NAAC ACCREDITED

तेजस्वि नावधीतमस्तु

ISO 9001:2008 & 14001:2004

FAIRFIELD

Institute of Management & Technology

'A' Grade Institute by DHE, Govt. of NCT Delhi and Approved by the Bar Council of India and NCTE

Reference Material for Three Years

Bachelor of Commerce (Hons.)

Code : 888

Semester- V

FIMT Campus, Kapashera, New Delhi-110037, Phones : 011-25063208/09/10/11, 25066256/ 57/58/59/60

Fax : 011-250 63212 Mob. : 09312352942, 09811568155 E-mail : fimtoffice@gmail.com Website : www.fimt-ggsipu.org

INDEX

Three Years Bachelor of Commerce (Hons.)

Code: 888

Semester – V

INCOME TAX LAW & PRACTICE (301)

INTRODUCTION TO INCOME TAX ACT 1961

Income tax is direct tax which is imposed upon income of the person. It is major source of income of central Government. Income tax is computed on accrued or received net taxable income by person during a previous year according to prescribed rate of income tax in current assessment year.

PREVIOUS YEAR- (sec.3) A previous year is that year in which income is earned and received. Previous year may be prior to assessment year and it may be for 12 month or less than 12 month. For ex.- previous year for assessment year 2018-19 is 2017-18.

In case of newly established business first previous year start from the day of setting of the business and end on 31st march of next year.

In case of undisclosed income, year in which the income arised will be previous year. If such year is not known , year in which such income comes to knowledge of IT department will be the previous year.

ASSESSMENT YEAR- sec. 2(9) current financial year is called assessment year, it start from 1st of April and end to 31st of March next year. Tax of any person is computed in assessment year for income earned in previous year. It means in assessment 2017-18 tax is computed for income earned in previous year 2016-17.

PERSON- sec. 2(31) According to income tax act 1961 person includes following-

1. individual
2. Hindu Undivided Family (HUF)
3. Company
4. firm
5. An association of person / Body of individual
6. Local Authority
7. Any artificial juridical person

ASSESSEE - sec.2(7) According to income tax act 1961, the following are included in term of Assessee

1. The person who is liable to pay tax
2. The person who is liable to pay penalty and interest along with tax.
3. The person upon whom the proceeding of assessment is started.
4. Deemed Assessee.

GROSS TOTAL INCOME- Gross total income of an assessee means the total income before deductions under sec. 80C TO 80U. if assessee has taxable income under only one head, then only that income under one head will be treated as GROSS TOTAL INCOME. GTI includes-

1. Income from salary
2. Income from House property
3. Income from business or profession
4. Income from capital gain

5. Income from other sources

TOTAL INCOME - the income which come after deducting deduction under sec. 80C TO 80U, is called TOTAL INCOME. It is also known as NET TAXABLE INCOME and income tax computed on this income.

INCOME IN WHICH TAX TO BE PAID IN SAME ASSESMENT YEAR IN WHICH IT EARNED-

1. Income from shipping business of non resident (SEC. 173)
2. Income of person leaving India.(SEC. 174)
3. AOP & BOI formed for a particular event or purpose .(SEC. 174A)
4. Income of person from transfer of property to avoid tax.(SEC.175)
5. Income of discontinued business.(SEC.176)

AGRICULTURE INCOME- sec. 2(1A)- following income covered under agriculture income –

1. Rent or revenue derived from land used for agriculture purpose, and land must situated in India.
2. Any income derived from cultivator or receiver of rent in kind of employing.
3. Income arised from farm building .

NON –AGRICULTURE INCOME – following income regarded as non agriculture income

1. Income from land used for properties or as bricks fields
2. Income from land used as stone quarries.
3. Income from fisheries
4. Income from water supply for irrigation purpose
5. Income from land let for storing crops or timber.

PARTLY AGRICULTURE AND PARTLY NON AGRICULTURE INCOME-

If an income comprises of both agriculture and non-agriculture income in such a case it become necessary on the part of assesse to segregate the income into two components – agriculture income and non- agriculture income.

Q. from the following information compute agriculture income and business income –

Sale of sugar- -24,00,000. Manufacturing exp. including depreciation – 6,00,000, cost of sugarcane – 5,00,000, market value of sugarcane- 15,00,000 , cultivation exp. 4,20,000.

TAX TREATMENT OF AGRICULTURE INCOME-

Agriculture income is exempt from tax but it shall be included in the total income in case of certain assesse for the purpose of determining the rate of tax on the non- agriculture income. This is also known as integration of agriculture income with non-agriculture income or the indirect way the taxing the agriculture income.

Integration of agriculture income with non-agriculture income shall be done in case of individual, HUF, AOP, BOI &artificial juridical person, it shall not be done in case of firm, company, co-operative society and local authority .

Integration of agriculture income with non-agriculture shall be done in the following 2 cases only-

1. Net agriculture income exceeds the maximum amount not charged to tax
2. Net agriculture income exceeds 5000 p.a

STEPS TO CALCULATE TAX-

1. Add net agriculture and non-agriculture income and calculate tax on it.
2. Add net agriculture income with maximum amount that is not chargeable to tax and calculate tax on it.
3. Deduct tax calculate in step no.2 from step no. 1 (tax on step 1- tax on step 2)

RESIDTENIAL STATUS OF AN INDIVIDUAL-

An individual is said to be resident in India if he satisfied any one of the basic condition-

1. He should be in India for 182 days or more during previous year.
2. He should be in India for 60 days or more in previous year and 365 days in preceeding four previous year. However in the following cases only first condition should be satisfied.

1. A person of Indian origin who visit India during previous year.
2. A person leave India for employment purpose and crew members.

If a person is resident in India than either he is resident and ordinary resident or resident but not ordinary resident, its depend upon additional conditions.

If he satisfied both additional condition than he is said to be resident and ordinary resident otherwise resident but not ordinary resident.

ADDITIONAL CONDITION

1. He should be resident in 2 year out of 10 previous year.
2. He should be 730 days in India during 7 year preceeding the previous year.

INCIDENCE OF TAX AS PER RESIDENTIAL STATUS

Types of income	ROR	NOR	NR
Income received or deemed to be received in India whether earned in India or outside India.	YES	YES	YES
Income earn in India whether received outside India.	YES	YES	YES
Income earned outside India ,received outside India but business controlled from India.	YES	YES	NO
Income earned outside India , received outside India but bring India during previous year from any other sources.	YES	NO	NO
Past untaxed income brought to India	NO	NO	NO

INCOME UNDER THE HEAD SALARY (UNIT 2)

Basis of charge (sec. 15)

1. Income under the head salary is taxable only if there is employer-employee relationship.
2. Salary is taxable on receipt or due basis whichever is earlier.
3. Arrear of salary, not charged to tax in an earlier previous year, are taxable in the previous year in which it is paid.
4. If any salary paid in advance is included in the total income of previous year, it shall not be included again in the total income when salary become due.
5. Any salary, bonus etc. by whatever name is called received by a partner from the firm shall not be regarded as salary.
6. Advance salary is taxable ,but advance against salary is not taxable(loan from employer)

Grade system-

Q. compute taxable salary for A/Y 16-17.

1. 10.000-2,000-14,000-3,000-20,000 he was appointed from 1-7-13.

Parts of salary- basically salary divided into following parts

1. Allowances
2. Perquisites
3. Retirement benefit**.**

Allowances- monetary benefit given by employer to employee is called allowance.it is divided in to different types.

1. Following allowance are exempt to the extent of amount received or amount spent whichever is less:-

a. Travelling allowance
b. Daily allowance
c. Conveyance allowance
d. Helper allowance
e. Academic allowance
f. Uniform allowance

2. Following allowance are exempt to the extent of amount received orlimit specified whichever is less:-

a. Children education allowance- Rs. 100 p.m per child up to 2 child.
b. Hostel expenditure allowance- Rs. 300 p.m per child up to 2 child.
c. Transport allowance- (Rs. 3200p.m for blind and handicapped).
d. Allowance to transport employee- 70% of allowance or 6000 p.m whichever is less.
e. Tribal area allowance- Rs. 200 p.m.
f. Underground allowance- Rs. 800 p.m.
g. Border area allowance- 200 to 1300 p.m
h. Hill compensatory allowance- 300 p.m to 7,000 p.m

3. **Following allowance are fully taxable :-**

a. Dearness allowance
b. City compensatory allowance
c. Medical allowance
d. Family allowance
e. Non practicing allowance
f. Warden allowance
g. Telephone allowance
h. Lunch allowance

4. Allowance exempt for certain person only-

a. Citizen of India who is gov. employee rendering service outside India. Any allowance received outside India is fully exempt.
b. All allowance received by judge of high court and supreme court.
c. Allowance received by employee of UNO.
d. Daily AND constituency allowance received by MPs and MLAs exempt.

5. **House rent allowance**- least of following is exempt-

a. Actual amount received
b. Rent paid less 10% of salary.
c. 50% of salary for metro city and 40% for other city.

Note – salary means, basic salary plus D.A plus commissions

PERQUISITES

Non- monetary benefit given by employer to employee is called perquisites. There are following types of perquisites-

Rent free accommodation:-

1. For govt. employee- it is decided as per gov. rule, generally it is exempt.
2. For other employee-

a. Accommodation is owned by employer- in this case taxability is depend upon population of the city, if population of city is more than *25 lakhs than 15% of salary* is taxable and for more than *10 lakhs butup to 25 lakhs 10% of salary* and if population is less than *10 lakhs7.5% of salary is taxable.*

b. Accommodation is not owned by employer- in this case *15% of salaryor actual rent paid* by employer *whichever is less* taxable.

c. Accommodation is provided in hotel- *24% of salary or actual charge* paid by employer whichever is less taxable. However nothing shall be taxable if accommodation is provided for not more than 15 days and on transfer of employee from one place to another.

Notes: –

1. Salary means- basic salary plus D.A plus bonus plus commission plus all taxable allowance.

2. If furniture is also provided with house then 10% of cost of furniture or actual hire charges if taken on rent, shall be added with taxable amount of RFA.
3. In case of transfer of employee from one place to another place, employee is provided house at new place as well as retain house at old place than for first 90 days one house with lower value is taxable but after 90 days both house is taxable.
4. If RFA is provided in remote area or mining sites or onshore oil exploration site then nothing shall be taxable.
5. If any amount is recovered from employee in behalf of RFA than such amount should be deducted from total taxable amount of RFA.

Value of interest free loan:-

If any interest free loan or loan at concessional rate is provided from employer to employee than ,value of benefit derived from such loan is taxable in hand of employee. For calculation of benefit rate of interest charged by SBI in previous is taken. However nothing shall be taxable if amount of loan do not exceed Rs. 20,000 or loan is provided for treatment of specified diseases.

Use and transfer of movable assets:-

If any movable assets is provided by employer to employee for use than 10% p.a of the actual cost or hire charges is taxable in hand of employee. If assets is transferred to employee than any benefit from such transfer is also taxable in hand of employee. For calculation of such benefit following depreciation is taken-

a. Computer & electronic item- 50% on basis of WDV.
b. Motor cars - 20% on basis of WDV.
c. Any other assets - 10% on basis of SLM.

Other benefits:-

a. Sweeper, watchman, gardener or personal attendant- in all cases actual cost to employer is taxable in hand of employee.

b. Gas ,electricity or water- manufacturing cost per unit or amount paid to outside agency, shall be taxable

c. Free education facility- it is taxable if amount of benefit is exceed Rs. 1000 per child p.m for two child.

d. Credit card bill- if card is used by employee or his family for personal purpose and bill paid or reimbursed by employer than it is taxable in hand of employee. However nothing shall be taxable if it is used exclusively for official purpose.

Medical perquisites:-

1. Expenditure incurred or reimbursed on any medical treatment provided to an employee or any member of his family is fully exempt without limit, for treatment in any hospital, dispensary maintained by employer, gov. ,local authority or approved by gov. for treatment of specified disease.
2. Health insurance premium reimbursed or paid on behalf of employee or any member of his family is fully exempt.
3. Reimbursement by employer of any amount actually spent by employee for obtaining his or any member of his family treatment in any hospital other than point 1, is taxable if amount is more than Rs. 15,000.
4. If employer provided treatment in any other country than medical expenses ,expenses on stay and travel expenses with one attendant is fully exempt subject to permitted by **RBI.**

Leave travel concession:-

Any concession received by employee for himself or his family for travelling to any place in India is exempt, to the extent amount spent, subject to following condition-

1. Exemption can be claimed for two journey in a block of four year i.e 2002-05,2006-09,2010-13 and so on.
2. Exemption is available for two children but exemption will be available for all the children borne before October 1, 1998.
3. **Amount of exemption-**

a. If journey is performed by air than economy class fair with shortest route.
b. In case of rail then first class rail fare by shortest route.
c. In case of bus, first class deluxe bus fare of recognised public transport.

RETIREMENT BENEFIT

Pension:-

For taxability point of view pension divided in two types-

1. Uncommuted pension- it is taxable for all employee as salary.

2. Commuted pension- it is taxable as under-

a. For gov. employee - fully exempt.

b. For non-gov. employee - *one third of commuted value* if he received gratuity but *one half of commuted value* if he not received gratuity.

Gratuity:-

1. For gov. employee- fully exempt.

2. For non-gov. employee, covered under payment of gratuity act-

Least of the following amount

a. 15/26 days salary of every completed year of service or part thereof in excess of 6 month.

b. 20,000,00

c. Amount received.

NOTE- salary means last drawn basic salary plus D.A.

3. <u>For non gov. employee not covered under payment of gratuity act1972.</u>

Least of the following is exempt

a. 15/30 days salary for every completed year of service

b. 20,000,00

c. Amount received

NOTE- salary means average salary of last 10 months preceding the month of retirement.

<u>Compensation on voluntary retirement:-</u>

Least of the following is exempt

a. Amount received

b. 5,00,000.

<u>Condition for claiming VRS:-</u>

1. Exemption shall be allowed only to employee of central/state govt. public sector undertaking, any other statutory corporation, local authority, university, IIT OR notified institute for management.
2. Exemption shall be allowed only if compensation does not exceed three month salary for each completed year of service or salary of balance month of service left before his normal retirement.

<u>LEAVE SALARY-</u>

1. Leave encashment during continuation of service is fully taxable for all employee
2. Encashment of leave after retirement – for gov. employee fully exempt . and for other employee least of the following amount is exempt –

a. Actual amount received.

b. Maximum amount 3,00,000

c. 10 month average salary for preceding the month of retirement

d. Cash equivalent of unavail leave (unavailed leave should be calculated on the basis of 30 days leave in one year)

<u>Provident fund:-</u>

It is basically retirement benefit scheme . under the scheme employee contribute part of his/her salary and employer contribute fixed amount 10 to 12 % of salary to employee. There are following types of provident fund.

1. Statutory provident fund (SPF)
2. Recognized provident fund (RPF)
3. Unrecognized provident fund (URPF)
4. Public provident fund (PPF)

PROVISION REGARDING SPF-

This scheme is applicable for gov, semi gov. and local authority and universities employees. Any interest earned on contribution of employee and employer is fully exempt . contribution by employer is fully exempt. Contribution of employee is eligible for deduction under section 80 C.

PROVISION REGARDING RPF-

A provident scheme in which the employee provident fund and miscellaneous provision act,1952 applies is recognised provident fund. Contribution of employer is exempt up to 12% of salary and interest cr. In RPF exempt up to 9.5 % p.a. exemption u/s 80C available for employee contribution.

PROVISION REGARDING URPF-

Contribution made by employer is exempt from tax, int. cr. To the fund is also exempt at the time of credit but no exemption on employee contribution available u/s 80C. on retirement payment received which represent employee own contribution is exempt. Int. received on employee contribution is taxable under income from other sources and balance (employer contribution and int.) is taxable under the head salary.

PROVISION REGARDING PPF-

Central gov. has established the PPF for the benefit of general public to mobiles personal saving. Any member of public (whether salaried , self employed) can contribute towards PPF. Minimum contribution is 500 and maximum contribution is 1,00,000 p.a . lock in period is 15 year or more

Deductions(sec.16)

1. Professional tax- any amount paid by employee shall be allowed as deduction in the year of payment.
2. Entertainment allowance- at first this is taxable for all employee but govt. employee can claim deduction under this section which is least of the following-

a. Amount received

b. 20% of salary

c. 5000

INCOME FROM HOUSE PROPERTY

BASIS OF CHARGE(SEC.22)

1. Annual value of building and land appurtenant thereto is taxable under this head.
2. If building is occupied by assesse for his own business or profession then nothing shall be taxable.
3. Income under this head is taxable only if assesse is owner of the building.
4. Even if letting out is business of assesse, still rental income of building is taxable under head house property only.
5. However rental income is not taxable if building is letout to carry on business and in case of composite rent, if it is not separable.

DEEMED OWNER(SEC. 27)

1. In the case of transfer to spouse or minor child(not being a minor married daughter),without adequate consideration ,transferor shall be deemed owner.
2. Holder of impartiable estate is deemed as owner.
3. In case of allotment or lease ,the person to whom building has been allotted shall be deemed as owner.
4. The person who acquired house without registration .
5. The lessee of building in case building is leased out for not less than 12 year is deemed as owner.
6. In case of disputed ownership income shall be taxable in hand of recipient

METHOD OF COMPUTATION

Gross annual value ---------------------------------
Less-municipal tax paid by owner-----------------------------
Annual value (net annual value)------------------------------
Less- Deduction u/s 24--------------------------------

DEDUCTIONS (SEC.24)

1. Standard deduction- 30% of net annual value. if NAV is nil than std. deduction shall be nil.
2. Interest on borrowed capital-this deduction has two parts in the first part previous year int. is deductible and in the second part one fifth of int. on pre-construction period is deductible.

