchasing

Purchasing involves acquiring materials of right quality, at the right quantity, at the right time from a right source and at a reasonable price. A separate purchase department should be established to perform purchasing activities. The size of purchasing department depends on the quantity to be purchased regularly by the organization. The purchase department determines the quality, quantity, items, price and time of purchase of materials. The function of purchase department is to purchase materials, supplies, machines, tools, spare parts etc. at the most favourable terms and conditions in a way that helps maintain the quality.

9.6.1 Factors for purchasing

The importance of purchasing in any organization is largely determined by four factors: availability of materials, absolute dollar volume of purchases, percent of product cost represented by materials, and the types of materials purchased. Purchasing must concern itself with whether or not the materials used by the organization are readily available in a competitive market. Perhaps the most important of the four factors is the amount of control purchasing and supply personnel actually have over materials availability, quality, costs, and services. Large organizations tend to use a wide range of materials, yielding a greater chance that price and service arrangements can be influenced significantly by creative purchasing performance.

9.6.2 Supply sourcing

Part of sourcing decision involves finding qualified suppliers who are willing to make and sell the product under the specified conditions.

Buyers have a number of places to go to locate sources of supply, some obvious and some indirect. The most obvious sources would include Yellow Pages, other purchasing departments, and direct marketing. Other sources of supply include manufacturer directories and trade registers. Practically every purchasing department has access to this source, either through the book or CD-ROMs.

Suppliers may also be found at trade exhibits, in supplier catalogues, or via recommendations from other knowledgeable sources, such as sales personnel and engineers. Probably the most important and frequently used source is the Internet.

Many organizations find themselves in a situation where a suitable supplier cannot be found. In this situation, the organization is forced to develop a supplier. Supplier development is sometimes referred to as 'reverse marketing,' which entails finding the supplier with the most potential for success and providing the required resources.

When the product being purchased is fairly standard and readily available, most organizations choose to utilize the competitive bidding process of supplier selection. This involves little or no negotiation. A request for bids is sent to a limited number of qualified suppliers asking for a price quote for the product, given the terms and conditions of the contract. The contract generally goes to the lowest bidder. For government bid requests, the contract legally must go to the lowest bidder qualified to fulfill the contract.

9.6.3 Supplier management

After locating proper suppliers and securing contracts, it then falls to the purchasing function to monitor and control the suppliers' performance until the contracts are fulfilled, if further business is to be conducted. All purchasing organizations need some method for assessing supplier performance. Many organizations have formal supplier-evaluation programmes that effectively monitor supplier performance in a number of areas, including quality, quantity delivery, on-time delivery, early delivery, cost, and intangibles.

For some organizations, consistent supplier performance results in certification. Supplier certification generally implies (or in some cases formally asserts) that the supplier has been a part of a formal education programme, has demonstrated commitment of quality and delivery, and has proven consistency in his processes. Frequently, organizations are able to take delivery from certified suppliers and completely bypass the receiving inspection process.

The buyer is also responsible for maintaining a congenial relationship with the suppliers. If the buyer is an unreasonable negotiator, and does not allow the supplier to make an adequate profit, future dealings may be engendered. The supplier may refuse to deal with the buyer in the future, or the supplier may greatly increase the price of a product the buyer could not obtain elsewhere. Also, relations can become strained when the buyer consistently asks for favoured treatment such as expediting or constantly changing a particular order's delivery schedule.

9.7 Purchasing methods

The purchase is made through any of the following methods:

- **Purchase through open tenders:** Open tender is invited for all purchases costing more than a pre-determined amount except for items for which the organization may decide otherwise.
- **Purchase through limited tenders:** Unless otherwise decided by the organization, a limited enquiry to the registered/approved suppliers is issued only in respect of supplies costing not more than a pre-determined amount, or when open tendering has been dispensed with. Enquiries/Tender Documents are issued per registered post or in person to those firms which are registered in respect of material sought to be purchased.
- **Purchase through single tender:** Except for an item, which the organization may specifically reserve for purchase from a particular supplier, no purchase is to be made on a single tender by selecting any particular supplier, even if he is a registered/approved supplier.
- **Petty cash purchases:** Petty purchases, not exceeding a pre-determined amount on each occasion, may be made on cash and carry basis after ascertaining the lowest rates and recording a certificate to this effect. Payments in respect of such petty purchases are made available with the purchasing authority.

- **Bulk purchasing:** Bulk purchasing is the purchase of much larger quantities than the usual, for a unit price that is lower than the usual. Wholesale is selling goods in tremendous quantities at a low unit price to retail merchants. The wholesaler will accept lower sales price for each unit, if the retailer will agree to purchase a much greater quantity of units, so the wholesaler can maximize his profit. A wholesaler usually represents a factory where goods are produced. The factory owners can use Economy of Scale to increase profit as quantities sold go up.
- **Economic Order Quantity (EOQ):** In this method, our interest is on the raw material that we are going to use in the production. However, we need to do the EOQ method for each kind of raw material, if the product needs multiple materials to be manufactured. Usually, this type of analysis is one shot method. It is so because the period we are planning to order for is long (the assumption is that the period is non-ending).

10 Sales and marketing

10.1 Importance of salesmanship

The actual process of selling is generally called 'salesmanship.' In some situations the physical presence of sales personnel is essential for a selling transaction to take place, while in other circumstances the 'salesmanship' might take the form of the skillful advertising or publicity, or even attractive well-planned window displays or an attractive website.

The great majority of businesses –whether they are involved in industrial, trading or service-provision – require skilled sales personnel.

10.1.1 The selling task

Selling is the need of the sellers. It is the internal aim of business. It is only a part of marketing strategy. Marketing is much wider than selling and much more dynamic. Selling revolves around the needs and interests of the seller. Marketing revolves around the needs and interests of the buyer. Selling seeks profit by 'pushing' the products on the buyer. Marketing too seeks profits, but not through 'pushing' the products but by meeting the needs of the customers and by creating value satisfaction for them. A truly marketing-minded company tries to create value-satisfying goods and services which the consumers want to buy. What it offers for sale is determined not by the seller but by the buyer. Selling is certainly a part of marketing. That is the last function in the process of marketing.

10.2 Sales and marketing management

The range of duties and responsibilities of the person designated to manage the selling activities of a particular business will naturally depend to a large extent on its size, what type of business it is, the range of products with which it deals, and so on. However, in general they are likely to include some or all of the following:

- Establishing and ensuring the smooth functioning of the most suitable channels of distribution for the products of the business;
- Market research, sales forecasting, budgeting and planning;
- Advertising, publicity and sales promotion;
- Recruitment, selection, induction, training and control of the sales team;
- Maintaining sales records and controlling the sales office.

10.3 Sales promotion campaigns

Promotion refers to the activities to push forward or to advance an idea, in such a way as to gain its approval and acceptance. Promotion is telling and selling. Sales are the life-blood of business. Tough competition has increased the importance of sales promotion efforts on the part of the producers and sellers. Thus, sales promotion means all the steps that are taken for the purpose of increasing sales. Promotional activity is basically an exercise in communication. Communication is very essential. For example, we have the best products with good package, fair price etc. The product cannot be sold to consumers unless they know about it. People must know that the right products are available at the right place and at the right price. This is the job of sales promotion.

10.3.1 Importance of sales promotion

In recent years, the importance of sales promotion has increased. It is due to the thinking of new ideas for creating a favourable condition for selling and promoting future sales. For a new product or new brand, sales promotion is very important. Sales promotion methods inform, remind or encourage the buyers at the point of purchase. A good sales promotional campaign will remove the consumers' dissatisfaction with respect to retail selling. Sales promotion increases as a result of the growing use of self-service and other sales methods.

10.3.2 Objectives of sales promotion

The main objectives of sales promotion are:

- To increase buying interest at the customer's level;
- To attract new customers;
- To inform the public about the new product and its specialties, attraction and advantages;
- To get the major share of the market;
- To create a good impression about the product;
- To meet the competition of other companies;
- To effect off-season sales to increase sales;
- To encourage the demand by popularizing the products;
- To keep the memory about the product alive;
- To create brand image;
- To remove customers' dissatisfaction;
- To bridge the gap between advertising and personal selling.

10.4 Types of sales promotion

10.4.1 Window displays and interior displays

It is the silent sales person that attracts the buyers' attention to the product and makes them decide to buy. Promotion at the point of purchase is very effective. Proper display of products is done by all – manufacturers, distributors, retailers. It varies widely. For example, showrooms and shops selling automobiles, garments, cosmetics, health products etc. attract the customers towards their products. Display helps the consumers examine the product and make buying decision. Thus display provides the maximum effectiveness.