INTEREST ON LOAN FOR SELF OCCUPIED HOUSE

1. In respect of such property, int. on capital borrowed for purchase, construction, repair, renewal or reconstruction is deductible up to Rs.30, 000. however if loan is taken on or after 1-04-1999 and property is acquired and constructed within five year from end of financial year in which capital was borrowed, the total deduction of interest shall not exceed Rs. 2,00,000.
2. Deduction of Rs. 2, 00,000 shall be allowed only if assesses furnishes a certificate, from the person to whom any int. is payable on capital borrowed.

ANNUAL VALUE (SEC. 23)

CASE 1-building is let out throughout the previous year
Gross annual value of such property is expected rent or actual rent whicheveris higher. Expected rent is municipal value or fair rent whichever is higher but it cannot exceed standard rent.

CASE 2-self occupied building and building which could not occupied due to employment.
Annual value of such property is nil.

CASE 3- Deemed to be le out property

In case there is more than one house property is self occupied than except one house remaining shall be deemed to be let out at the option of assesse.

CASE 4- property which is let out but remained vacant during the whole or part of the previous year.

In this case actual rent is taken as GAV. If in the vacancy period property is self occupied than normal rule is applied for determining GAV.

UNREALISED RENT

1. If due to any reason assesse couldnot realise rent in previous year such rent is called unrealised rent.
2. Such unrealised rent should be deducted from actual rent or GAV determined.
3. If assesse recover unrealised portion of rent than it is treated as income of assesse of that previous year in which rent is realised, whether or not assesse is owner of property in that assessment year.

CAPITAL GAINS (UNIT 2)

Basis of charge (sec. 45(1))

1. Any profit or gains arising from the transfer of a capital assets, shall be chargeable to income tax under the head capital gain.
2. It shall be deemed to be the income of p/y in which transfer took place.
3. Capital gain is exempt if it is covered u/s 54, 54 B, 54D, etc.

Capital assets (sec. 2(14))

1. It means property of any kind held by assessee whether or not connected with his business or profession.

However it does not include:-

a. Stock in trade
b. Personal effects (movable property held for personal use by assessee or any member of his family but it does not include jewellery, Archaeological collections, drawing, painting ,or any work of art.)
c. Agriculture land in India not situated in urban area.
d. Gold deposit bonds issued under gold deposit scheme 1999.

Types of capital assets

There are two types of capital assets:-

1. Short term capital assets.

2. Long term capital assets.

Short term capital assets

1. A capital assets held by assessee for not more than 36 months immediately preceding the Date of transfer.
2. However in the following cases ,if period of holding is not more than 12 months immediately preceding the date of transfer, than it shall be treated as short term capital assets-

a. Share held in a co.
b. Any security listed on recognised stock exchange.
c. Unit of UTI/Mutual fund.
d. Zero coupon bond.

Long term capital assets

A capital assets which is not a short term capital assets is called long term capital assets.

Transfer

Transfer in relation to capital assets includes:-

1. Sale ,exchange or to give up or surrender of assets
2. Extinguishment of any right therein
3. Compulsory acquisition thereof under any law.
4. In case where the assets is converted into stock in trade of a business, such conversion.
5. Allowing the possession of any immovable property under transfer of property act 1882.
6. Allotment or lease under a housing building scheme of society, co. or other association.

Method of computation of capital gains

Sale consideration received/ accrued on transfer-

Less: cost of acquisition.

Less: cost of improvement.

Less: expenditure incurred wholly and exclusively in connection with transfer.

Cost of acquisition

1. It means amount which assessee has paid or incurred at the time of acquisition of assets.
2. In relation to goodwill ,tenancy right, route permit, loom hours, right to carry on business, patents, copyright or trade mark, the amount of purchase price in considered as COA. In case of self- generated , COA is nil.
3. Cost of acquisition of assets acquired before 1/4/81 is actual cost of owner or fair market value on 1/4/81 is to be taken at the option of assessee.
4. In case of LTCG, index COA is to be computed with following formula-

Cost of improvement

1. All expenditure of capital nature incurred on improvement of assets shall be treated as COI.
2. COI incurred before 1/4/81 shall be ignored in all cases.
3. In case of LTCG, index COI is to be computed with following formulA

Exemption of capital gain

Sec. 54

1. Individual and HUF are entitled to take exemption under this section.
2. If one residential house is transferred and other residential house is purchase within two year or completed construction within 3 year than capital gain invested is exempt from tax.
3. If unutilised amount is deposit in a capital gain A/C scheme up to date of furnishing return of income than such amount is also exempted.
4. Holding period of assets transferred should be minimum 3 year/1 year.
5. If new assets purchase by assessee is sold within 3 year from date of purchase/constructed than capital gain claim as exempt shall be reduced from COA of new assets.

Sec. 54B

1. Only individual can claim exemption under this section.
2. If one agriculture land is transferred and other agriculture land is purchase within two year from date of transfer than capital gain invested is exempt from tax.
3. Same as sec. 54
4. Holding period of assets transferred is 2 year or more.
5. Same as section 54.

Sec. 54D

1. All assessee is entitled to claim exemption under this section.
2. If land and building for industrial undertaking is transferred and other land and building for industrial undertaking is purchased within 3 year from such transfer than capital gain invested is exempt from tax.
3. Same as sec. 54
4. Same as sec. 54B.
5. Same as sec. 54.

Sec. 54EC

1. Same as 54D
2. Ay any assets transferred and long term specified assets (bonds of NHAI,RECI) is purchased within 6 month from date of such transfer than capital gain invested is exempt from tax.
3. Not applicable.
4. Same as sec. 54
5. If sold within 3 year of acquisition , exempted capital gain taxable as LTCG in the year of transfer of new assets.

Sec. 54F

1. Same as sec. 54.
2. If any assets other than residential house is transferred and residential house is purchase within 2 year or constructed within 3 year from date of transfer than proportionate net consideration invested is exempt from tax.
3. Same as sec. 54
4. Same as sec. 54

5. If sold within 3 year from date of purchase/construction ,capital gain exempted shall be taxable as LTCG in the year of transfer

INCOME FROM OTHER SOURCES

Basis of charge sec.56(1)

A sources of income which does not specifically fall under any one of the other four heads of income is to be computed under the head income from other sources.

Specific income sec.56(2)

1. Dividends.
2. Winnings from lotteries, crossword puzzle, races, card game, gambling or betting of any form.
3. Income from letting of furniture, machinery, plant, etc.
4. Interest on securities.
5. Sum received under keyman insurance policy including bonus.
6. Where any sum of money, the aggregate value of which exceeds 50,000. Received without consideration by any individual or HUF the whole of such sum is taxable.

Provided shall be taxable in case of gift received from any relative, or on the occasion of marriage of individual ,or under a will or by way of inheritance or from any local authority, trust,university.

NOTE- relative means:-

1. Spouse of individual
2. Brother or sister of individual
3. Brother or sister of the spouse of the individual
4. Brother or sister of either of parents of the individual.
5. Any lineal ascendant or decendant of individual.

Taxability of dividend

1. Any amount declared, distributed or paid by a domestic company by way of dividends is exempt from tax in hand of employee, because company who declared or paid dividends pay corporate dividend tax which is currently 16.2225% (15% plus surcharge @5% plus 2% education cess and @1% secondary and higher education cess.).

2. Dividend from foreign co. is taxable in hand of assesse.

3. Dividend declared or paid by UTI and mutual fund unit is also exempt.

Taxability of lotteries, puzzle game, horse race, card game

1. Any winning amount from lotteries, game, horse race is taxable in the hand of assesse with flat rate which is 30% plus education cess @ 2% and SHEC @ 1%.
2. No deduction is allowed in respect of any expenditure incurred in connection to winning such amount.

3. In case of horse race , expenses relating to activity of owning and maintaining race horse is allowed for deduction.
4. If net income (gross income minus TDS) is given in question than for computation of tax it should be GROSSING UP by use of following formula:-

Taxability of interest income

1. Income, by way of interest on securities, is chargeable under the head income from other sources if it is not chargeable under the head PGBP.
2. Interest is taxable on receipts basis if assesse follow cash basis accounting system and on due basis if no accounting system is followed.
3. In case of govt. securities there is no need for grossing up of income because it is exempt.
4. In case of interest on other securities , if NET amount is given than it should be grossed up for computation of tax

NOTE:-

1. Rate of TDS in case of saving bond is 10%.
2. Rate of TDS for non gov. securities whether listed or not is 10%.
3. In case of saving bond if interest income is more than 10,000 than TDS is deducted.
4. An case of interest on debenture ,no tax is deductible if amount of interest is less than Rs. 2500.
5. Collection charges, interest on loan, any other expenditure not being capital nature is allowed as deduction from interest income.

Taxability of income from letting of machinery , furniture, plant etc.

1. If any income earn from letting of machinery, furniture, plant and it nor chargeable under the head PGBP than it is chargeable under the head income from other sources.
2. Following expenses are allowed for deduction:-

a. Repair and insurance of machinery, plant , furniture.
b. Depreciation based on block of assets.
c. Any other expenditure which is exclusively for earning such income and not in capital nature.

Taxability of gift from unrelated person

1. Where any sum of money received by assesse which is more than 50,000 Rs. Without consideration than whole of the aggregate value is taxable in hand of recipient.
2. Where any immovable property is received by assesse without consideration which stamp duty value is exceeds RS. 50,000,THE stamp duty value of such property is taxable in hand of recipient.
3. Where any movable property is received by assesse without consideration which fair market value exceeds RS. 50,000, the whole of aggregate fair market value of such property shall be taxable.
4. Where any movable property acquired for a consideration which is less than fair market value of such property than amount exceeding RS. 50,000 the aggregate fair market value of such property as exceeds such consideration shall be taxable in the hand of recipient.

NOTE:-

1. After death of employee , if pension received by his legal heir such pension is called family pension. Family pension is considered as income of person who receive such pension and taxable under income from other sources.

2. Deduction is allowed in case of family pension which is 33.33% of pension or 15,000RS. Whichever is less.

3. Interest on post office saving bank account is exempt up to 3500 RS. For individual account and 7000 RS. For joint account.

4. Interest paid outside india on which TDS is not deducted is not allowed for deduction.

5. Interest paid on amounts borrowed for meeting tax liability is not deductible.

DEDUCTIONS

SECTION 80C

1. This deduction is available only to individual and HUF.

2. Maximum amount of deduction under this section is 1,50,000.

3. On the following amounts deduction is allowed:-

a. Life insurance premium on life of himself, spouse, and children, in HUF any member of family. Premium paid in excess of 10% of the capital sum assured shall not allowed for deduction.
b. Contribution by employee towards SPF and RPF.
c. Contribution by any person to public provident fund (PPF)
d. Subscription to national saving certificate (NSC) & national saving scheme (NSS).
e. Contribution in any unique link investment plan (ULIP).
f. Amount invested in deposit scheme of a public company engaged in infrastructure facility or approved mutual fund.
g. Repayment of loan taken from central/state govt./any other bank/LIC/National housing bank, employer where employer is statutory corporation or, public co. or university, or college or local authority or co-operative society, for purchase or construction of a residential house property.
h. Tuition fees at the time of admission or thereafter for full time education for any two children of such individual to any university, college, school or other educational institution situated in india.
i. Fixed deposit with scheduled bank for not less than five year.
j. Subscription to notified bond of NABARD (National agriculture bank of rural development)
k. Investment in sukanyasamridhi account and amount can be invested by an individual as guardian in the name of girl child who is of the age of 10 year or less. Interest received is exempt. Amount received in maturity is also exempt. Account can be closed after completion of 21 year of age . in case of marriage , payment is allowed after completion of 18 year.

SECTION 80CCC (investment in pension fund)

1. This deduction is allowed only to individual.
2. Maximum amount of deduction is 1,50,000.
3. Payment regarding annuity plan of any insurance company for receiving annuity or pension.

SECTION 80CCD

1. This deduction is allowed only to individual.
2. Maximum amount of deduction is 1,00,000.
3. Deduction in respect of contribution to pension scheme of central govt.

SECTION 80CCE

Total deduction allowed under section 80C, 80CCC, 80CCD can not exceed RS. 1,00,000.

SECTION 80D

1. This deduction is allowed only to individual and HUF.
2. Payment regarding medical insurance premium for self, spouse, dependent parents, dependent children, or any member of HUF.
3. An assessee shall be allowed deduction of RS. 15,000 (20,000 for senior citizen)or amount paid whichever is less.
4. Deduction is allowed only if payment is made any mode other than cash.

SECTION 80DD

1. This deduction is allowed only to individual and HUF.
2. Payment regarding expenditure on medical treatment , or training or deposit in a scheme for receiving annuity or lump sum amount for the benefit of disabled dependent relative or member of HUF.
3. An assessee shall be allowed deduction of RS. 50,000 irrespective of actual amount deposit or spent. In case of disability more than 80% RS. 75,000 allowed as deduction.
4. For claiming deduction a certificate issued by medical authority should be furnished alongwith return.

SECTION 80U

1. This deduction is allowed to individual who is handicapped.
2. An assessee shall be allowed deduction of fixed RS. 50,000 irrespective of amount spent, RS. 75,000 in case of disability is more than 80%.
3. For claiming deduction a certificate by medical authority should be furnish along with return.

SECTION 80DDB

1. Individual and HUF are entitled for this deduction.
2. Payment regarding actually incurred any expenditure on medical treatment of specified disease of himself or depend relative or any member of HUF.
3. An assessee shall be allowed deduction of RS. 40,000 (RS. 60,000 for senior citizen)or amount spent whichever is less.
4. Deduction shall be reduced by the amount received from insurance co. or employer.

5. For claiming deduction a certificate by specified doctor should be attached with return.

SECTION 80E

1. This deduction is allowed only for individual.
2. Payment regarding interest on loan taken for higher education of himself or spouse or children.
3. Deduction is allowed to extent of interest paid in the previous year.
4. Deduction is allowed for maximum period of 8 year starting from year in which payment of interest on loan begins.

SECTION 80G

1. Deduction under this section allowed to all assessee whether company or non company.
2. Payment regarding donation in sum of money only not in kind allowed as deduction.
3. Proof of payment should be attached with return.
4. For deduction donations are classified into various types:-

A. Donation made to following are eligible for 100% deduction without any qualifying limit-

a. National defence fund set up by central govt.
b. Prime minister national relief fund.
c. Prime minister earthquake relief fund.
d. An approved university/educational institution of national eminence. Etc….

B. Donation made to the following are eligible for 50% deduction without any qualifying limit-

a. Jawaharlal Nehru memorial fund.
b. National children fund.
c. Prime minister drought relief fund.
d. Indira Gandhi memorial trust.
e. Rajiv Gandhi foundation.

C. Donation to the following are eligible for 100% deduction subject to qualifying limit

a. Donation to govt. or any approved local authority , institution or association to be utilised for promoting family planning.
b. Donation made by company to Indian Olympic association or to any other notified institution, for development of infrastructure for sports in india.

D. Donation to the following are eligible for 50% deduction subject to qualifying limit-

a. Donation to govt. or any approved local authority , institution or association utilised for any charitable purpose other than promoting family planning.
b. Any approved charitable institution which satisfy condition of section 80G.
c. To any authority for satisfying the needs of housing accommodation or any corporation for promoting interests of minority community.
d. Any notified temple , mosque, gurdwara , church or other place notified by central govt. to be historic, archaeological, or artist importance, for renovation or repair of such place.

For calculating qualifying limit all donation covered under (C) AND (D) above shall be aggregated and the aggregate amount shall be limited to 10% of Adjusted gross total income.

NOTE- Adjusted gross total income means GTI minus LTCG minus STCG minus other deduction under this chapter.

SECTION 80GG

1. This deduction is allowed to individual who is self-employed or if employed neither getting HRA nor RFA.
2. Assessee ,spouse, minor child or HUF do not own any residential accommodation in the city where he works.
3. Amount of deduction is least of following-

a. Rent paid less 10% of adjusted GTI
b. 25% of adjusted GTI
c. 2,000 p.m

SECTION 80QQB

1. Allowed to individual resident in India.
2. Deduction is allowed for income from assignment of copyright of any book.
3. Such book should be work of literary, artistic, or scientific nature and not text book of school guides or newspaper etc.
4. An assessee shall be allowed as deduction RS. 3,00,000 or actual royalty whichever is less.
5. In respect of royalty received from outside India only that royalty shall be considered which is brought into india in foreign exchange within 6 month from the end of P/Y or the extended time.

CLUBBING OF INCOME

Income from assets transferred to spouse

1. Where any assets other than house property is transferred by an individual to his/her spouse directly or indirectly than any income form such assets shall be the income of transferor.
2. However clubbing shall not be done if assets is sold for adequate consideration or transfer under an agreement to live apart or relationship of husband and wife does not exist either at time of transfer or at the time of accrual of income.