10.4.2 Consumer sales promotion

It is aimed to inform or educate the consumers and to encourage them to buy certain products. Consumer sales promotion increases the use of the product by the consumers, and attracts new customers. The following are the various sales promotion schemes:

- **Sampling:** Free samples are given to consumers to increase their interest in the product. They are also given to introduce a new product and increase the market share. It increases the sales volume when the product is a new one to the customers. It is an effective method when the product is purchased often e.g. soaps, detergents, tea, coffee etc. It is a method of demand creation. Sampling gives a chance to the consumers to compare certain products with others. Samples may be delivered door to door, sent by mail, picked up in a store, attached to another product etc. It is the most effective way to introduce a new product.
- **Coupons:** Coupons are supplied along with a product. They can be mailed, enclosed in the packets or provided in the advertisements. The purpose is to attract the customers and bring them to a particular shop to increase the sales of a particular brand.
- **Demonstrations:** It is a promotional tool to attract the attention of customers. When products are of a complex and technical nature, demonstration is necessary e.g. computers, software, field machinery etc. Demonstration is also done in front of customers for goods such as mixer, grinder, in retail shops.
- **Contests:** These are conducted to attract new customers or to introduce new products. The customers are asked to state in a few words why they prefer a particular product. To participate in the contest, the customers must purchase a product and submit the evidence (a label of package or a card attached to the product) with the entry form for the contest. Consumers' skill and their ideas are tested and the prize is given to the best entry. It encourages sales at the retail level.
- **Money refund offers:** If the purchaser is not satisfied with the product, a part or all of the purchaser's money will be refunded. It is stated on the package. It will create new users and strengthen brand loyalty. Sometimes, the money will be refunded if 10 top covers or empty bottles or packages are sent back to the manufacturer/retailer.

- **Premium offer:** It is a temporary price reduction which encourages the buyers. Products are offered at a reduced price to encourage purchasing. It is offered to consumers mainly for consumer goods like soap, brush, toothpaste, washing powder, soft drinks, milk cartons etc. For example, when the customer buys two pieces of soap, a soap box is given free. The soap box is the premium. In certain cases, the price is reduced. The reduced price is the premium.
- **Price off offer:** It encourages sales during the period when the sales are quite low. It gives a temporary discount to the consumers i.e. goods are offered at a price lower than the printed price. For example, fans and air-conditioners may be sold at reduced price during winter.
- **Consumer raffle draw:** Retailers give tickets or coupons to the customers on the purchase of goods for a certain amount. At the specified time, lots are drawn, and the prizes given.
- **Free trial:** Customers are invited to try the product without cost, in the hope that they will buy the product. Thus buyers are encouraged by free trial to create interest in purchase.

10.5 Advertising

In the modern business world, suitable publicity is done through advertising, which is adopted by almost all types of companies. Some or all of the following media of advertising may be used:

- **Indoor advertising:** The following are the methods of indoor advertising:
  - Press – newspaper, magazine
  - Radio
  - Television
  - Film
  - Text messages on mobile phone
  - Telemarketing
- **Outdoor advertising:** Outdoor advertising passes the message to those people who are the moving audience. Following are the various types of outdoor advertising.
  - Posters
  - Billboards
  - Tickers
  - Sandwich men (dressed in fancy clothes)
  - Handbills (leaflets)
  - Display on vehicles
- **Direct advertising:** The objective of direct advertising is to create a direct contact with the customers. It may be of the following types:
  - Sales letters
  - Booklets and catalogues
  - Folders
  - Package inserts
  - Store publications

10.6 The sales team

The personal qualities sought in members of a sales team will vary on the posts, the products to be sold, and the methods by which they are to be sold; some products, for instance, require a degree of 'technical knowledge' by sales personnel attempting to sell them. Some posts require a bright, cheerful disposition, others perhaps a more sober disposition, and so on.

Suitable specific training needs to be organized for various categories of sales personnel. There is considerable difference in the training requirements of 'sales assistants' who will be required to sell from shops, showrooms, stores, etc., and those of 'commercial travellers' or 'sales representatives' who will be out in the field.

11 Production management and Industrial administration

11.1 What production involves

In general usage, the word 'production' refers to the making of things from raw and/or processed materials, or the assembly of items which have already been through a process of 'production.' The basic objective of production is the conversion of the materials and/or components into more useful and saleable forms.

11.2 Factors for efficient production

The management of a business enterprise must consider the following factors before efficient and profitable production can commence.

11.2.1 The market

Before embarking on production, management must be sure that a market for the products exists or can be created. Market research is essential, to discover the extent and size of the potential market, the existing or potential competition which will be faced by the 'new' products, and of course what prices potential customers will be prepared, or can afford, to pay.

11.2.2 Design and technical considerations

The design of products will need a careful planning, as will the methods of production to be employed. The two matters are interrelated, and there must be coordination between the design and technical functions.

11.2.3 Production resources

All the necessary resources for efficient production must be available. They will include capital, adequate supply of materials/components, the right plant and equipment, skilled manpower etc.

11.2.4 Support services

The management must ensure that the production department gets assistance and services from other sections or departments, such as purchasing, stores, accounts, administration, personnel, sales etc.