Income of minor child

1. All income that accrue to minor child will be included in the total income of that parent whose total income is greater (before including income of child).
2. If marriage of parents does not exist it shall be included in the income of that parents who maintains the child.
3. Where any such income is once included in the total income of either parents ,any such income of any succeeding year shall be included in the income of other parent only if AO is satisfied that child is being maintained by the other parent.
4. Income of minor child shall not be clubbed if child is suffering from any disability or income of child on account of manual work or activity involving skill, talent or specialised knowledge.
5. If income of child is so included , the parent shall be entitled to an exemption of maximum RS. 1,500 in respect of each minor child.

Income from assets transferred to daughter in law

1. If an individual transfer any assets to his daughter in law , without adequate consideration income from such assets will be include in the total income of transferor .
2. If transferred assets is invested in any business than following amount shall be included in the income of transferor :-

Income from self- acquired property converted into joint family property

1. If an individual, who is a member of HUF , convert his self- acquired property as property to the HUF than income derived by such property shall be included in the income of transferor .
2. If the converted property is subsequently transferred among the members of family the income derived from such converted property received by spouse of transferor will be included in the income of transferor.

Income transferred without transfer of assets

1. If a person transfer income to another person , without transfer of assets from which the income arises, then such income shall be taxable in the hand of transferor.

Revocable transfer of assets

1. If whole or part of income or assets can be re-transferred to transferor than such transfer is called revocable transfer.
2. If there is revocable transfer of any assets than income from such transfer shall be taxable in the hands of transfer.

Remuneration of spouse

1. An individual is chargeable to tax in respect of any salary , commission , fees or any other remuneration received by spouse from a concern in which the individual has substantial interest.
2. If husband and wife both has substantial interest in the concern and both are receiving remuneration from the concern than remuneration of both shall be clubbed in the hand of that spouse whose total income is greater, before clubbing the income.
3. Substantial interest means if an individual along with relative is entitled to at least 20% equity share or 20% profit.
4. Relative means husband ,wife, brother or sister of any lineal ascendant or descendant of individual

SET OFF, CARRY FORWARD AND SET OFF

Set off loss from one source against income from another source under same head of income

1. If there is loss under any source falling under any head of income , other than capital gain than assessee shall be entitled to set off such loss against income from any other source under same head.
2. If there is short term capital loss, the assessee shall be entitled to set off such loss against income of any other capital asset.
3. If there is a long term capital loss, the assessee shall be entitled to set off such loss against income from long term capital asset .

Set off loss from one head against income from another

1. If there is loss under any head of income , other than capital gain he shall be entitled to set off such loss against income for that assessment year under any other head.
2. If there is loss under the head PGBP and assessee has income under the head salary, than he shall not entitled to set off such loss against salary.
3. if there is loss under the head capital gain , assessee shall not set off such loss against income under other head.

Carry forward and set off of loss from house property

1. if there is loss under the head income from house property , such loss can not be set off against income from any other head as well as income from house property than such loss should be carried forward up to 8 assessment year and set off against income from house property only.

Carry forward and set off of business losses

1. if there is loss under the head PGBP but not being a loss of speculation business , and such loss cannot be setoff against income under the any head or same head in same assessment year than it should be carry forward and set off against income under same head in following eight assessment year.

Losses in speculation business

1. Any loss in respect of speculation business , shall not be set off except against profit of another speculation business.
2. If such loss cannot be set off in same assessment year than it should be carry forward and set off from profit of same head in following four assessment year.

Losses under the head capital gain

1. If there is loss under the head capital gain the loss shall be carried forward to the following assessment year and if loss relates to short term capital asset, it shall be set off against income under the head capital gain up to 8 assessment year.
2. If loss relate to long term capital asset it shall be set off against income from long term capital asset only up to 8 assessment year.

Losses from certain specified sources falling under the head income from other sources

1. In this case of an assessee, being the owner of horses maintained by him for running in horse race , the loss incurred in the activity of owning and maintaining race horse in any assessment year shall not be set off against income from any sources other than activity of owning and maintaining race horse in the year and shall be carried forward to following assessment year and it shall be set off against the income from the activity of owning and maintaining race horse.
2. No such loss shall be carried forward for more than four assessment year.

Double Taxation Avoidance Agreement

For NRIs who are working in other countries, the Double Taxation Avoidance Agreement helps to avoid paying double taxes on income earned in both their country of residence and India. There are 80 countries which India has this agreement with.

What is Double Taxation Avoidance Agreement (DTAA)?

The DTAA, or Double Taxation Avoidance Agreement is a tax treaty signed between India and another country (or any two/multiple countries) so that taxpayers can avoid paying double taxes on their income earned from the source country as well as the residence country. At present, India has double tax avoidance treaties with more than 80 countries around the world.

The need for DTAA arises out of the imbalance in tax collection on global income of individuals. If a person aims to do business in a foreign country, he/she may end up paying income taxes in both cases, i.e. the country where the income is earned and the country where the individual holds his/her citizenship or residence. For instance, if you are moving to a different country from India while leaving income sources such as interest from deposits in here, you will be charged interest by both India and the country of your current residence as per your consolidated global earnings. Such a scenario can have you pay twice the tax over the same income. This is where the DTAA becomes useful for taxpayers.

Benefits of DTAA:

There are lots of benefits associated with DTAA for taxpayers. The basic benefit includes not having to pay double taxes on the same income. Apart from this,

- Lower Withholding Tax (Tax Deduction at Source or TDS)
-
- Tax credits
- Exemption from taxes

The primary idea behind DTAA agreements with various countries is to minimize the opportunity for tax evasion for tax payers in either or both of the countries between which the bilateral/multilateral DTAA agreement have been signed. Lower withholding tax is a plus for taxpayers as they can pay lower TDS on their interest, royalty or dividend incomes in India, while some agreements provide for tax credits in the source or country of operations so that taxpayers don't pay the same tax twice. In some cases, such as agreements with Mauritius, Cyprus, Singapore, Egypt etc. capital gains tax is exempted which can be a boon to taxpayers as they

Income Tax Return is the form in which assesses files information about his Income and tax thereon to Income Tax Department. Various forms are ITR 1, ITR 2, ITR 3, ITR 4, ITR 5, ITR 6 and ITR 7. When you file a belated return, you are not allowed to carry forward certain losses. These returns should be filed before the specified due date. Every Income Tax Return Form is applicable to a certain section of the Assesses. Only those Forms which are filed by the eligible Assesses are processed by the Income Tax Department of India. It is therefore imperative to know which particular form is appropriate in each case. Income Tax Return Forms vary depending on the criteria of the source of income of the Assesses and the category of the Assesses.

Advance tax

Advance tax is also known as pay as you earn tax as it can be deposited from time to time with the income tax department in advance as opposed to the lump sum amount. The **advance tax** is to be paid as per the due dates mentioned by the income tax department in the form of installments. Under this schemes, every assesses is required to pay tax in a particular financial year, preceding the assessment year, on an estimated basis. However, if such estimated tax liability for an individual who is not above 60 years of age at any point of time during the previous year and does not conduct any business in the previous year, and the estimated tax liability is below ₹ 10,000, advance tax will not be payable. Until FY 2015-16, the due dates and amount of advance tax were different for corporate taxpayers and individual taxpayers. However, from FY 2016-17, both categories of taxpayers were brought at par. Further, individuals opting presumptive scheme of taxation u/s 44AD, 44ADA are liable to pay advance tax in single installment.

The due dates of payment of advance tax for F.Y 17-18 are:-

	In case of corporate assesses as well as Individuals	**For Persons opting sec 44AD & 44ADA**
On or before 15 June of the previous year	Up to 15% of advance tax payable	-
On or before 15 September of the previous year	Up to 45% of balance of advance tax payable	-
On or before 15 December of the previous year	Up to 75% of balance of advance tax payable	-
On or before 15 March of the previous year	Up to 100% of balance of advance tax payable	Up to 100% of the advance tax payable

Any default in payment of advance tax attracts interest under section 234B and any deferment of advance tax attracts interest under section 234C.

ENTREPRENEURSHIP DEVELOPMENT (303)

UNIT – 1

Introduction

Entrepreneurial development today has become very significant; in view of its being a key to economic development. The objectives of industrial development, regional growth, and employment generation depend upon entrepreneurial development.

Entrepreneurs are, thus, the seeds of industrial development and the fruits of industrial development are greater employment opportunities to unemployed youth, increase in per capita income, higher standard of living and increased individual saving, revenue to the government in the form of income tax, sales tax, export duties, import duties, and balanced regional development.

Meaning & definition of Entrepreneur

The word "entrepreneur" is derived from the French verb enterprendre, which means 'to undertake'. This refers to those who "undertake" the risk of new enterprises. An enterprise is created by an entrepreneur. The process of creation is called "entrepreneurship".

There was various definition of entrepreneur.

According to America heritage dictionary;

"Entrepreneur is a person who organizes operates and assumes the risk for business venture"

According to encyclopedia Britannica

"Entrepreneur as the individual who bears the risk of operating a business in the face of uncertainty about future condition and who is rewarded accordingly by his profit or losses".

Richard Cotillion *says*

"Entrepreneur is the agent who purchased the means of production for combination into marketable product".

So we can say that entrepreneur a person who takes risk for establishing a new venture or business in order to create utility for the welfare of human being as well as for him of herself. She or he is always a person who seeks out opportunities and takes on challenges.

Meaning and Definition of Entrepreneurship:

Entrepreneurship is considered as of assuming the risk of an entrepreneur.

According to Natheal H. Leff:

Entrepreneurship is the capacity for innovation investment and expansion in new markets product and techniques.

Webster highlights entrepreneurship as economic venture organizing and risk taking capabilities.

Joseph A Schumpeter describe entrepreneurship is the force of creative destruction whereby established way of doing things are destroyed by the creating of new and better ways to get things done.

According to S. S. Kanaka:

Entrepreneurships is a process involving various actions to be taken to establish an enterprise.

Entrepreneurship is a process of actions of an entrepreneur who is a person always in search of something new and exploits such ideas into gainful opportunities by accepting the risk and uncertainty with the enterprise.

From the functional view point entrepreneurship is defined as the combination of activities such as perception of market opportunities gaining command over scarce resources purchasing input producing and marketing of product responding to competition and maintaining relation with political administration and public bureaucracy for concession licenses and taxes etc.

Characteristics of an entrepreneur:

An entrepreneur is a person who initiates a business venture. there are some essential feature of an entrepreneur which are describe below.

Risk taking capability: every business has risk of time money etc .so an entrepreneur must have the risk taking capability.

Creativity and innovation: an entrepreneur has an initiator possesses creativity and innovative power.

Need for achievement: the entrepreneur has strong desire to achieve the goal of business. he is always driven by the needs for achievement.

Need for autonomy: an entrepreneur does not like to be under anybody. it is the need for autonomy which drives a person to be an entrepreneur.

Internal locus of control: an entrepreneur believes in him his work.

External locus of control: he also believes in fate for ultimate result.

Self confident: an entrepreneur has confidence in him.

Leadership capability: an entrepreneur must have leadership capability to lead works under him

Industriousness: a successful entrepreneur must have leadership capability to lead workers working under him.

Decision making capability: the entrepreneur has capability to take quick decision

Adaptability: he has the capacity to adapt with any kind of situation that arise in the enterprise

Foresightness: The entrepreneurs have a good foresight to know about future business environment.

Others; the other feature are dynamism, ambition, education and training, long term involvement, future orientation.

Qualities of successful entrepreneur:

To become a successful as an entrepreneur in its business life, a businessman should possess a quite a number of essential qualities. Those are noted below:

Moderate risk taking: an entrepreneur always takes calculated risk to operate the organization

Hard work: an entrepreneur is very much hard worker, he or she always busy with various types work.

Accountability: a successful entrepreneur is accountable well as his associates always accountable to him.

Educated in real sense: successful entrepreneur is educated In real sense .he tries to implement his organizational objectives through his education.

Analytical mind: a successful entrepreneur is analytical minded. he scrutinizes every activity on the organization.

Dynamic leadership: a successful entrepreneur is always dynamic to operate the organization
Presence of mind: a successful entrepreneur is always at present of mind he is always aware of activities that to happening in the organization and around him
Accommodative: a good entrepreneur has the capacity to make his own place at every sector
Courageous and tactful: Corsages and techniques is very much essential for a successful entrepreneur
Maker of right decision: A successful entrepreneur makes right decision in right time in right place
Foresighted: a successful entrepreneur foresights the future and take decision accordingly
Right perception of things: A successful entrepreneur things in a right way
Enjoy simple life: A successful entrepreneur always deals a simple life a general people of the society
Strong desired to success: A successful entrepreneur have a strong desire to success. he is driven by the desire to success
Innovation: innovation is the process of making new something. A successful entrepreneur is innovative
Self confidence: A successful entrepreneur is self confidence. does not really on other for decision or fate
Goal setting: a successful entrepreneur set the goal
Keen observation: A successful entrepreneur always observes the origination
Sociable: A successful entrepreneur is sociable person
Loves to work; A successful entrepreneur is very much addicted to work
Loves new ideas: A successful entrepreneur loves new ides of the organization
Team builder: A successful entrepreneur builds a suitable team
Clean understanding: A successful entrepreneur clearly understands every things
Ability to conceptualize: A successful entrepreneur is able to conceptualize the reality
Others: the other qualities are patience, optimistic ,strategist, etc

Relationship between entrepreneur and entrepreneurship:

The relationship between entrepreneur and entrepreneurship are discussed below:

Entrepreneur
vs
Entrepreneurship

Entrepreneur is a person. Entrepreneurship is a process.

Entrepreneur is an organizer. Entrepreneurship is an organization.

Entrepreneur is an innovator. Entrepreneurship is an innovation.

Entrepreneur is a risk bearer. Entrepreneur is a risk bearing.

Entrepreneur is a motivator. Entrepreneur is a motivation.

Entrepreneur is a creator. Entrepreneur is a creation.

Entrepreneur is a visualizer. Entrepreneur is a vision.

Entrepreneur is a leader. Entrepreneurship is a leadership. Entrepreneur is an imitator.

Entrepreneurship is an imitation.

Distinction between an entrepreneur and a manager.

Sometimes the word entrepreneur and manager are used as synonyms. In fact there are some differences between them. They are described below –

Subject matter ------------ ***Entrepreneur*** ------------ ***Manager***

Motive

Thinking function. His main motive is to start a new venture by setting up an enterprise. Doing function. His main motive is to render service to the organization already established.

Status

Entrepreneur is the owner of the enterprise. Manager is the service holder or servant of the enterprise.

Risk bearing

Being owner of the enterprise assume all risk and uncertainty involved in the enterprise. As the servant don't take or bear risk and uncertainty involved in the organization.

Reward

Reward is profit which is highly uncertain. Get salary as a reward which is fixed and certain.

Innovation

An entrepreneur is an innovator. A manager is not an innovator in that sense he implements the plan prepared by the entrepreneur.

Qualification

They are not highly qualified but have extraordinary experience forecasting. They are highly qualified (institutional education). After the above discussion we can say that at a time an entrepreneur can be a manager but a manager cannot be an entrepreneur.

Different types of entrepreneurs:

On the basis of nature ***Clarence Danhof*** classified entrepreneurs into four categories. These are

Innovative entrepreneurs: An innovative entrepreneur in one, who introduces new goods, inaugurates new method of production, discovers new market and recognizes the enterprise. It is important to note that such entrepreneurs can work only when a certain level of development is already achieved and people look forward to change and improvement.

Imitative entrepreneurs: These types of entrepreneurs creatively imitate the innovative technical achievement made by another firm. Imitative entrepreneurs are suitable for underdeveloped countries as it is hard for them to bear the high cost of innovation.

Fabian entrepreneurs: Fabian entrepreneurs are characterized by very great caution and skepticism to experiment any change in their enterprises. They usually do not take any new challenge. They imitate only when it becomes perfectly clear that failure to do not so would result in a loss of the relative position in the enterprise.

Drone entrepreneurs: They are characterized by a refusal to adopt any change even at cost of severely reduction of profit.

Some other types of entrepreneurs:

Solo operators: These are the entrepreneurs who essentially work alone and if needed at all employ a few employees. In the beginning most of the entrepreneurs start their enterprises like them.

Active partners: Active partners are those entrepreneurs who start or carry on an enterprise as a joint venture. It is important that all of them actively participate in the operations of the business.

Innovators: Such entrepreneurs with their competence and creativity innovate new products. Their basic interest lies in research and innovative activities.

Buyers' entrepreneurs: These are the entrepreneurs who do not like to bear much risk. They do not take the risk of production but take the risk of marketing a product i.e. wholesaler and retailer.

Life timers: These entrepreneurs believe business as an integral part of their life. These entrepreneurs actually inherit their family business i.e. goldsmith, potter etc.

Challengers: These are the entrepreneurs who initiate business because of the challenges it presents. They believe that 'No risk, No gain'. When one challenge seems to be met, they begin to look for new challenges.

Beside these, there are Govt. and Non-govt. entrepreneurs.

Factors of Entrepreneurship development:

(A) Personal factors

Ability to cope with the situation
Age
Education
Personality
Intrapersonal communication ability
Achievement motivation
Self-confidence
Competence
Emotion
Understanding capacity

(B) Environmental factors

1. Socio-cultural factors

Religion
·Values
Rural-urban orientation
Marginality
Education
Tradition

Political and legal factors

·Govt. legal bindings
·Govt. policies
·Rules and laws related to the industry and business

(C) Institutional factors:

·Financial institution
·Training and development institution
·Consulting firms
·Incubators organization (old & pioneer)
·Research organization

Causes of success and failure of entrepreneur:

An entrepreneur may sometime become successful and sometime becomes failure. There are some causes of such success and failure. They are noted below:

Selection of business: It is an important aspect. That means an entrepreneur has to determine what type business he is going to start. Form various points of view the feasibility of the business should be tested.