11.3 Production policy

Once the objective has been decided upon – in this case to manufacture a product or a range of products – basic policies must be laid down as to how that objective is to be achieved. The production policy formulated must incorporate how production will be carried out, that is, the methods of production, and the quantities of different products to be manufactured. The production policy laid down for a particular business might have to take account of some or all of the following factors.

11.3.1 Product range

It is important for a business to get 'right' the range of products which it produces. In general, a degree of specialization is necessary, and smaller manufacturing businesses usually concentrate on a relatively narrow range of products. It makes sense for them to do so because:

- Of the experience they build up in manufacturing and marketing those products;
- The variety of plant and machinery required will be limited;
- The most efficient processes will have – or should have – been deployed;
- Finding, training and retaining the skilled labour needed.

11.3.2 Production levels

There are factors which limit the extent of the activities of a business, particularly (a) the demand for its products, and (b) its production capacity. Other 'limiting factors' might include shortages of manpower (skilled workers in particular), shortages of or delays in obtaining raw materials and/or components, inadequate storage or production space, insufficient capital, and so on.

Another factor which might influence production levels is the 'cost per unit' at different levels of production. The purpose of a costing system is to analyze in detail the expenditure of a business and then to allocate it in such a way that the cost of each job, product, contract or process carried out is revealed. Note the following:

- **Cost:** This refers to all the expenditure which can properly be allocated as having been incurred in the production and/or distribution of a specific article, or in the provision of a specific service, or in carrying out a contract, or in performing a job.
- **Unit:** Depending on circumstances and on the activities of a particular enterprise, a 'unit' can refer to a specific article produced and/or sold, or to a process or a service, a contract or a job, or to a section or a department of the enterprise.
- **Prime cost:** This comprises the values of all expenses (e.g. materials, components, labour, power etc.) which can be identified as being chargeable directly to the unit being cost, whatever that unit consists of.
- **On cost (commonly called 'overheads'):** This refers to the total of the expenditure which has to be incurred by an enterprise in the course of its activities but which cannot be related to any specific unit. Examples can include office rent and salaries, and general expenses and many others, all of which constitute 'indirect' expenditure.

11.3.3 Financial considerations

Most businesses have to undertake production in advance of sales and the receipt of income there from. It is therefore essential that sufficient finance – working capital – is available to meet all production expenses until such time as income is generated from the sale of the results of that production.

11.3.4 Expansion

Many businesses need to expand – either by increasing production of existing products, or by diversification – in order to survive. Management must ensure that its own expertise and techniques are adequate to the new problems which are likely to arise as a result of increasing production or venturing into new areas of production and new markets.

11.4 Methods of production

The method which will be selected for the production of a particular product will depend on the nature of that product and on the quantity of it to be produced. Methods or types of production can be broadly classified into the following.

11.4.1 Job production

This type is used for single products – often called 'one-off' – or a small number of identical products, which are made to the specifications of a particular customer. Basically it involves the bringing together of all the necessary materials, components and parts in order to fabricate, assemble and commission a single item or a system; examples include the building of a ship or a bridge, or the development of a software program.

11.4.2 Batch production

This type is employed when a limited quantity of a product is to be produced at one time, the final quantity of which is known in advance i.e. before production commences.

11.4.3 Flow or Continuous production

This method is employed in large scale or mass production on a continuous basis, in which all the operations are performed continuously without a break. This is the assembly line or conveyor belt system, and examples include the mass production of motor vehicles, DVD players, televisions, electrical and household appliances etc.

11.5 Factory location, planning and layout

While selecting the site for a factory or workshop, the following factors should be considered.

11.5.1 General area

The area selected should be suitable from the points of view of:

- Convenience in obtaining the raw materials and/or components which are necessary in the production processes.
- Ease of access for transport delivering raw materials/components and collecting finished products for business.
- The area should be well served by the necessary 'utilities,' such as electricity, water, and telecommunication etc.
- There should be a sufficient supply of labour of the required calibers: skilled, semi-skilled and unskilled, as needed.
- The attitude of the local authorities towards a particular business is also significant. In some cases local authorities encourage industry in their areas.

11.5.2 The Site

The following factors are to be considered:

- Good access for transport.
- The site should be large enough not only for the factory or workshop itself but also for all the support services like stores, office, parking etc.

11.5.3 The building

The type of building required or available might, of course, have a considerable bearing on the area and site, so all three might be interrelated. When possible and practicable, it is logical that the largest available 'open' area should be used for the major processing stage e.g. the machine shop. The other processes, sections or departments should then – as far as the shape and size of the building permit – be logically positioned near to it and to each other.

11.5.4 Positioning of machinery

In job and batch production, machines should be grouped together according to their functions, regardless of the products being manufactured; this is often called ‘process layout.’ On the other hand, for flow or continuous production, machinery should be positioned to coincide with the sequence of processes to ensure the minimum of movement between the ‘raw materials stage’ and the finished product; this is commonly called ‘product layout.’