Proper planning: Proper planning me s also important. For planning, planning premises like political, economic, social premised should be considered first. The steps of planning should be followed properly.

Initial capital: if the initial capitals are not an optimal level the organization would fall. So whether the enterprise is big or small the initial capital should be sufficient enough.

Determination of market demand: Through research the demand in the market should be identified. Both for long term and short term it should be considered.

Marketing of product: If the promotion policy, channel of destitution, transportation is not good the enterprise would fall.

Education and experience: One of the important tasks of the entrepreneurs is to select right person for the right post because the success of an enterprise depends on the right selection of employees.

Joint initiative: One may have much money and another may have more merit. Through joint initiative it can be balanced. But sometime for joint initiative misunderstanding arise, or sometimes corruption occur which may result in fall of enterprise.

Employment: Recruitment and appointment should be properly done. Those who have specialized skill should be appointed to that specialized job. Inefficient, corrupted employees may be responsible for fall of business.

Location of business: Site selection is an important factor. While starting a new business, an entrepreneur should think about the location of the business. In this case, many factors should be considered such as availability of raw materials, proper communication system, availability of labor, marketing facilities and so on.

Qualities of management: The management must have a minimum quality to success otherwise it would fall.

These are the common causes for which one enterprise may become successful and another may fall.

Emergence of Entrepreneurial Class

Environmental changes in the economy have led to the emergence of a new entrepreneurial class or business entrepreneurship. Their functions and role have undergone significant changes. In earlier days, entrepreneurship was regarded as individual responsibility and after some time it assumed collective responsibility.

At present, the entrepreneurship is oriented towards the whole economy and the nation.

We can understand the emerging form of business entrepreneurship with the help of the following points:

Commercial Entrepreneurship

The first time, this word was used in the 18th century in the French economy. The French economist, Richard Cantillon used this word when he observed that the businessmen of his country were selling their respective products in a limited market and at an uncertain price. He also observed the qualities of initiation, capacity to take risks and patience, in them. The French authors made a distinction between employers and the entrepreneurship. The role of entrepreneurs also has gone on changing with economic development. Initially, it was individualistic, then it became collective and now it has become industry and nation oriented. Its concept and functions are on changing the path, due to industrialization.

Industrial Entrepreneurship

The industrial revolution, technological developments, advertisements in the means of transportation and communications and non-interference by the State in business has resulted in the changes in nature, functions, and roles of entrepreneurship. The importance of the entrepreneurs is being accepted for the promotion and establishment of the industries. Now, the entrepreneur is being recognized as the promoter, coordinator, organizer of the enterprises and as the risk taker. There was no difference between the entrepreneur and the capitalist because the nature of the business was quite simple. In those days, most of the business activities were economical and commercial, except for manufacturing activities. The economists started thinking in terms of economic class and its nature, as a result of the emergence of companies in the business world and giving more emphasis on organization. “How the businessmen perform the functions of the entrepreneurial class, takes the risks, assemble capital and labour, prepare the general outline of the business and observe even the minute details”. They are the persons who make the forecasts and take care of the inlet and outlet of the commodities. They also search markets of consumption, keep knowledge about the employees and also of the whole business. Now, the time has changed. the industrial revolution, development of the means of transportation and communication, increased technical knowledge and state interference in business, etc. have brought several types of changes in the nature of the entrepreneurial class.

Innovating Entrepreneurship

The production and distribution of commodities and services, on large scale and rapid advancements in science and technology put emphasis on research and investigations. Increasing competition in the economy and business on the international level is due to globalization, economic liberalization, privatization, corporatization, customer orientation of marketing activities, mounting production, etc. All are the offshoots of the industrial revolution and these phenomena have widely increased the necessity and importance of the entrepreneurial class. The success of business in growing economies, so it has become essential that the products and their qualities be improved by improving production techniques. Economies in the cost of production may also be ensured. consumer satisfaction is to be achieved and efficiencies are increased at all levels, through various types of innovations, so that the enterprise may sustain the growing challenges of competition, the sale of products in high quantities. It will result in success in the business. In developed economies, the business cannot sustain without introducing innovations. The person or group of persons responsible for such innovations have been termed as innovating entrepreneur and his ability on this account is known as innovating entrepreneurship. It is not essential that the owner of wealth be also an entrepreneur. To be an entrepreneur, leadership is required more than ownership. He has differentiated, outlook than the traditional entrepreneurs who carry out only one type of production and the innovating entrepreneurs, who make production on the basis of new techniques, search new markets and establish the new organization. The innovating entrepreneurs create new demand, reduces the prices and bring changes in the position of traditional economic equilibrium. Such type of entrepreneurial class maintains circular flow in the economy and earn more profits by making contributions in the process of development.

The entrepreneur should have three qualities,

1. Knowledge of innovations
2. Incorporations of innovations,
3. Achieving success by use of innovations.

The unique feature of review is that the entrepreneur is not much influenced by the environment. Rather, he aspires for achieving his own business empire, by being influenced by his own tendencies and he also desires to have the family hold on his business empire and also the feelings of being higher than others.

The arguments are based on the assumption that high business knowledge and human capabilities are confined only to selected persons and families, belonging to higher strata.

Such thoughts should have emerged due to the reason that in those days the persons who invented new things earned money by adopting the innovations.

The entrepreneur does not emerge from poor strata. Strong persons with sharp intelligence and abilities exist in the whole society and in all ages. Due to favorable or unfavorable circumstances, some go ahead and some lag behind.

In the foreign ruled countries, the emergence of entrepreneurs has been relatively low, due to adverse circumstances. In Japan, a good number of entrepreneurs have emerged only from the lower strata.

But, the thoughts about the quality for development of the entrepreneurs are always relevant.

Conclusion

Thus, the emergence of the entrepreneurial class has been due to the circumstances and favorable business environment. Now, the entrepreneur emerges only from high classes has completely vanished. Although the entrepreneurs may belong to high families, they may be developed also following are the causes of the development of the entrepreneurial class.

Theories of Entrepreneurship

Schumpeter's Theory of Innovation:

Joseph Schumpeter propounded the well-known innovative theory of entrepreneurship. Schumpeter takes the case of a capitalist closed economy which is in stationary equilibrium. He believed that entrepreneurs disturb the stationary circular flow of the economy by introducing an innovation and takes the economy to a new level of development. The activities of the entrepreneurs represent a situation of disequilibrium as their activities break the routine circular flow.

Innovations of entrepreneurs are responsible for the rapid economic development of any country. Talking about innovation, he referred to new combinations of the factors of production, Schumpeter had assigned the role of innovator to the entrepreneur, who is not a man of ordinary managerial ability, but one who introduces something entirely new.

Innovation could involve any of the following:

Innovation of new products.
Innovation in novel methods or processes of production.
The opening up of a new market.
Entrepreneurs might find new source of supply of raw materials
Innovation in management. This means reorganization of an industry.

Let us try to understand the meaning of different facets of the term innovation.

The introduction of new product means the product which the consumers have not seen and is of a new and better quality and utility. A new method of production refers to a novel process not yet been used in manufacturing and commercial production. This may increase the productivity and lower cost of production.

The discovery of a new market means a new market which may have existed before but was not entered by the enterprise for commercial purposes. A new source of raw material similarly refers to a source or a place which has not been commercially exploited by the enterprises before. Innovation in management refers to reorganization and reconciliation of the position of the enterprise in the industry by building a monopoly like control or dismantling existing monopoly of others in the industry.

Schumpeter was very explicit about the economic function of the entrepreneur, whom he considered as the prime mover in economic development and the entrepreneur's task is to innovate or carry out new combinations.

Schumpeter had differentiated between invention and innovation. We should understand that invention refers to creation of new materials and innovation refers to application of new materials into practical use in industry. Similarly, there is a distinction between an innovator and an inventor. The inventor is the one who invents new materials and new methods. On the other hand, the innovator is the one who utilizes these inventions and discoveries in order to make new combinations.

Bringing about innovations is the main task of the entrepreneur and not the maintenance of the enterprise. Entrepreneurs dream and have a willingness to establish a private kingdom. They enjoy creating and getting things done. These "innovating entrepreneur" has played an important role in the rise of modem capitalism.

Criticisms:

Schumpeter's theory has been subjected to the following criticisms:

i. Critics feel that the theory over emphasized on innovative functions of the entrepreneur. It ignored the organizing aspects of entrepreneurship.

ii. Schumpeter had completely ignored the risk-taking function of the entrepreneur, which cannot be ignored. Whenever an entrepreneur develops a new combination of factors of production, there is enough risk involved.

iii. The theory is more applicable in developed countries only. In developing countries there is a paucity of innovative entrepreneurs.

iv. The theory does not provide the explanation as to why few countries have more entrepreneurship talent than others.

Despite of all the above criticisms Schumpeter's theory is considered as a landmark in the expansion of entrepreneurship theories.

1. Need for Achievement Theory of McClelland

According to McClelland the characteristics of entrepreneur has two features – first doing things in a new and better way and second decision making under uncertainty. McClelland emphasizes achievement orientation as most important factor for entrepreneurs. Individuals with high. Achievement orientation is not influenced by considerations of money or any other external incentives. Profit and incentives are merely yardsticks of measurement of success of entrepreneurs with high achievement orientation. People with high achievement are not influenced by money rewards as compared to people with low achievement. The latter types are prepared to work harder for money or such other external incentives. On the contrary, profit is merely a measure of success and competency for people with high achievement need. Professor David McClelland, in his book The Achieving Society, has propounded a theory based on his research that entrepreneurship ultimately depends on motivation. It is the need for achievement, the sense of doing and getting things done, that promote entrepreneurship. According to him, N- Ach is a relatively stable personality characteristic rooted in experiences in middle childhood through family socialization and child-learning practices which stress standards of excellence, material warmth, self-reliance training and 30 low father dominance.

According to David McClelland, regardless of culture or gender, people are driven by three motives:

- Achievement,
- Affiliation
- Power

Need for Achievement

A drive to excel, advance and grow. The need for achievement is characterized by the wish to take responsibility for finding solutions to problems, master complex tasks, set goals, get feedback on level of success.

Need for Affiliation

A drive for friendly and close inter-personal relationships. The need for affiliation is characterized by a desire to belong, an enjoyment of teamwork, a concern about interpersonal relationships, and a need reduce uncertainty.

Need for Power

A drive to dominate or influence others and situations. The need for power is characterized by a drive to control and influence others, a need to win arguments, a need to persuade and prevail.

McClelland found that certain societies tended to produce a large percentage of people with high achievement. He pointed out that individuals, indeed whole societies that possess N-ach will have higher levels of economic well-being than those that do not. McClelland's work indicated that there are five major components to the N-ach trait: (a) responsibility for problem solving, (b) setting goals, (c) reaching goals through one's own effort, (d) the need for and use of feedback, and (e) a preference for moderate levels of risk-taking. The individual with high levels of need achievement is a potential entrepreneur. The specific characteristics of a high achiever (entrepreneur) can be summarized as follows:

(i) They set moderate realistic and attainable goals for them.

(ii) They take calculated risks.

(iii) They prefer situations wherein they can take personal responsibility for solving problems.

(iv) They need concrete feedback on how well they are doing.

(v) Their need for achievement exist not merely for the sake of economic rewards or social recognition rather personal accomplishment is intrinsically more satisfying to them.

According to McClelland, motivation, abilities and congenial environment, all combine to promote entrepreneurship. Since entrepreneurial motivation and abilities are long run sociological issues; he opined it is better to make political, Social and economic environments congenial for the growth of entrepreneurship in underdeveloped and developing countries.

2. Max Weber's Theory of Social Change (Emphasis on Impact of Religion):

Max Weber advocated a sociological explanation for the growth of entrepreneurship in his theory of social change. He felt that religion had a profound influence on the growth of entrepreneurship. The religious belief and ethical value associated with the society plays a vital role in determining the entrepreneurial culture.

Max Weber opined that the entrepreneurial energies of a society are exogenously generated and supplied by religious believes. Some religions profess the basic values to earn and acquire money whereas some religions put less emphasis on it. In order to understand the gist of Max Weber's theory we need to understand few fundamental points of the theory.

In his theory spirit of capitalism is a fundamental concept. Capitalism refers to the economic system where market forces of demand and supply are allowed to play freely. As economic freedom and private enterprises are promoted in capitalism, the entrepreneurism is eulogized and entrepreneurial pursuits are encouraged. Spirit of capitalism promotes the entrepreneurs to engage in entrepreneurial pursuits and earn more and more profits.

The urge to acquire money and profits drives the individuals to become entrepreneurs. The spirit of capitalism will be widespread in the society that favours capitalism. Another associated concept was that of adventurous spirit which refers to the impulsive force that influences and promotes entrepreneurism. Weber felt that the belief systems of Hinduism didn't encourage entrepreneurship.

Hinduism laid less emphasis on wealth accumulation, and material life. The Hinduism didn't profess the spirit of capitalism and was thus an obstacle in the promotion of entrepreneurship. Weber was of the opinion that the Protestant ethic provided the mental attitude in a society that promotes spirit of capitalism and favours entrepreneurship.

The rate of industrial growth depends upon the values professed by the religion of the society. The Protestants had advanced at a faster rate in establishing capitalism in Europe owing to the value system professed by Protestant ethic. Protestant ethic granted them the rational economic attitude, accumulating assets, and permitted them to take pleasure in the material life.

Criticisms:

Max Weber had tried and made a commendable contribution in explaining the growth of entrepreneurship.

But, his theory has been challenged and criticized by many researchers and scholars on the following grounds:

i. The theory is based on unrealistic and invalid assumptions.

ii. The theory has been found empirically invalid.

iii. Max Weber has been criticized by many sociologists on his view on Hinduism and entrepreneurship. The rapid expansion of entrepreneurship in India in the post-independence period disproves that Hinduism is averse to the spirit of capitalism and to adventurous spirit.

iv. The views on Protestant ethic were also not completely correct. Capitalism has flourished in regions where Protestant ethic is not present.

3. The Uncertainty-Bearing Theory of Knight:

Frank H. Knight (1957) in his book Risk, Uncertainty and Profit regards profit of the entrepreneur as the reward of bearing non-insurable risks and uncertainties. Entrepreneurship is genuinely associated with risk bearing. Knight had distinguished risk into insurable risks and non-insurable risks.

Let us try to understand the underling concept of risks.

There are certain risks that are measurable and the probability of such risk can be statistically estimated and hence such risks can be insured. Example of insurable risks include theft of commodities, fire in the enterprise, accidental death etc. On the other hand, there are certain risks which cannot be calculated.

The probability of their occurrence cannot be statistically ascertained. Such risks include risks associated to changes in prices, demand and supply. These risks are non-insurable. Prof. Knight opined that the profit is the reward for bearing the non-insurable risks and uncertainties.

Uncertainty-bearing is one of the most vital functions in a dynamic economy. The entrepreneur bears the uncertainty involved in the enterprise. The expectation of profit is the supply price of the entrepreneurial uncertainty bearing exercise. In a state of economy (competitive) where there is no risk, every entrepreneur will have a minimum supply price.

If the reward allocated to the entrepreneur is below it, the entrepreneurs will abstain from providing their entrepreneurial services. The existence of uncertainty tends to raise the minimum supply price. The entrepreneurs expect a level of profit for bearing the uncertainty.

The salient points of Knight's theory include:

i. According to the theory, the entrepreneur earns pure profits for bearing the uncertainty.

ii. The probability of uncertainty or non-insurable risks cannot be statistically estimated.

iii. Entrepreneurs undertake risks of varying degrees according to their ability ad inclination. The theory suggests that the more risky the nature of enterprise, the higher level of profit earned by the entrepreneurs.

iv. Profit is the reward of the entrepreneur for bearing uncertainties and risks. Hence, it should be a part of the normal cost.

v. The reward of the entrepreneur is uncertain. Entrepreneur guarantees interest to lender of capital, wages to workers and rent to the landlord.

vi. The level of uncertainty in business can be reduced by applying the technique of consolidation. The total level of uncertainty can be reduced by pooling individual instances.

Criticisms:

F.H. Knight's theory is one of the most sophisticated theories to explain supply of entrepreneurship based on profit. But, the theory suffers from certain drawbacks as pointed by the critics.

i. The role of an entrepreneur has not been elaborately provided by the theory. The entrepreneur's activity has been restricted to uncertainty bearing. Modern business activities are different. Often, there is a dichotomy between ownership and management. These factors have not been taken into consideration.

ii. The uncertainty-bearing theory discussed the concept of profit in a vague way. The exact estimation of profit for the entrepreneur has not been provided in the theory.

iii. Profit as a residual income of the entrepreneur has been criticized.

iv. Critics feel that uncertainty-bearing should not be treated like other factors of production like land, labour and capital. It is a psychological concept and should be treated in a different manner.