11.5.5 Machinery, plant and equipment

What machinery, plant and equipment will be required and used by a particular manufacturer will depend on many different factors: the natures and quantities of products manufactured, the methods of production employed, whether the production processes are ‘labour intensive’ or are ‘machine intensive,’ what is available in the country concerned, and the finance available.

11.6 Materials handling

The term ‘materials handling’ embraces all the activities involved in the movement, handling and storing of materials and items. Efficient and economical materials handling is essential not only for the smooth running of the production department, but also in the stores department. Frequently the materials handling systems required for efficiency in production must be coordinated with the stores; materials might have to be transported from their storage areas to the production area, moved through the production processes, returned to the stores (in a different form from that in which they left) and eventually be distributed. Any interruption to or hold-up in the smooth flow of materials can cause severe problems for some or all of the stores, production and sales departments.

11.6.1 Safety

The materials handling system employed must be safe and must reduce to a minimum the possibilities of accidents occurring which can result in injury to personnel and damage to equipment and materials.

Adequate training in the use of equipment is essential, and applies equally to both manual and powered handling equipment (as well as to all other production machinery and equipment). It is not sufficient to merely teach a person how to operate a particular piece of equipment. He/she must be taught to do so in the most efficient and careful manner and the need to take safety precautions at all times must be clearly understood and appreciated.

11.7 Production planning and control

The twin functions of planning and control of production are closely related, and are frequently the responsibility of one section or department. What is called the 'preplanning stage' covers matters relating to what products are to be produced and the designs of those products, the sizes of output to be aimed at, budgeted costs, selling prices, delivery times etc. Thereafter, 'planning' is required to ensure the most effective and economical coordination of materials, labour and machines, that is, to ensure that the right materials, men and materials are in the right places in the right quantities at the right times.

Control is defined as *"that function which checks that what was planned to happen **does** happen."* Production control therefore requires that standards are set and targets are established, and that actual performances are compared with them on a regular basis, and that any necessary corrective action is taken without delay should performance deviate from the plans or standards.

11.7.1 Progress control

This is necessary to ensure that production performances conform to the time-schedules. It involves a continuous check on production progress, determining the reasons for any deviation from the time-schedules, resolving the problem or removing the course of it, if necessary adjusting materials deliveries and advising the sales department of any changes in planned delivery times or dates.

11.7.2 Inspection

This is essential to ensure that finished products attain the laid down standards. At the same time it should be designed to reduce or eliminate waste, whether of materials, components or finished products.

The most common types of inspection include the following:

- **Raw materials inspection** – to ensure that they conform to the specified standards.
- **Work in progress inspection** – this comprises a series of checks which are carried out at various stages of the production processes.
- **Quality control** – the inspection of the final product to ensure that it complies with the set standards.

11.7.3 Work study

This is concerned with examining all aspects of production work, and is carried out with the object of improving efficiency and reducing wasted effort, both of which will result in improved productivity. There are two areas of work study:

- **Motion study:** Its aim is to find – from detailed study of what is currently being done – ways of reducing time-wasting movement, for example, by locating tools or materials more conveniently for a machine operator.
- **Work measurement:** It is concerned with measuring the time taken to perform the various activities involved in a task and by adding up the various times, arriving at the total time taken to perform the whole task. Work measurement seeks to determine how long a certain job should take a qualified and experienced worker to perform, and the results can be used in setting performance standards.

11.7.4 Costing

The data contained in the final accounts can be used as a basis for analyses, calculations and deductions. Nevertheless, the final accounts do not themselves tell management exactly how much it costs to run a particular section or department of the business, or exactly how much it costs to run a particular section or department of the business, or exactly how much it costs to produce and/or sell a specific product or group of products. The provision of that information is the function of costing, or cost accounting. In addition, a well-designed costing system is the most valuable tool of management (in particular the management of an industrial enterprise) in the following areas:

- **Costs** – control can be exercised over all costs.
- **Stocks** – control can be exercised over all stocks.
- **Policy formulation/decision-making** can be based on accurate and reliable data regarding the operations of the enterprise.
- **Estimating and tendering** will be based on accurate data showing, for example, the 'real' cost of producing an article or of performing a job.
- **Selling prices** can be fixed with precision because they will be based on accurate information. By showing the composition of the total cost of an item, costing figures can indicate how its selling price should be adjusted to meet changing circumstances.
- **'Loss' areas** will be revealed i.e. activities which are inefficient or areas which are wasteful of materials, labour, machine-time, tools or equipment.
- **Budgetary control** is facilitated because anticipated costs can be calculated more accurately, and actual expenditure can be compared with forecasts, at the same time permitting any variations to be investigated fully.

12 Financial accounting

12.1 Need

Many businesses suffer because their owners or managements do not pay sufficient attention to financial accounting. Complete and accurate accounting records, information from which can be presented – in a summarized form – in various 'financial statements,' can provide a wealth of valuable data for management.

It is compulsory for every business to keep records of its business transactions. In order to do this a bookkeeper is needed to assist in recording the financial transactions of the business. The process involves the use of a computerized accounting system or it can be done manually.

12.2 Bookkeeping

Bookkeeping involves recording, analyzing and totaling of mercantile transactions with a view to showing the records of every transaction which occurs. This transaction refers to any activity which has a monetary value. It may be sale of goods or services, settlement of debt, or receipt or payment of money. Accounting has to be done for all such transactions.

12.2.1 Purpose

The overall purpose of bookkeeping is to ensure that the financial transactions of the business are accurately recorded so that informed economic decisions can be made about the allocation of various resources. This financial information can be used to meet many objectives: monitor receivables to ensure that payment is received on a timely basis, monitor payables to avoid interruptions in the business' supply channels, ensure that funds are available when expensive assets need to be replaced, quantify the effect of price changes on total revenues, get a better feel for the true cost of the products and services they sell, and much more.

12.3 Principles of bookkeeping

There are five basic principles of bookkeeping:

- **Principle of double entry:** Each transaction is entered twice in the book of accounts. For every debit entry there must be a corresponding credit entry.
- **Principle of recording:** All accounting entries emanate from a source document. This is the authority for entry into journals.
- **Principle of profit determination:** The life of a business is divided into time periods. Revenue and expenses from those periods can be matched to determine whether a profit or loss has been obtained.
- **Principle of reporting:** Accounting information is to be conveyed to a person without accounting knowledge in a clear, logical and understandable form.
- **Principle of control:** Accountants and bookkeepers must be constantly alert to ensure that the accounting practices minimize the chances of error and fraud.

In simple terms, the main reasons for bookkeeping are:

- To keep records of income and expenditure so that the profit or loss during a period of time can be easily worked out;
- To keep a record of assets and liabilities so that the financial situation of the business can be worked out at any time.

12.4 Books of account

In large companies business transactions are directly recorded in computer systems. In most countries bookkeeping is done as per 'double entry bookkeeping' rules. When this is done manually, information is recorded in actual 'books of account.' In this system, transactions are first recorded in the 'day books' which are also called 'books of original entry.' From these different 'day books' information is transferred to the ledger in a summarized form.

12.4.1 The ledger

The ledger is the main book of account. We can get the following information from the ledger:

- Total income of the enterprise, and sources of income;
- Amount spent on each expense, and total expenditure;
- Total value of assets and value of each asset;
- Total value of liabilities and value of each liability;
- Details of debtors and the amount owed to the enterprise;
- Details of creditors and the amount;
- Details of profit and loss made.

The ledger is not one account but rather a collection of accounts. Each account is meant to record details of a person, organization, type/source of income and expenditure. Each account can be distinguished by its separate account number or folio.

12.4.2 The cash book

Records of all receipts and payments (including bank accounts) are made in this book. This information comes from cash sales bills and vouchers, cash purchase bills, cash payments, cheque payments, bank pay-in-slips etc.

Though the cash book is a part of the ledger, it is maintained separately. A cash book is actually on two pages – left-hand side records debits, and the right-hand side records credits.

12.4.3 The sales book

The details of credit sales – for which payment has not been received at the time of sale – are recorded in the sales book. Entries in the sales book are made from copies of invoices issued to the customers. These invoices contain information about the goods or services supplied – quantity, description, price, charges such as shipping and transport, applicable government taxes, discounts etc.

12.4.4 The purchase book

Details of purchases of current assets are recorded in the purchase book. They include raw materials, component parts, goods for reselling etc. Information for these entries is obtained from the invoices raised by the suppliers of various items.

12.4.5 The returns inwards book

Sometimes goods sold are returned by the customers for various reasons – wrong delivery, damaged goods etc. Entries about such returns and credit notes issued to the customers are recorded in this book.

12.4.6 The returns outwards book

Sometimes the enterprise returns some goods to its suppliers for various reasons. Entries about such returns and credit notes issued by the suppliers are recorded in this book.

12.4.7 The journal

This book records only the unusual transactions, for example, equipment or vehicles or any other fixed asset purchased on hire-purchase terms. The journal is also used for making 'opening entries' while opening a new set of account books. It is also used for making 'adjustments' for making correction in wrongly-made entries. The journal also records 'closing entries' at the end of the financial year, for example, for transferring some amounts from ledger accounts to profit and loss account.