4. Theory of Frank Young (Emphasis on Changes in Group Level Pattern):

A Micro-sociological interpretation of entrepreneurship as coined for the theory propounded by Frank Young emphasizes that the entrepreneurial initiatives are conditioned by group level pattern. Young rejected the psychogenic interpretations of entrepreneurship. He considered the solidarity groups responsible for building entrepreneurship.

We shall try to understand his theory by studying the various specific elements attached to this theory.

Frank Young opined that the entrepreneurial characteristics are observed in clusters, ethnic groups, occupational groups and groups with political orientation. Entrepreneurism at the individual level is the manifestation of the group level pattern. Young disapproves the notion of an entrepreneur working individually. The entrepreneur functions as a member of a group.

The entrepreneurial initiatives and actions are the outcome of the experiences and exposures of an individual entrepreneur as a member of a particular group, the family background of the entrepreneur and the manifestation of the general values of the group. The economic problems faced by the individual entrepreneurs are mitigated by the solidarity of entrepreneurial groups. The individual entrepreneurs enjoy the confidence of their association with the solidarity groups which help the individual entrepreneurs to overcome any sort of economic problems.

Frank Young deduced the group level pattern behaviour exhibited by the entrepreneurs on the basis of his test known as Thematic Appreciation Test (TAT) on groups of entrepreneurs.

The Young's theory includes the idea of reactive subgroups. These reactive sub-groups play an important role in enterprise creation. The reactive groups crop up whenever a group experiences low status recognition, limited or no access to social networks and have better institutional resources as compared to other groups in the society at the same level.

5. Economic Theory of Entrepreneurship:

G.F. Papanek (1962) and J.R. Harris (1970) were of the view that economic incentive is the main factor that influences entrepreneurial activities. Economic gains spontaneously develop the willingness among the entrepreneurs to undertake diverse entrepreneurial initiatives. The relationship between an individual's inner urge and the desired economic gains has a profound influence in the development of entrepreneurial competencies. Entrepreneurship development and economic growth takes place whenever certain economic conditions are favourable.

6. Mark Casson Theory (Economic Theory):

Mark Casson's theory is an original synthesis of other approaches. Mark Casson in his book 'The entrepreneur- An Economic Theory', published in 1982, talks about the entrepreneur. According to Mark Casson the Entrepreneur might be a property developer, a small businessman or just someone who knows how to 'turn a fast buck'. His book as expressed by Mark Casson endeavoured to provide a balanced view on the topic of entrepreneur.

Mark Casson felt that there was no established economic theory of the entrepreneur. Except for the discipline of Economics, all the social sciences had a definition of entrepreneur. He felt that there were two main reasons for the non-existence of an economic theory of the entrepreneur. These reasons were related to the limitations of the two main schools of economic thought prevalent at that point of time. First reason was that the neoclassical school of economics made extreme assumptions regarding the access to information.

The second reason was that the Austrian school of economics was committed to extreme level of subjectivism. This made the formulation of predictive theory of the entrepreneur impossible. The Mark Casson's book the theoretical reconstruction proceeds on two fronts. The first is to recognize that individuals differ not only in their tastes but in their access to information.

Individuals with similar taste but with different information may take different decisions. The entrepreneur exhibits this phenomenon. The entrepreneur will decide in one way which would be very different from what everyone else would decide. The entrepreneur considers that the totality of the information available to him/her with respect to some decision is unique. The entrepreneur's perception of the situation has a profound influence on the allocation of resources. The entrepreneur expects to earn profit from the difference in perception by 'taking a position' vis-a-vis other people.

Many of the predictions of the economic theory of entrepreneurship come from considering the tactical aspects of the strategy of the entrepreneur. The second area of reconstruction stems from recognition of the difficulty that is inherent in organizing a market. Mark Casson suggested that unlike neoclassical assumptions in reality transaction involves a significant resource cost. It is important for the entrepreneur's success that the entrepreneur minimizes the transaction cost incurred in establishing any given volume of trade.

Mark Casson has presented his book on Entrepreneur- An economic theory in fifteen chapters. Mark Casson had attempted to converge the two different approaches associated with the entrepreneurship theory. The functional approach was adopted by the economists and the indicative approach adopted by economic historians. The entrepreneur is defined as someone who specializes in taking judgmental decisions about the coordination of scarce resources.

7. Kunkel's Theory (Emphasis on Entrepreneurial Supply):

John H. Kunkel had built up his theory on the edifice of entrepreneurship supply. He was of the opinion that the sociological and psychological factors influence the emergence of entrepreneurs. Supply of entrepreneurs has a functional relationship with the social, political and economic structure.

In order to understand Kunkel's theory, let us understand few concepts associated with his theory.

In an economy, the supply of entrepreneurship depends on the following structures existing in the economy:

(i) Demand Structure:

This refers to the demand situation prevailing in the economy. The entrepreneurs expect rewards for their contributions and their behaviour is influenced by the rewards. The demand structure of an economy can be enlarged by rewarding the entrepreneurs with material rewards for their entrepreneurial activities.

(ii) Limitation Structure:

This structure influences the entrepreneurs and other members of a society. The society in this structure restricts specific activities. The entrepreneurs and the other members come within the ambit of this structure.

(iii) Opportunity Structure:

This structure is regarded as one of the most significant structure that influences the supply of entrepreneurs in an economy. This structure includes the existing market structure, the available managerial and technical skills, information about production techniques, supply of labour and capital.

(iv) Labour Structure:

This structure relates to the availability of skilled labour willing to work. The labour structure in influenced by number of factors like the mobility of labour, available alternatives of employment, level of traditionalism and prevailing work culture.

In Kunkel's theory, the conditioning procedure is a major determinant of the activities of the individuals. The behaviour of the individuals is highly subjected to the conditioning procedure surrounding the environment of the individuals. To influence and alter the individuals' activities there is a need to change certain factors of situation that influences the conditioning.

Criticisms:

Kunkel's theory despite of great recognition is criticized on the following grounds:

I. The theory is based on unrealistic postulates.

II. The different structures that influence supply of entrepreneurship are not that simple.

III. The theory of Kunkel tried not consider the ambiguous concepts like values, personality etc.

8. Hoselitz's Theory (Emphasis on Marginal Groups):

Hoselitz's theory emphasized that the cultural factors and the role of culturally marginal groups in entrepreneurial development. In his theory, Hoselitz had highlighted the importance of the culturally marginal groups in development of entrepreneurship and their contribution to economic development of the economy. The marginal groups are the minorities in the society and they yearn to elevate their conditions and in the process promote economic development.

In several countries the entrepreneurial aptitude are associated to persons of particular socio-economic classes. The importance and contribution of the culturally marginal groups like Lebanese in West Africa; Jews in Europe towards the economic development of those regions reflect the gist of the theory.

Hoselitz opined that the marginal men placed in an ambiguous position and therefore they are best suited to make creative adjustments in situations of change. They bring about genuine adaptations in their behaviours. They become entrepreneurs and promote economic development.

9. *Cochoran's Theory:*

Thomas Cochran in his theory had tried to discuss the supply of entrepreneurship from the sociological point of view.

We can understand the crux of his theory by discussing some of the principle elements of his theory.

Cochran had suggested that the cultural values of a society, social expectations and role expectations play an important role in determining the supply of entrepreneurs. The basic problems associated with economic development include non-economic issues. The social factors are responsible in determining the entrepreneurial dynamism and the supply of entrepreneurs.

As far as the entrepreneur is concerned, Cochran opined that the entrepreneurs are not extraordinary persons or super normal persons and they are not abnormal individuals deviant from the society. Rather the entrepreneurs represented role models of the society. An entrepreneur represents a society's model personality.

The entrepreneur plays an important social role. The role played by the entrepreneur is highly influenced by the model personality that crops up depending on the social conditioning. The role of an entrepreneur is defined by the defining group in corporate world which include the members of board of directors and other top officials.

Cochran was of the opinion that the intrinsic character and behaviour of the executive is highly dependent and conditioned by the type of childbearing and schooling. Thus all social and cultural factors play an important role in influencing the expectation levels, personality, behaviour of everyone in the society and entrepreneur's role specially.

The level of dynamics associated with entrepreneurial depends on social factors. These factors result in major changes. The model of Cochran was built on American experience of entrepreneurial dynamism. In the nineteenth century, American economy had experienced major changes as a result of the dynamism exhibited by the entrepreneurs.

Thomas Cochran held the view that the factors having a profound influence on the performance of the entrepreneurs include- First, the attitude of a person towards his/her own occupation. Second, the role expectations conceived and expected by the sanctioning group. And third, the operational requirements of the concerned job.

Criticisms:

Cochran's theory despite having earned high appreciations has been criticized on the following counts:

i. The theory doesn't provide a satisfactory explanation of the supply of entrepreneurs in an economy.

ii. The theory concentrates only on the social factors and their impact.

iii. The theory ignores the influence of important elements like risk, profit and innovation.

iv. The multiple roles associated with the entrepreneur have not been focused in the theory.

10. *E. E. Hagen's Theory (Emphasis on Withdrawal of Status Respect):*

E. Hagen in his theory had accredited the withdrawal of status respect of a group as the starting point for entrepreneurship development process. Before we discuss the concept of withdrawal of status respect let us try to consider the various crucial facets of the theory.

The theory is based on a general model of the society. His theory viewed the entrepreneur as a trouble shooter who contributes to economic development. The creativity of the entrepreneur brings about social transformation and economic development. Economic growth is associated with the social and political changes. He didn't encourage the entrepreneurs to imitate other's technology.

Hagen had ascribed the genesis of entrepreneurship to withdrawal of status respect of a group. The social group that experiences the withdrawal of status respect engulfs itself into aggressive entrepreneurism. In such a situation the status loosing group and the members of status loosing group endeavour to regain their status by undertaking rigorous entrepreneurial drive.

Hagen had suggested the events that could create as well as indicate withdrawal of status respect of a social group. First, dislodgment of a traditional elite group from its prior status, Second, defamation of valued symbols through some change in the attitude of the superior group. Third, Unpredictability of status symbols in the changed allocation of economic power. Fourth, when social group doesn't enjoy the expected status when it migrates to a new society.

There four possible reactions to the withdrawal of status respect which relates to four different personality types:

(i) The retreatist – An individual who works in the society but is indifferent to the work and position.

(ii) The ritualist – An individual who works in the manner accepted and approved by the society but has no hopes of improving his/her position.

(iii) The reformist – An individual who fights against the injustice and tries to rebels against the established society in order to form a new society.

(iv) The innovator – An individual who endeavours to bring about new changes and utilizes all opportunities. This personality reflects the personality of an entrepreneur.

Criticisms:

I. The theory lacks general application. It is not always true that all the social groups have behaved in the manner as advocated in the theory.

II. The theory ignores the various other factors accountable for development of entrepreneurship.

11. Leibenstein's Theory (Emphasis on X-Efficiency):

The concept of X-efficiency was introduced by Harvey Leibenstein a noted economist in1966 in his article titled "Allocative efficiency vs. X-efficiency". This is also referred to as X-inefficiency. In general X-inefficiency refers to the difference between the optimal efficient behaviour of business in theory and the observed behaviour is practice which occurs owing to different factors.

X-efficiency refers to the effectiveness with which a given set of inputs are used to produce outputs. If a particular firm is producing the maximum output it can, given the resources it employs with the best available technology, it is said to be technical-efficient. X-inefficiency occurs when technical-efficiency is not achieved. Whenever an input is not used effectively the difference between the actual output and the maximum output attributable to that input is a measure of the degree of X-efficiency.

Harvey Leibenstein had mentioned that for allocative efficiency the whole economy was considered whereas in case of X-efficiency just specific companies and industries are to be considered.

X-efficiency arises either because the firm's resources are used in the wrong way or because they are wasted, that is, not used at all.

The entrepreneur has been entrusted two roles; first the role of a gap filler and second an input completer. The production function usually has certain deficiencies. These deficiencies and gap arise because all the factors of production function cannot be marketed. The entrepreneur has been entrusted the job to fill the gaps in the market. The second role of the entrepreneur is input completion. The entrepreneur has to mobilize all the available inputs in order to improve the efficiency of existing production methods.

Leibenstein advocated two types of entrepreneurship. First type is the 'Routine entrepreneurship' which involves the important functions of management of business. Second type is that of the 'New entrepreneurship' which involves innovative entrepreneurship.

Criticisms:

The Leibenstein's theory has been often compared with the neoclassical views.

The theory has many novel contributions but has been criticized on following counts:

I. The exact influence which the X-efficiency has on output of an organisation cannot be determined.

II. The theory is less predictable as compared to normal theories.

12. M. Kirzrier's View on Entrepreneurship:

Israel Meir Kirzner, an American economist has made remarkable contributions towards entrepreneurship. He has contributed many books. His ideas and theory on entrepreneurship can be understood by the going through his book 'Competition and entrepreneurship' published in 1973. There are six chapters. The second chapter is devoted to discuss the topics like nature of entrepreneurship, the different facets of entrepreneurs, entrepreneurial profits.

We shall try to understand the basics features enshrined in his ideas.

The basis of Kirzner's idea of entrepreneurship is spontaneous learning. The simplest situation in which spontaneous learning can occur is a Crusoe situation. Further, Kirzner calls the state of mind that enables spontaneous learning to occur alertness.

Kirzner introduces the notion of the pure entrepreneur by saying that there are two distinct ways in which this notion enters the analysis of the market process: First, by means of contrast with Robbinsian economizers, and Second, through the alertness.

According to Kirzner, the pure entrepreneur is "a market participant whose decisions are entirely incapable of being subsumed under the category of Robbinsian economizing." And the pure entrepreneur is "a decision-maker whose entire role arises out of his alertness to hitherto unnoticed opportunities."

Kirzner's notion of entrepreneurship as equilibrating combines three ideas. The first is that subconscious learning is equilibrating to the isolated actor. The second is that subconscious learning about arbitrage opportunities is equilibrating in markets. The third is that subconscious learning would lead to a general equilibrium if there were no changes in the non-entrepreneurial determinants of demand and supply.

13. Baumol's View on Entrepreneurship:

William J. Baumol a noted economist had made significant contributions towards the theory of entrepreneurship. He has many articles like 'Entrepreneurship in Economic Theory', 'Entrepreneurship: Productive, Unproductive, and Destructive' to his credit that reflects his notion on entrepreneurship.

Baumol (1968) discussed role of entrepreneur. He felt that the role of the entrepreneur is vital to economic growth. Baumol's approach to entrepreneurship within the economy shows that the entrepreneur is basically nonexistent in the models of economics. He stated that the entrepreneur has been read out of the model because the economic models are based on well-defined variables like output and price. There is no scope for analyzing the issues related to like inventiveness, cleverness, ambition of the entrepreneur in the models. He opined that theories won't be able to portray the function of entrepreneurial activity.

Again in an article Baumol laid out a simple hypothesis. He stated that the total supply of entrepreneurs varies across the societies. Moreover, the productive contribution of the society's entrepreneurial activities also varies due to allocation of their activities into productive and unproductive activities.

14. Peter Drucker's View on Entrepreneurship:

Peter Ferinand Drucker was an Austrian born American multifaceted management consultant, author, professor who described himself as a social ecologist. Drucker's book Innovation and Entrepreneurship published in 1985 is a great contribution. Peter Drucker regards the definition of J. B. Say on entrepreneur. J.B. Say was of the opinion that the "entrepreneur shifts economic resources out of an area of lower and into area of higher productivity and greater yield."

Peter Drucker viewed the entrepreneur as a unique agent of change. Drucker writes that "the entrepreneur always searches for change, responds to it, and exploits it as an opportunity."

In his book "Innovation and Entrepreneurship", Peter Drucker offers guidelines on how entrepreneurs can become innovative. Drucker opined that successful innovation practices are result of systematic hard work. Drucker introduces systematic innovation as a framework for exploiting innovative opportunities.

He also considered that the entrepreneurial society is the outcome of innovative entrepreneurship combined with government facilitation.

Drucker takes the instance of the United States of America as a successful entrepreneurial economy. He has separately dealt with three branches- existing business, public service institutions, and new ventures.

UNIT – 2

Promotion of a Venture

"Promotion of a venture" means initiating all necessary efforts required to form a business or any other enterprise. Promotion starts from the stage of 'conceiving an idea of forming an enterprise and ends with its actually being established, and if necessary or desirable then being registered as per law.'

According to C. W. Grestenbeg : "Promotion may be defined as the discovery of business opportunities and the subsequent organization of funds, property, and managerial ability into a business concern for the purpose of making profit there form Entrepreneur identifies the opportunities and investigates which of them are profit yielding from economic point of views. If he finds the venture profit yielding then he takes the second step, that is of collecting the important resources. iz., land resources, human resources, natural resources and labour etc.

Meaning of Opportunity

Opportunity is a positive trend in external environment. It is an attractive project idea whicn an entrepreneur accepts as a basis for his investment decision. Finding out the possibilities of a business is generally regarded as identification of business opportunity. A mere "possibility" is to be distinguished from business "opportunity". Good business ideas must be capable Of being converted into feasible projects. Entrepreneurs generally have different possibilities and select only highest reward paying possibly for execution. Thus, a business possibility may take the shape business opportunity fit proves as commercially viable.

Objectives of Identification of Business Opportunities

An entrepreneur desirous of investing on a project has to look for suitable opportunities. This is not simple, since he has a very wide choice, and the dimensions of the choice are . product/service, technology, equipment, scale of production, market, time-phasing and location. The vast range of opportunities makes the task Of identification very difficult. The main objectives of identification of business opportunities may be summarised as follows :

(i) To evaluate the possibilities of utilising physical resources of a particular region from the technical angle.

(ii) To identify those industries which are not based on local resources

(iii) To identify the industrial potentialities in particular region and country as a whole.

(iv) To estimate the capital, labour, transport, power, fuel, raw material for feasible industries.

(v) To estimate the capital, labour, transport, power, fuel, raw material for feasible industries.

(vi) To explore the development possibilities of the region with regard to agriculture, minerals, labour, irrigation etc.

(vii) To identify those areas and directions which are necessary for the balanced growth of region.

(viii) To evaluate the impact of financial resources, production, employment in industrial development process.

Meaning of Opportunity Analysis

Before taking a decision to implement new ideas, it is necessary to study in depth their profitability and viability so that the venture may be successful and there may be reasonable return on investment. Such studies are called opportunity analysis and is done in various ways. While selecting a project, a prospective entrepreneur as to consider various aspects like input, output, social cost and benefits. An entrepreneur is always on lookout for potential profitable

opportunities and exploits them in the best interest of his enterprise. Various factors such as financial and non-financial incentives provided by the government, availability of markets and environmental factors etc. are also considered by the prospective entrepreneur in the process of opportunity analysis.

Factors of Opportunity Analysis or Sources of Opportunities Analysis

Following factors or sources are included in the opportunities analysis :

(1) **Market and Demand Analysis**: Success of an business unit not depends on the amount of production but mainly on the fact that what amount of goods it can be sold in the market. Therefore, market and demand analysis is considered origin of opportunity analysis. Size of a business unit and technology used in it depends to a great extent on its market size and demand of customers. Hence, it is very essential that demand estimates are properly made and all the relevant factors must be taken into consideration like population, GDP growth, per capita consumption, competition with substitutes and imports, technical norms of consumption in case of intermediate goods and growth in the consuming industry. If anyone of these factor is not assessed correctly it is most likely that estimates may not be correct.

(2) **Resource Analysis**: entrepreneur has to see whether adequate amount of resourcs such as land, raw-material, machines, technology, financial sources, man-power etc. are available or not. If the adequate amount of these resources is not available then project will be assumed as come to an end. On the contrary, if resources are available then an entrepreneur has to see the sources and method of acquiring these resources.

(3) **Technical Analysis**: Technical possibilities for establishing a project is analysed in the technical analysis. If it is found that from the technical point of view project establishment is not feasible then no question arises to consider other factors. Scientific and Industrial Research have developed several new processes and technologies which offer opportunities for commercial exploitation But before applying new technology, it is necessary to get opinion Of experts and study all related facts properly to assess the effects Of changing.

(4) **Business Environment** Analysis environment analysis is necessary before establishment of a new enterprise. An important aspect of the business environment affecting investment opportunities is the government’s policy framework. Main factors affecting the business environment are as follows :

(i) Industrial policy, (ii) Licensing policy, (iii) Industrial Development and Regulation Act, (iv) Price Control Policy, (v) Distribution System, (vi) Incentives for industries in backward region,

(vii) Incentives for small scale units, (viii) Incentives for export-oriented units, (ix) Recrulation of Foreign Exchange, (x) Assessment of profitability and position of existing industr.es etc.

(5) **Financial Analysis**: Financial analysis is a broad under which availability of financial resources and profitability of a project is analysed. Various factors such as cost of project, cost of raw-material, technical cost, marketing cost, operating cost etc. are considered in the financial analysis. Generally, financial analysis study the following aspects :

(i) Total Cost of ‘a project including cost of land, building, machines, raw material, cash flow etc.

(ii) Sources and requirements of fixed and working capital.

(iii) Expected sales, terms of credit, income, profit, interest, return on investment etc.

(iv) Assistance and financial concessions from the government.

(v) Social profit analysis in case of public enterprises.

(vi) Return on capital investment.

(6) Risk Analysis: Various types of risks are found in a particular business in which economic risk, social risk, environmental risk,. technical risk etc. are the main risks. With the change of business environment, nature and extent of risk also get changed. An entrepreneur has to decide in the identification of opportunity analysis that what amount of risk is involved in availing opportunity and upto what extent risk acceptance will prove profitable to him.

(7) Plant Location and Layout Situation: The main object Of plant location analysis is to find out the place where plant is to be established. The decision of plant location depends upon various factors such as, availability of raw material, labour, power supply, transportation facilities, communication and bank facilities, social amenities, service facilities, market etc. The government also allows certain incentives and concessions for industries development in backward areas such as, concessions in taxes, facilities of training, light and land at cheaper rates, financial subsidies, facilities for import of raw-material etc. An entrepreneur should take into consideration all these factors while deciding the plant location. An entrepreneur should also prepare best layout so that he can produce maximum production at lower cost.

(8) Evaluation Analysis: It is the last stage of opportunities analysis. Following are included in the evaluation analysis :

(i) Evaluation of various aspects of project.
(ii) Evaluation of economic profitability.
(iii) Evaluation of Social profitability.
(iv) Evaluation of cost of project.
(v) Evaluation of availability of essential resources.
(vi) Evaluation of existing competition.
(vii) Evaluation of competition in global market.
(viii) Evaluation of effects of there external factors.

External Environmental Analysis

Meaning of External Environmental Analysis, The word “External Environment Analysis” has been made up of two words ‘External Environment’ and ‘Analysis’. The first word ‘External Environment’ Means elements or factors outside the institution of the entrepreneur, like – economic, social, cultural, political, physical, educational, technical, religious, ethical and international, etc. which affect his business.

The other word, ‘Analysis’ means reactions towards those factors or elements or issues, neglect thereof or taking of decisions by predicting the opportunities.

Hence, in composite form, external environment analysis means such process through which decision is taken, by assessing economic, socio-cultural, political, physical, educational, technical, religious, ethical and international environment or factors or element, or issues. and also opportunities.

External environmental analysis or evaluation is a process through which strategic planner (entrepreneur) evaluates economic, social, official, supply, technological and market conditions to determine the opportunities and challenges for their enterprise and according to which he adjusts his strategy and objectives.

Thus, external environment analysis is that process through which the entrepreneur determines opportunities, threats, reactions, neglects and challenges by evaluation of those factors and in consonance whereof, adjusts his strategies and objectives.

Features of External Environmental Analysis

Following Characteristics of external environment analysis may be observed by studying and analyzing its meaning.

1. Continuous Process

External environment analysis is a continuing process because till an entrepreneur will not keep the continuous watch on the changes happening in the environment, he will not be able to have knowledge about the threats and challenges.

2. Determination of Opportunities and Challenges

By external environment analysis, the entrepreneur evaluates all factors and parties to determine the opportunities and challenges for his enterprise, so that he may face the challenges of some factors and their tendencies.

3. Adjustment of Strategies and Objectives

In the external environmental analysis, the entrepreneur evaluates those factors to determine opportunities, threats, reactions and challenges for his enterprise. Thereafter, he adjusts his strategies and objectives in accordance with those factors.

4. Inner Knowledge Process

External environmental analysis is a process through which environmental conditions are known on the one side, knowledge is also gained about future possibilities and hidden opportunities. As a result, the decision making and making adjustments of strategies and objectives, by the entrepreneur become easy.

5. Opportunities and Threats

External environmental analysis is the opportunity and threat analysis, 'meaning thereby that the external environmental analysis provides the opportunity to the entrepreneur that presently the circumstances are favorable and hence decision may be taken quickly and may be implemented also, so that profit may be earned. **On the contrary**, the external environmental analysis may also pose the threat that the circumstances are not favorable and hence caution and care be exercised, otherwise, losses may occur.

6. Goal Orientations

Through external environmental analysis, the entrepreneur makes efforts to know the future possibilities and their real effects or makes efforts to achieve his goal by searching business opportunity with the help of **external environmental analysis**.

Need and Importance of External Environmental Analysis

For an entrepreneur, continuous study and evaluation of external environmental analysis are essential. External Environmental Analysis

For the entrepreneur analysis of external environment is necessary, so that he may know.

1. Which of the environmental factors are posing threats to the present strategy and obtainable objectives of the entrepreneur?
2. Which of the environmental factors are presenting opportunities, which may be availed by making necessary adjustments in the present strategy?

Importance and necessity of external environmental analysis may be easily understood with the help of following points.

1. Success of Entrepreneurship

For the success of an enterprise, advance evaluation of the far-reaching favorable effects and ill effects of the external environment and its factors is necessary. If such advance evaluation provides some specific knowledge, the entrepreneur gets alert about them and tries to adjust his decisions, accordingly.

2. Formulation of Viable Plans

We have studied that the business environment is dynamic, and not static. Hence, the entrepreneurs should effectively assess and analyze it to give practical and functional shape to his plans.

3. To Create Measures for Competitive Environment

The competitive environment is also an essential part of the total environment, which cannot be left unseen. **Hence**, it is essential for the entrepreneur that he should study and analyze the external environmental factors, so as to work out measures against the strategies of their competitors and to adopt counter Strategies. Thus, external environmental analysis is necessary for working out strong measures against the competitors.

4. Formulation of Successful Plans

Components of planning include objectives and goals, policies, Budget, Time, standards and strategies. The forecast is the base of planning. **Hence**, for the preparation of successful business plans of the entrepreneurs, determination of various components, basis and their effects is necessary. Not only that, but the study of factors of the external environment is totality is also essential.

5. Helpful in Selection of the Best Alternative

External environmental analysis and investigation not only help the strategic decision makers in restricting the volume of available alternatives but also in removing the is irrelevant alternatives, by taking future opportunities and challenges and threats into consideration. The best strategy cannot be easily identified, but unwanted alternatives may be removed to a large extent and the best available alternative and may be selected through external environmental analysis and investigation.

6. Use of Profit Opportunities in Business

The external environmental analysis provides information on various opportunities of gaining profit in business. **For that,** it is essential that the entrepreneur may remain alert towards, that environment and factors. Similarly, the entrepreneur should have knowledge about economic events, social changes, government policies, and foreign Corporation, etc. so that various available opportunities may be availed for earning optimum profits. Such knowledge maybe also make him alert towards future challenges and threats. Thus, the entrepreneur may use several opportunities for Profit in his business through external environmental analysis.

7. To Provide Permanency to Possibilities for Sale of Products

In the external environment and its factors, the products, production procedure, and methods, cost structure, marketing strategies, distribution chain, technical and sale methods of the competitors are also studied. By analyzing these, the possibilities of the sale of products may be provided permanency, because by such analysis the entrepreneur becomes capable to easily take strategic decisions.

8. Leadership of Market

External environmental analysis is also required because through it is the entrepreneur get knowledge about new products and new services available in the market, fashion, likings of the consumers, new techniques of production and methods, etc. With the use of such knowledge, the entrepreneur may increase his sales by efficiently leading the market, which will surely result in good profits to him.

9. Vigilance Towards Future Threats and Challenges

The external environment analysis also provides advanced Information about various future threats and challenges to the entrepreneur and make him alert. High management of the corporation (entrepreneur) and his planning department continuously keep watch on happenings in the markets, and which threats and opportunities are waiting for him.

10. Permanent Residence of the Institution and Entrepreneur

External environment analysis by any entrepreneur is essential to ensure stable existence of his institution, the reason being that by doing so, he keeps watching on the environment and its factors and makes necessary adjustments in his Strategies and objectives. If he does not do so, his own existence or of his institution will gradually come to an end.

Entrepreneurship Environment

The entrepreneurial activity depends upon a complex and varying combination of socio-economic, political, psychological and other factors. Entrepreneurship is not an inborn quality; it is a product of environment. To be successful, an entrepreneur has to remain dynamic and responsible to the whole environment. Environment is a combination of various dynamic, complex and uncontrollable external influences within which an entrepreneur has to function. In case of favorable business environment, entrepreneurship developed rapidly. Environment creates challenges, pressures, risks, opportunities, gains and threats for the entrepreneur. Entrepreneur needs a rational vision on his part to take advantages of these changing conditions.

Both entrepreneur and environment are dependent on each Other. All external environments affect the working of an Entrepreneur but entrepreneur also shapes the environment. The Influence of entrepreneurial acts on the external environment especially on the society can be measured easily.

Role of Economic Environment in** the **Development of Entrepreneurship

One of the most important factors affecting entrepreneurship is economic environment. It exercises the most direct and immediate influence on entrepreneurship. Economic environment is usually complex, rapidly changing, uncertain and not easily controllable. Hence its study becomes all the more important. Economic environment mainly includes the economic system economic conditions, economic policies, state of various resources and facilities like capital, raw materials, infrastructure and so on prevailing within the country. Economic conditions play an important role in the formation of stratifies business policies. For example in the developing nation's level of income, consumption, savings, employment and demand is lower in comparison to the developed nations. Keeping in view of all these factors, an entrepreneur takes decisions about his economic activities. Similarly, if the interest rates are increased, then the funds needed for investment may become costlier.

Again, business tax policies can encourage some enterprises for expansion, diver-ossification, or modernization programmers. Export promotion schemes announced by the Government may attract many new entrepreneurs to form their ventures. The influence of these economic factors may differ from venture to venture, especially keeping in mind their internal environment. The important elements of economic environment and their influences may be discussed as follows:

1) Economic System: Economic System of a country may be capitalist, socialist, democratic or mixed. Economic system determines the nature and scope of entrepreneurship. It also affects mobilization of resources. In the capitalist system, entrepreneur-ship developed rapidly while socialist economy creates hindrance in the way of entrepreneurship. Entrepreneurs can work independently in the capitalist economy which is not so in the socialist economy.

(2) Economic Conditions: Economic condition of a country may be of developed, developing and underdeveloped. The nature of Entrepreneurship is determined by the level of development of economy. ‘In developed economy, entrepreneurs have to undertake innovative activities for survival and growth but in the developing and underdeveloped countries, entrepreneurs do not take much interest in the innovative activities. In these countries, entrepreneurs have to face many problems and challenges for their development,

(3) **Structure of Economy:** The factors like national income, rate of capital formation, development of capital market, rate of investment, saving and foreign trade etc., is the structure of the economy. The favorable growth of these factors may promote entrepreneurship.

(4) **Trade Cycles:** Cycle of inflation and deflation, create many challenges and problems in the development and expansion of entrepreneurship. Changes in major economic variables like money income, cost of living, interest rates, savings, credit availability etc. have an immediate impact on the working an enterprise.

(5) **Economic Policies and Laws:** The government enacts various laws to regulate the business environment. Industrial policy, Licensing policy, monetary policy, import-export policy are considered economic policies which produce a great effect on the entrepreneurship activities. Company Law, Banking Law, Foreign Exchange Law and other laws affect the business environment. Favorable economic policies and laws promote the development of entrepreneurship.

(6) **Financial Resources:** Adequate Funds are required for bringing together other factors of production. It also encourages innovations and introduction of new things. Lack of required capital for industrial activities may impede and discourage entrepreneurs.

(7) **Human Capital Formation:** Human capital formation is the process of increasing knowledge, work skills and the abilities of all people engaged in productive activities. The low level of education, knowledge and efficiency or labor may inhibit emergence of entrepreneurship.

(8) **Resources of production**: Supply of various resources of production such as raw material, machines and equipment, power technical labor etc. deeply affect the growth of enterprise and risk-takers. Labor’s expectations, prevailing wage rates, productivity, labor union activities etc. influence the growth of entrepreneurship. **(9) Market, prices and competition:** In the modern competitive world, no entrepreneur can think of surviving in the absence of latest knowledge about market and various marketing techniques, the size and composition of market, price level of products, and the position of competing institutions also affect the survival and growth of entrepreneurship.

Role of Social Environment in the Development Of Entrepreneurship

Social environment strongly affect the entrepreneurial behavior, which contribute to entrepreneurial growth. Social environment includes the values, attitudes, beliefs, customs, religion and habits of the people. Prosperous and developing social environment motivate the development of entrepreneurship whereas traditional and orthodox social environment put hindrance in the way of entrepreneurship development. In brief, effect of social environment on the entrepreneurship development may be explained as follows:

(i) **Customs and Religious Traditions:** Customs, religious faith and ideology also affect entrepreneurial growth. In a developing country like India, there are such religious traditions which are not conductive to entrepreneurship. People are fatalists and they do not like to work hard or do something new. They remain satisfied with old.

(ii) **Family Background:** The environment of family affects entrepreneurship. Joint family can provide family resources to invest and expand family business. If the father is a professional, entrepreneur or businessman, the son is more likely to enter the same line because of certain inherent advantages. Mobility of the entrepreneur is influenced by the occupational and social status of the family.

(iii) Desire for improvement and protection of status: The desire for improvement and protection of status forces people to behave responsibly. People work hard to maintain and improve their status and it contributes to entrepreneurial growth.

(iv) Social Mobility and Social Marginality: There are some persons of the view point that high degree of mobility is conductive for the emergence of entrepreneurship. Social marginality also positively influences entrepreneurship.

(v) Values: Values are enduring beliefs that people hold about morals, equality, freedom, work ethic, and so on. When values change, the impact is felt in the ways in which entrepreneurs, government and society operate.

(vi) Attitude towards changes and Risk-taking: People's attitude towards changes, capacity and feelings of risk-taking etc. also affects the entrepreneurial environment. Positive attitude to adopt changes and risk-taken, influence the development of entrepreneurship.