12.4.8 End of year financial accounts

The end-of-year financial accounts are the basis of financial situation of the business. In addition, they form the basis of income tax and are often the basis of bonus plans for employees. Dividends are also calculated from year-end figures, and budgets for upcoming years are dependent on the operating results of the current year.

- **Manufacturing account:** Business enterprises need to know what it costs to produce their goods. This information is the basis for making several decisions (including having reasonably accurate end-of-year accounts). Manufacturing activities are closely related to trading activities. Hence both Manufacturing Account and Trading Account have a connection. Based on the final figures in Trading Account and the cost of production as shown in Manufacturing Account, a business enterprise can decide whether it is profitable to continue producing the current products. In a manufacturing enterprise the prime cost consists of the following:
    - Opening stock of raw materials
    - Work in progress
    - Value of materials purchased
    - Wages and salaries
    - Rents and rates
    - Transport and other miscellaneous expenses

  The cost of producing goods is derived at by calculating the difference between:
        - Value of stocks at the end, and
        - Value of work in progress.

- **Trading account:** Most of the enterprises are involved in trading or distribution of products or services, for example, hypermarkets, shopping malls etc. They buy goods at wholesale prices and resell them at retail prices. These goods are sold at a price higher than at what they are purchased. The resultant margin is the reseller's profit.
  In a trading enterprise, the prime cost consists of:
    - Value of opening stock,
    - Net value of purchases during the period,
    - Warehouse expenses, and
    - Shipping and taxation.

  Considering the above, a Trading Account can have either gross profit or gross loss.

- **Profit and loss account:** The profit and loss account shows the profit or loss for the period. It is usually headed "for the year ended………" It includes:
    - Revenues, and
    - Expenses of the business for the relevant period.

  The difference between revenues and expenses is referred to as the net profit/loss. Some organizations – particularly non-profit organizations – refer to this figure as the net surplus/deficit.

  Net profit/loss is defined as:

Net profit/loss = revenues – expenses

Revenues are inflows derived by the enterprise as a result of the sale of goods or provision of services. Revenues typically include sales, interest received, rent received, dividends received, etc. Another term for revenue is income.

Expenses are day-to-day outflows incurred by the business in providing goods or services to customers. Expenses typically include advertising, accounting fees, bank charges, cleaning, electricity, interest paid, motor vehicle expenses, postage, printing and stationery, rent, salaries and wages, superannuation, telephone etc.

- **The balance sheet:** Though the Balance Sheet is not an account, it is included in the final end-of-year accounts. It is rather a statement showing the financial position of the enterprise on a given date. Hence it does not have a debit and credit side. It shows Assets and Liabilities, which can be recorded either in the horizontal or the vertical format.
  The Balance Sheet reports the enterprise's assets, liabilities, and equity:
  - **Assets:** Assets are defined as future economic benefits owned or controlled by the enterprise. Assets are essentially anything owned by the enterprise that is valuable and contributes to revenue generation. Assets include cash at bank, accounts receivable, inventory, land and building, and plant and equipment. Assets are usually classified as either current or fixed assets. If an asset is expected to be 'realized' (or converted into cash) within the next 12 months, it is classified as a current asset. On the other hand, if an asset is not expected to be converted into cash within the next 12 months, it is classified as a fixed asset in the balance sheet.
  - **Liabilities:** Liabilities are amounts owed by the enterprise to outside parties. They include bank overdrafts, accounts payable, tax liabilities and loans payable etc. Liabilities are classified as current or fixed. If it is expected to be settled within the next 12 months, it is classified as current liability; otherwise it is classified as a fixed liability.
  - **Equity:** Equity is generally made up of Capital, Revenue Profits (or accumulated losses), and Reserves. Equity represents the investments made by the owners of the enterprise and the sum of accumulated profits made over the years.

13 Office organization and control

13.1 Introduction

In business 'the office' is a section or department of an enterprise delegated the responsibility for performing certain important functions and providing certain essential services for the business as a whole.

13.2 Functions of the office

The office of any business is basically concerned with information – which is often called 'data.' Its activities can be broadly divided into:

- Gathering, receiving and recording information;
- Collating the information collected, analyzing it and presenting it in the formats required;
- Storing the information e.g. filing it or recording it on computer, so that it is readily available when required;
- Communicating the information, in the formats required to those people who need it.

Information will be received both from within the business and from external sources, and similarly will have to be communicated to destinations both within the business and outside it. If the office is to play its full 'service role,' it must be well organized and staffed, and must be provided with adequate machines and equipment.