(vii) Work Ethics: It is dedication or preoccupation with work. It is a sense of duty and work which is needed for entrepreneurial progress. The Japanese have achieved tremendous progress because of their commitment of work.

(viii) Educational and Technical Know How: Education, entrepreneurship and development are very closely related, rather say they are interrelated. Education is the best means of developing man's resourcefulness, which encompass different dimensions of entrepreneurship. It is further expected that the high level of education may enable the entrepreneurs to exercise their entrepreneurial talent more effectively and efficiently.

Thus, an entrepreneur cannot build up its image in the society without considering the social objects, values, interests and welfare. This type of social awareness increases the image of business enterprise. If economic growth and entrepreneurial development are to take place, the various forces of social environment must be taken into consideration.

Socio-economic environment has a great impact on the entrepreneurial behavior and success of entrepreneur. The entrepreneurial activity depends upon a complex and varying combination of socio-economic, psychological and other factors. In the developing nations low level of income, consumption, savings' demand, and employment exists, so entrepreneurs consider all these factors while determining their economic activities. Similarly restrictions imposed by monetary and physical policy of the government also affects business enterprises. Economic conditions, economic system, structure of economy etc. also influence the entrepreneurship activities. Social environment i.e. values, religion, customs, attitudes, education, ambitions etc. influence the development of entrepreneurship. An entrepreneur cannot build up its image in the society without considering the social objects, values, interests and welfare. Thus, socioeconomic environment has a great role in entrepreneurship development.

Role of Technological Environment in the Development Of Entrepreneurship

Technological Environment means the development in the field of technology which affects business by new inventions of productions and other improvements in techniques to perform the business *work.*

Technological change presents significant opportunities and threats for entrepreneurs.

Technology developments affect business operations in a number of ***positive*** ways:

- Increasing access to, and storage and manipulation of, data.
- Increasing speed and volume of communication.
- Reduced language and cultural barriers.
- Reduced costs of production.
- Reduced administration costs, waste and increased efficiencies.
- Increased outsourcing of key functions cutting operating costs.
- Higher quality products at competitive prices through improved innovation and development.
- Better working conditions, flexible working practices and greater opportunity for personal development.
- Increasing access to global markets and greater mobility in business transactions.

However, there are some ***potential negatives*** associated with technology development

- The real costs of remaining ahead of competitors.
- Fewer barriers to entry to markets, allowing smaller companies to compete using relatively low cost web marketing tools.
- Empowering customers to seek lower prices and better deals.
- The increasing support costs such as licensing of software, maintenance of equipment and the training of staff.
- Reduced job security.
- The pace of constant change undermining existing organisational structures and threatening social relationships.
- The increased risk of interconnected systems failing and resulting chaos. Not all systems are secure and it is increasingly difficult to protect systems from hacking.

<u>Legal Requirements for Establishment of a New Unit</u>

Establishing a new business unit is a complex and risky task. Entrepreneurs have to fulfil various legal formalities for establishment of a new unit. Hence, the entrepreneur needs to be aware of any regulation that may affect the establishment of his new unit. Legal formations may be necessary at different stages of the start up. These formalities differ in relation to the form of enterprise adopted by the entrepreneur, such as sole proprietorship, partnership firm and company. The legal requirements also differ in reference to the size of the business unit, such as small scale, medium scale, or large scale enterprise. Moreover, consumer product enterprise and industrial product enterprise may attract different legal formalities. Following legal requirements are fulfilled for the establishment of a new business unit :

(1) Incorporation and Registration : There found various forms of business proprietorship in the private sector such as sole-trader, partnership, Joint Hindu family and company etc. In case of sole-proprietorship, partnership and Joint Hindu family, registration is not compulsory, while in case of company, incorporation and registration is essential.

INCORPORATION OF A COMPANY

Company is established through legal procedure and have a separate legal entity from its owners. Legal procedure of establishment a company is termed as incorporation. For this purpose, registration of company has to be made with the Registrar of companies. An entrepreneur is required to submit an application for registration following documents :

(i) Application form duly filled in and signed by an authorised person.

(ii) **Memorandum of Association :** The Memorandum of Association, is the charter of the company. This includes its objectives, its name, the address of its registered office, the capital which the company is authorised to raise, the nature of liability of members as well as the names, addresses and agreement of people who agree to form a company.

(iii) **Articles of Association :** The other important document is the articles of association which contains the rules and regulations relating to the internal management of the company. However, it is not necessary for a public company limited by shares to file the articles of association. If such public company does not file Articles of Association, it is deemed to have adopted 'Table A' of schedule I of the Act.

(iv) **Written consent of the directors :** Written consent of the directors who are agreed to act in that capacity, duly signed by each director, along gith a written undertaking by them to take the necessary qualification shares, if any, as provided in the articles.

(v) A copy of agreement with any individual for appointment as a managing director, or a whole- time director or manager.

(vi) A statutory declaration stating that all the legal requirements of the Act precedent to incorporation have been complied.

(vii) A letter of intent under Industries (Development and Regulation) Act, 1951, if the company s business comes with the purview of this Act.

(viii) Address of registered office of the company. However a company may file registered address within 30 days of its registration.

(ix) At the time of registration, the prescribed registration fees and filing fee for each document filed for registration are to be paid to the Registrar's office. After receiving these documents, Registrar scrutinise these documents and if he is satisfied that all the documents are in order, he shall enter the name of the company in the register of companies and issue a certificate of incorporation.

CAPITAL SUBSCRIPTION

Next step in the registration of a company is to raise capital for the proposed company. Company obtain the necessary capital by selling shares to the public. Following procedure is adopted for this purpose :

(i) Permission of public issue from 'The Securities and Exchange Board of India.

(ii) Agreements with tho underwriters, brokers and share issue managers.

(iii) Filing a copy of prospectus with the Registrar.

(iv) Invite the public to purchase the shares of the company by putting the prospectus in circulation.

(v) Receiving applications for shares through the company sbanker.

(vi) Formal resolution of allotment, if the subscribed capital is at least equal to minimum subscription of 90% of capital issue.

(vii) In case, minimum subscription is not received, the entire amount with application would have to be refunded at the end of 120 days from the circulation of prospectus.

(viii)Issue of allotment letters and share certificates.

(ix) In case a company having a share capital, but not issuing a 'prospectus', filing a 'Statement in lieu of Prospectus' with the Registrar at least three days before the first allotment resolution.

COMMENCEMENT OF BUSINESS

A public company cannot commence business immediately after incorporation unless it has obtained a certificate of commencement of business from the Registrar. Following documents have to be filed for this purpose :

(i) Shares payable in cash have been allotted to the extent of the minimum subscription;

(ii) Every director has paid in cash the application and allotment money on the shares taken by him;

(iii) No money is liable to be refundable to the applicants for failure to apply or obtain permission for the shares or debentures to be dealt in on any recognised stock exchange.

(iv) A statutory declaration duly verified by one of tho directors or the secretary in the proscribed form that tho above conditions have been complied with has been filed with the Registrar.

The Registrar will scrutinize those documents and if ho is satisfied, he shall issue a "certificate of commencement of Business, This certificate is conclusive evidence that the company can commence its business and use its borrowing powers

(2) **Small Unit Registration Certificate :** The entrepreneur of a small scale unit should seek registration of his selected project unit with the Directorate of industries. This will make the entrepreneur and his unit eligible for availing Government assistance. A unit is normally registered provisionally first and accorded permanent registration later.

(3) **Registration under the Factories Act :** An entrepreneur must registered his enterprise under the 'Factories Act, 1948', before starting the manufacturing unit. Factories Act contains provisions regarding licencing and registration of factories, working hours, health, safety and welfare measures, employment of women and young persons, annual leaves, dangerous operations etc. The Act fixes the minimum age of persons who can enter a factory for work at 14 years. The Act, lays down the provisions regarding cleanliness, ventilation, overcrowding, lichting, explosive gases, dust, fume, fencing of machinery etc.

(4) **Import License :** If imported raw-material and other equipments are necessary for the new business enterprise, then he should obtain the import licence from the export-import controller.

(5) **Permission of Finance Ministry :** For the agreement Of foreign collaboration, an entrepreneur must obtain the permission of finance ministry.

(6) **No Objection Certificate (NOC) :** The unit must obtained all necessary clearances. For example, NOC from Pollution Control Board is obtained if required.

(7) **Industries (Development and Regulation) Act, 1951 :** The licencing policy for industries is determined under this Act. The Act states that the Central Government may specify the requirements which shall be complied by small scale industrial undertakings to be regarded as a small scale or an ancillary industry. This may be done by the Central Government with a view ascertaining which small scale or ancillary industrial undertaking needs supportive measures, exemptions or other favourable treatment under this Act to enable them to maintain their viability and strength.

(8) **Foreign Exchange Regulation Act :** All foreign collaborations required the approval of the government and are subject to the regulations under the Foreign Exchange Regulation Act. All investment by foreign companies in India is permitted only with the approval of the Reserve Bank of India. The Reserve Bank of India's approval is again based on the approval of the investment proposal by the government.

(9) **Registration of Trademark :** According to Trade and Merchandise Marks Act, 1958 (India) the mark' "includes a device, brand, heading, label ticket, name signature, word, letter or numeral or any combination thereof." The purpose of registration of trademark is that the consumer may distinguish the product of manufacturer/service provider from others and therefore 'decepti.vely similar' trademarks are not allowed to be used because they can cause confusion to users. Once a trademark is registered as per provisions of Trade and Merchandise Marks Act, 1958 and Trademarks Act, 1999 no one else can use similar trademark on any of its packing. The trademarks are registered for unlimited period and helps in the promotion of sales.

(10) **Registration under the Sales-tax Authority :** An entrepreneur should get registered his enterprise in the sales-tax department of the state government and obtain certificate for this purpose. Besides above mentioned legal formalities, an entrepreneur have to fulfil some other formalities also depending on the nature of product produced by the new business unit. For

example he has to get registered his unit under the Service Tax Act, Food and Drugs Control Act etc.

Raising of Funds

Raising **investment funds** can offer a significant jumpstart to one's business and increase the likelihood of success. Depending on the type of business and its domain, an enterprise would like to raise capital for business, to either start its operations or grow it at a faster pace. Fortunately, there are various new entrepreneurial funding sources.

However, it is also important to select from the best source based on the entrepreneur's requirements and their financial standing. Partnering with a right investor can help a business soar to higher levels and sustainably achieve success.

*As per a recent survey, in 2016, a total of $4 billion **investment funds** were deployed in Indian start-ups. The volume increased by 3% from 2015.*

On the other hand, many entrepreneurs shut their shops due to lack of funding. Money is the bloodline for any business, and it needs the fuel called *capital* to survive the painstaking journey from ideation to growth. And that is a common reason, why most of the entrepreneurs at almost every stage are seeking outside investments.

Along with the cumbersome task of complying with all the legal requirements of incorporation, there is one more important area where startups need to put up significant amount of effort - raising funds, both to start the business and to operate it. Without this, your brilliant idea stays just an idea.

SEBI (Venture Capital Funds) Regulations, 1996, tried to fill the gap of capital funding for startups from institutional source. Before the emergence of venture capitalists in India, startups usually had a handful of options such as raising money from friends and family, private placements, IPOs and loans from banks or central as well as state level financial institutions namely, IDBI, IFCI, SIDBI, etc. Early 2007 - 2008 saw private investors enter the startup space and the formation of angel investing community.

Subsequently, in 2012, SEBI introduced Securities and Exchange Board of India (Alternative Investment Funds) Regulations that recognize AIFs as a distinct asset class with the objective to encourage startups and permit fund investment strategies in the secondary markets.

According to SEBI, Alternative Investment Funds refer to any fund established or incorporated in India as a trust/company/LLP which:

1. privately pools investment from investors, whether Indian or foreign, for investing it in accordance with the regulations
2. And is not covered under SEBI (Mutual Funds) Regulations, 1996, SEBI (Collective Investment Schemes) Regulations, 1999 or any other regulations that regulate fund management activities.

After exhausting your personal sources of finance - co-founders, (which is also known as 'bootstrapping' or self-funding), family, and friends some other alternatives for funding are:

Crowd-funding

An unconventional route, crowd funding refers to taking funds in the form of loan{1} or an investment, usually in smaller denominations, from large number of investors at the same time. The funding is done online for easy pooling of resources. You will have to put up a detailed business proposal mentioning the revenue model, goals, targeted markets, etc. on a digital crowd-funding platform. Investors can either pledge to pre-buy your product offering or make donations.

Seed funding

The term seed funding is based on the analogy of planting a tree (or business) with the help of a seed (or funds). Seed firms are also sometimes known as 'incubators', invest in early stages of startup often when the business is still just an idea. Substantial funds are raised to support market research and development for the company.

Angel funding

According to SEBI (Alternative Investment Funds) Regulations, 2012, angel investor is defined as "any person who proposes to invest in an angel fund and satisfies one of the following conditions -

1. an individual investor with net tangible assets of at least Rs. 2 crore, and
   a. has early stage investment experience,
   b. has experience as a serial entrepreneur,
   c. is a senior management professional with at least ten years of experience
2. Body corporate with a net worth of at least Rs 10 crore;
3. A registered Alternative Investment Fund or a Venture Capital Fund registered under the SEBI (Venture Capital Funds) Regulations, 1996.

Angel funds are defined by SEBI "as a sub-category of Venture Capital Fund under Category I- Alternative Investment Fund that raises funds from angel investors and invests in accordance of SEBI (AIF) regulations."

With their experience and knowledge, one can gain a lot more than money, for example, management & entrepreneurial skills, important insights, contacts.

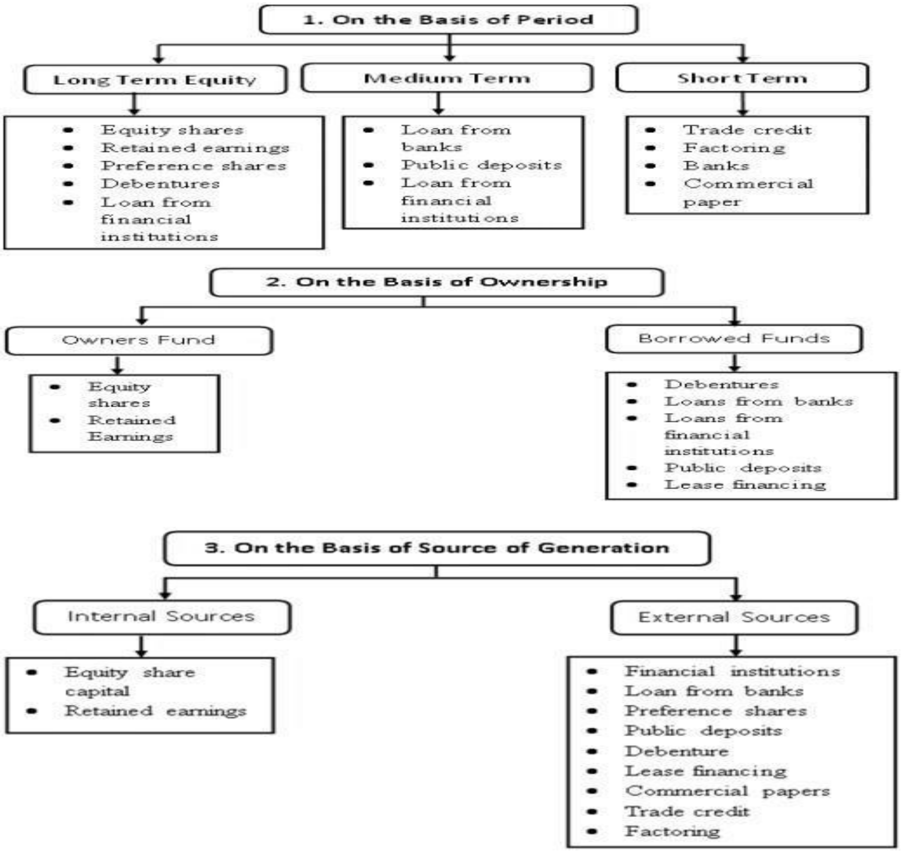
Series A,B, C funding

These rounds of funding differ based on the level of maturity of the startup and type of investors involved.

Series A funding is used by startups in optimizing product offerings and user base by creating business models that generate long-term profit. The important factor focused on this stage is scale of operations and users. Usually, early stage venture capital firms with high risk appetite are seen investing in this round of ..

Series B round of funding is the second round wherein the focus is on taking business to the next level in terms of scaling and expansion. Private equity investors and venture capitalists contribute to the capital of your business when certain pre-determined milestones are achieved. The cost of funding at this stage is higher as compared to Series-A funding.

Series C round of funding is the third injection of capital which is usually available to succes ..