13.2.1 Centralization and decentralization of offices

Smaller businesses, in particular, will have just one 'central office,' perhaps quite small, to provide the clerical and/or secretarial services required by all employees, sections or departments, as appropriate. Complete centralization of all office activities might not always be possible, particularly in larger businesses, because to a certain extent the clerical requirements of different departments might be specific to them, for example invoicing might need to be done in the sales department or the accounts department, stock records might need to be maintained in the stores department, personnel records will have to be available in the personnel department, and so on. For such reasons some office services might have to be decentralized while other, more commonly required, services might be centralized.

13.3 Office location and layout

Exactly where an office will be located in relation to other departments of a business will depend on a number of factors, not the least on the type and size of the business, the nature of its activities, the premises from which it operates, the space available within those premises, and so on.

13.3.1 Multi-room layout

This form of layout comprises two or more rooms, which might be located on two or more floors of a building, or even different buildings. This layout is common in particular in businesses which have grown over a period of time, and the corresponding increase in the demands on the office have necessitated the allocation of more space, wherever it has been available at the time; alternatively it may have been brought about by decentralization.

13.3.2 Open-plan layout

This basically comprises one large room in which a fairly large number of clerical and/or secretarial staff works. The room might be divided into 'sections' by the use of partitions, which might be no more than a metre high, and which might be made wholly or partly of glass. Supervision of personnel working in the room should be easier, and fewer supervisors might be necessary. In addition, it is usually easier to rearrange workload in the event of absences due to holidays or illnesses, during particularly busy times, or while some staff members are overloaded while others have little to do.

13.3.3 Combinations of layouts

Both types of layout described above might be necessary in many businesses; some sections might be multi-room while others might be open-plan, depending on the work performed in the different sections. However, whenever circumstances permit, the layout of the office, or different sections of it, should be designed to encourage the most efficient performance of the work to be carried out in it.

13.4 Planning the office layout

The following are some of the important matters to be taken into consideration when planning the layout of an office, or when redesigning the layout of the existing one:

- Avoiding overcrowding;
- Minimization of staff movement;
- Minimizing noise distractions;
- Suitable lighting;
- Ventilation;
- Heating/cooling;
- Toilets and cloakrooms;
- Adequate supervision;
- Prevention of accidents.

13.5 The office environment

A clean and neat office will go a long way towards encouraging efficient and accurate work to be performed in it. There should be ease of access for cleaning purpose, and suitable cleaning materials and, if necessary, equipment such as vacuum cleaners, should be provided. Part of the training of office personnel should be the necessity for neatness and tidiness; if they leave their desks tidy at the end of the working day in particular cleaning will be easier, and there will be less chance of documents and other items being jumbled together, misplaced or disposed of in error by cleaners.

13.5.1 Office furniture and fittings

Considerable variations will be found between the furniture and furnishings provided for the office of different businesses, and often also between that provided for different sections or clerical centres of the same business. In general the guiding factor should be 'utility;' the furniture provided should be the most suitable for the performance of the type(s) of work involved. In practice, that factor might be tempered by other considerations, for example:

- **Cost:** New modern furniture can be very expensive. Smaller businesses could purchase second-hand furniture.
- **Image:** Businesses which cater for and aim to attract affluent customers might need to provide expensive furniture and luxurious furnishings
- **Status:** Supervisors and managers might expect to be provided with better quality furniture and furnishings than are provided for their subordinates.
- **Standardization:** Although the foregoing factors might dictate otherwise, there can be advantages in the standardization of the types, colours and styles of desks, tables and chairs, as standardization will minimize the factors of jealousy and friction.

13.5.2 Office machinery and equipment

The range of office machinery and equipment available today is greater than at any time in the past, and new and/or improved models are constantly being introduced on to the market.

Most offices require to be provided with a variety of different machines and pieces of equipment. Some will be 'standard' items, perhaps relatively inexpensive, such as staplers, paper punches and calculators, while others might be more expensive but still of 'general' use, such as photocopiers, intercoms, and filing equipment. Yet other items might be more 'specialized' and be used only by certain sections or clerical centres of the office: examples include franking machines, fax machines, duplicators, and/or printing machines, and of course computers.

The very general rule should be to provide an office, or section of it, with the most suitable machinery and equipment which it really needs to perform its functions efficiently within the financial resources of the business.

13.5.3 Computerization

Almost all the businesses today are established with a computer system as a 'central' or 'core' component. The system originally installed is likely to be changed, modified, upgraded or expanded as circumstances and requirements change.

It is advisable to invest in a good computer system, install the software packages as required for the business, have a suitable capacity server, and a reliable network security system. This is necessary because almost all the business is done today using the Internet and various software programs such as finance, marketing, inventory control, communication etc.

14 References

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