<u>Venture Capital sources & documentation required</u>

Venture Capital

The term venture capital was originally coined in U.S.A. and has been developing world wide. The move spread in India in 1973 when R.S. Bhatt Committee recommended the formation of venture capital fund in the country. The concept of venture capital was evolved to help those persons who have good product ideas, but lack the necessary funds to convert these ideas into production. It is a source of finance for the new and untried enterprises having new ideas and new technologies with high risk, but with a potential for rapid growth. Venture capital is usually structured in the form of equity and debt capital. It is provided by the wealthy investors, firms, institutions and companies for all stages of financing the new venture. Some think that venture capital is the early-stage financing of new start-up ventures. Others think that venture capital is the financing of high and new technology-based enterprises. More accurately, venture capital is an alternative form of equity and debt financing made available to new ventures who have technically qualified entrepreneurs with inadequate funds, having high risk but good growth prospects. A few definitions of Venture Capital are as follows :

International Finance Corporation, Washington (IFCW) defines venture capital as “equity or equity featured capital seaking investment in new ideas, new companies, new products, new processes or new services that offer the potential of high returns on invest. ment. It may also include, investment in turn around situations, ” According to the Bank of England, “Venture capital is an activity by which investors support entrepreneurial talent with finance and•business skills to exploit capital gain.” According to Pratt, Venture capital is thought of as, “the early stage financing of new and young enterprises seeking to grow rapid Thus, venture capital is an alternative form o/ equity financing made available to new ventures and technically qualified entrepreneurs with inadequate funds, high risk and good growth prospects.

Entrepreneurial firms which are high risk units, high return ventures and which face the difficulty of funds get their finances from venture capitalists, This type of capital is provided only for new ventures.

Characteristics Or Essentials Of Venture Capital

The venture capital financing is different from traditional or conventional financing in that the traditional financiers invest in proven technologies and low risk ventures, whereas venture capitalists invest in new technologies and high risk ventures. Some of the main distinguishing features of venture capital may be summarised as follows :

(1) **High Risk :** Venture capitalists provide finance to high risk ‘high-reward ventures. These risks involve technology risk, market risk, liquidity risk or any other type of risk.

(2) **Equity-Debt Financing :** Venture capitalists manage for both equity and debt finances. They invest in shares to get high returns. They earn capital gains by selling the shares once the enterprise prove profitable. They provide debt financing in the form of debentures.

(3) **Long-Term Investment :** Venture financing is a long-term investment of funds. Funds are provided för 5 to 10 years. Venture capi!al is not repayable on demand. The investor has to wait for a long time to earn profit.

(4) **Participation in Management** : As already explained venture capitalist not only invests in the equity shareholding of the entrepreneurs company but also participates in the management affairs and gives his advice from time to time. Venture Capitalist has an active involvement in the business of the entrepreneur after making an investment. Thus we can say that venture capitalists don’t just invest, rather they build companies.

(5) **Creative Capital :** Venture Capital is termed as a creative capital as it propelled new ideas to major commercial successes. It helps entrepreneurs to launch enterprise with a specific promise.

(6) **Professional Entrepreneurs :** Usually, the venture capital is provided to those entrepreneurs who are professionally or technically qualified but lack adequate funds to start a new venture. The entrepreneur should have the capability to make an intense effort to do the business. He should also have proper knowledge of his markets, along with risk management quality.

(7) **New Technology :** Venture capitalists provide finance usually to those entrepreneur who try or employ new technology which may produce uncertain results.

Sources of venture capital

The concept of venture capital was originated in the U.S.A. Now it has become a worldwide concept in the field of risk financing of industrial projects. The development of venture capital in India is still in infancy, being about a decade old. It is a growing capital market. In fact in India, ‘risk financing is still in an evolutionary state. The funds available to Indian venture capital industry are small. What is the need or relevance of venture capital in India when there are commercial banks and financial institutions to provide funds to industrial enterprises, small or large ? In developed countries, where there is highly progressive industrial environment as well as advanced entrepreneurial culture, it is common for entrepreneurs to set up companies to produce new products by Obtaining funds from venture capitalists.

On the other hand, in India and also in other developing countries, 'risk' financing of this type is yet in its infant stage. Of course, there are a large number of commercial banks and financial institutions in India, which provide 'traditional' (non-risk) financing mainly to those enterprises that use proven or established technologies with minimum level of risk. Such financing is collateral-security oriented and asset-based. It involves uniform repayment of fixed instalment. It is security oriented rather than risk-oriented. Traditional finance has a preference for foreign technology firms, and do not trust the entrepreneurs who adopt new products or new technology involving greater risk. In this background of weaknesses or drawbacks of traditional finance the venture capital assumes an important role to play in providing risk finance to small and medium size entrepreneurs. Sources of Venture Capital in India may be divided into three categories :

(I) All India Level Venture Capital Funds. (Il) State-Level Venture Capital Funds. (Ill) Specific Venture Capital Funds.

(1) All India Level Venture Capital Funds :– Many Venture Capital Funds are established at All India level to provide venture capital in India. Some of the important venture capital funds are as follows :

(1) IFCI Venture Capital Fund Limited : IFCI provided venture capital assistance for the first time in 1975 after the establishment of risk capital foundation (RCF). The financial capital assistance under IFCI's risk foundation scheme has been mainly for the traditional industries like textile, iron and steel and chemical. It provides assistance basically for technologists and professionals. General limit of contribution is up to 50% of promoter's contribution, subject to a ceilling of Rs. million. Only public limited companies were eligible for this finance. IFCI charge no interest on such loans but a nominal service charge is levied. Mode of repayment was that, repayment will be out of dividends and the period of repayment is fixed according to the facts of each case.

(2) IDBI Venture Capital Fund : IDBI Venture Capital Fund (VCF) was started in 1986 with an initial capital of Rs. 10 crore. This fund provides venture capital to low and medium grade ventures. IDBI has started seed capital scheme for venture capital finance Main points of seed capital scheme of IDBI are :

(i) Project cost upto 'Rs.Æ0 'millions'and project should be in small or medium firms.
(ii) Assistance will not exceed Rs. 1.5 per project.
(iii) Debt-equity norm of 2 : 1 is stipulated.
(iv) Free of interest loans and nominal service charge.
(v) Assistance is provided through SIDCs/SFCs.
(vi) Policy of being lender of last resort for financial requirements.

(3) ICICI Venture Management Company Ltd : The Government of India issued Venture Capital Guidelines in Novem- ber, 1988. These guidelines authorised all India Financial Institutions, Commercial Banks and their subsidiaries to launch venture capital companies. ICICI in 1988 formed Technology Development and Investment Corporation of India. (TDICI). This corporation managed various schemes •of venture capital financing on commerciallines. This is also the largest venture capital firm in India. It provides assistance to industries directly or through venture funds which are managed by it for other institutions and venture funds out of its own resources. TDICI accepts and evaluates the promotor's business plan by knowing his management team, nature of his product, market conditions for his product, competition, his investment requirement etc. TDICI goes through the entrepreneur's business plan, if it finds the plan to be good, and the promotor is clear about his business he gets, his work is almost done, otherwise his project is dropped.

(4) Canbank Venture Capital Fund Limited (CVCFL) : Canbank Venture Capital Fund Limited was established in 1989. At present Canbank has three subsidiary units which possess Rs. 164 crore, Rs. 10•5 crore and Rs. 30 crore respectively. Up to 30th March 2003 Canbank has provided financial aid of Rs. 3424 crore to 51 institutions. Influenced by the success of these venture funds, Canbank is going to establish a fourth venture fund subsidiary, which will be able to provide assistance of venture capital of Rs. 100 crore.

(11) State Level Venture Capital Funds :- In India various state level venture capital funds have been established by the State Governments after realising the significance and role of venture capital in industrial development. These venture capital funds have been promoted by state government. A few among them are :

(1) Gujarat venture Finance Limited (GVFL) : Under venture capital funds sponsored by state level financial institutions is GVFL promoted in July, 1990 to provide venture capital for the commercialisation of new technological developments and innovative products. It shares risk of entrepreneurs by providing financial assistance in the form of equity and quasi equity.

(2) Punjab Infotech Venture Fund (PIVF) : PIVF is dedicated to investing in companies in the Information Technology Sector within the State of Punjab. The Fund's investments in companies will be through the route of equity and quasi equity instruments. The Fund will seek to achieve its returns through dividends and capital gains at the time of divestment through an initial public offering or a negotiated sale of its holding. The Fund is being managed by Punjab Venture Capital Limited, an asset management company, promoted by the PSIDC acting as the nodal agency of the Government of Punjab.

(111) Specific Venture Capital Funds Despite of Commercial Banks, Private Sector Banks and Financial institutions are also providing venture capital funds to entrepreneurs. Some of these VCFs are :

(i) India Investment Fund which is established by Grindlays Bank and afterwards it was taken over by Standard Chartered Bank.

(ii) Credit Capital Venture Fund established by Credit Capital Corporation.

(iii) Technology Development and Information Co. Ltd. At present around 16 private sector funds are registered with SEBI and this number is expected to grow faster.

Difference Between Traditional and Venture Capital

Basis of Distinction	**Traditional Financing**	**Venture Capital Financing**
Technology	Traditional Financing	
Risk	It involves low risk.	It involves high risk.

Security	The lender adopts a policy of 'playing safe' and insists on some valuable collateral security for repayment of loan amount.	This is not necessary to demand security for venture capital financing.
Participation in	Investor does not take any responsibility for management of the borrower's enterprise.	The venture capitalist actively involves himself in the management of borrower's firm.
Finance Stage	It is provided in the developmental stage.	Basically it is provided inthe start-up stage, although it is also given for expansion, development or traditional acquisition purpöses
Period	it is generally a medium-term finance	It is a long-term financing.
Amount of Funds	Traditional lenders provide small funds.	Venture capitalists provide huge funds.
Relations	They maintain conditional commercial relations.	They maintain long- term business relation-ships with entrepreneurs.

Explain the Venture Capital Fund.

According to SEBI or Securities and Exchange Board of India, Venture Capital Fund is a Fund registered in the form of a company or corporation or trust according to the guidelines of SEBI and :

(i) Have a sufficient fund of capital;

(ii) Collect the fund according to the prescribed rules of SEBI;

(iii) Invest Funds according to the rules laid down by SEBI.

A venture capital fund can be constituted in the form of a trust or a company. Venture capital fund appoints on asset management company to manage the portfolio of the fund. A venture capital fund should have Rs. 5 crore (Rs. 50 million) before it can start venture capital activities. As per guidelines issued by the Central Board of Direct Taxes, a venture capital fund could invest upto 40% of the Paid up capital of investor company or upto 20% of the corpus of the fund in one venture.

<u>Various documents required for venture capital.</u>

Venture capital process is different from normal project financing. Tyebjee and Bruno (1984) have given a model of venture capital investment activity which, with some variations, is conmonthly used at present. According to them the venture capital investment process is a sequential process that involve five steps. Documents required at each stage are as follows :

(1) Deal Orientation : At this stage, a letter of introduction is necessary from the referring party sent to the Venture Capital Company. It should present details about the potential venture, its technical viability and good image of the entrepreneur.

(2) Screening : Screening of proposals is necessary to save the time and money cost. Only proposals which clear screening test are considered for evaluation. At this stage the Venture Capital Company may ask for technology and product profiles as well as venture or investment profile depending on the criteria used in the screening process.

(3) Evaluation or Due Diligence : Evaluation or due diligence means careful and proper detailed analysis, The proposals that have successfully passed through the screening process are then subjected to a detailed evaluation process called due diligence. Most of the venture coming to a venture capitalist are new ventures being set up by first-time promoter, neither the ventures have any track record nor the entrepreneur are have any operating experience. In such cases, the venture capital company uses a subjective but comprehensive evaluation. At this stage the Business Plan is an important document upon which the evaluation is based. Most venture capitalists ask for a business plan to make an assessment of the possible risk and return on the venture. Well prepared plan is the best introduction of the entrepreneur who is going to set up a new venture. A detailed and well-organized business plan is the only way to gain the attention Of the venture capitalist and to obtain the needed funds.

(4) Deal Structuring : If the proposed venture and its business plan are found as viable, then venture capitalist and the entrepreneur negotiate the terms of the deal, such as : the amount Of money to be invested, the form of investment (equity or debt), the price of Investment, exit period, etc. This process is termed as deal structuring. At this stage, a written agreement is prepared between the entrepreneur and the venture capitalist. This contains all the terms and conditions agreed between them. This agreement is written on a stamp paper, signed by both and is registered with the government agency. It is treated as a valid evidence before a court of law in case of a dispute.

Explain the Seed Capital.

Seed Capital is relatively small amount of capital provided to an entrepreneur, generally to prove a concept or an idea. According to The European Venture Capital Association "Seed

Finance is the fianncing of the initial product development or the capital provided to an entrepreneur to prove the feasibility of profitability; seed capital in other words is a start up capital. " According to Mumford and Dotzler, "seed capital is used to finance initial research and development on the concept, build a prototype, to market research analysis the business plan. " Seed Finance stage is the most difficult stage to finance because (i) the entrepreneur's idea is yet to take a definite and commercial shape, (ii) he has no business plan, (iii) his product has recently passed through research and development stage (iv) there is yet no complete management team. When an entrepreneur who does not have adequate funds of his own, approaches the suppliers of seed capital with his proposal. It is the riskiest stage of venture capital because returns from seed capital investments typically don't start to come through for seven to ten years.

Advantages of Venture Capital

- They bring wealth and expertise to the company
- Large sum of equity finance can be provided
- The business does not stand the obligation to repay the money
- In addition to capital, it provides valuable information, resources, technical assistance to make a business successful

Disadvantages of Venture Capital

- As the investors become part owners, the autonomy and control of the founder is lost
- It is a lengthy and complex process
- It is an uncertain form of financing
- Benefit from such financing can be realized in long run only

Forms of Ownership

A key first step for any entrepreneur is setting up an organization that will be used to formally embark on the business journey, but many new business owners struggle to identify the best way to move forward. These are the most common ways to organize a business, from the simplest through the most complex.

1. Sole Proprietorship

A sole proprietorship is the most basic form of business ownership, where there is one sole owner who is responsible for the business. It is not a legal entity that separates the owner from the business, meaning that the owner is responsible for all of the debts and obligations of the business on a personal level. In exchange for that liability, the owner keeps all the profits gained from the business. This form of business ownership is easy and inexpensive to create and has few government regulations, making it a more flexible type of ownership with complete control at the discretion of the owner. In addition, profits are taxed once, and there are some tax breaks available if the business is struggling. Sole proprietorships often are limited to the resources the owner can bring to the business. For these reasons, sole proprietorships are often most appropriate during the early stages of a business where the owner has little capital/resources to work with but also has few debts to pay.

2. *Partnership*

Partnerships are a form of business ownership where two or more people act as co-owners. There are two forms of partnerships, which are General Partnerships and Limited partnerships, differentiated primarily by the liability coverage by the owners. In a general partnership, all owners of the business have an unlimited liability in the business (the same as a Sole Proprietorship). For a limited partnership, at least one of the partners has a limited liability, meaning they are not personally responsible for the debts of the business. Regardless of the type of partnership, they are relatively easy and cheap to create, have few government regulations and are only taxed once, like a sole proprietorship. The added benefit of a partnership is the combination of knowledge and resources that are brought to the table thanks to the additional owners. Profits do have to be shared between owners and there is always the potential for conflicts to arise between partners over business decisions. This type of ownership is often useful in the early stages of the business where multiple people are involved. Due to the sharing of profits and the additional resources, this type of ownership is often expected to yield higher growth rates then a sole proprietorship.

3. *Corporations*

Unlike the previous two examples, Corporations are a form of ownership that is a legal entity separate from its owners. This creates a limited liability for all owners, but results in a double taxation on profits (first as a corporate income tax, then as a personal income tax when the owners take their profits). Corporations tend to have an easier time raising capital then sole proprietors or partners in large part due to the greater sources of funding made available to them, such as selling stock. However, this does result in greater government regulations for corporations, such as requirements for more extensive record keeping. In addition, setting up a corporation is much more difficult, requiring more resources and capital to cover expenses and create legal documentation. This ownership form is best suited for fast growing or mature organizations that have owners looking for limited liability.

4. *Limited Liability Company*

A form of business ownership that is taxed like a partnership but enjoys the benefits of a limited liability like a corporation is a "limited liability company". In comparison to a corporation, it is simpler to organize and does not receive double taxation. While simultaneously receiving more credibility then a partnership or sole proprietor when it comes to gathering resources such as working capital. Unfortunately, this form of ownership is usually reserved for a group of professionals such as accountants, doctors and lawyers.

5. *S Corporation*

A lesser known ownership style, an S corporation is a type of business ownership that allows its owners to avoid double taxation because the organization is not required to pay corporate taxes. Instead, all profits or losses are passed on to owners of the organization to report on their personal income tax. This form of ownership does allow for limited liability, similar to a corporation, but without the double taxation. The disadvantages of this organization's special nature is the increased level of government regulations and the restrictions on the number and type of shareholders it may have. This type of ownership is used in the mature stage of a businesses lifecycle and often by private organizations due to the restrictions on ownership.

6. *Franchise*

Franchising is a form of ownership far different from the ones previously mentioned. This form of ownership allows a franchisee to borrow the franchisor's business model and brand for a specified period. It comes with a list of advantages including: training on how to operate your franchise, systems and technologies for day-to-day operations, guidance on marketing, advertising and other business needs, and a network of franchise owners to share experiences with.

The main disadvantages to this ownership structure are franchising fees, royalties on sales or profits, and tight restrictions to maintain ownership. Franchise owners also have limited control over their suppliers they can purchase from, are forced to contribute to a marketing fund they have little control over. If a franchisee wants to sell their business, the franchisor must approve the new buyer. Despite these disadvantages, franchises are great for owners who are looking for an 'out of the box' to owning their own business.

7. Co-operative

Cooperatives are organizations that are owned and controlled by an association of members. This form of ownership allows for a more democratic approach to control where each share is worth the same amount of votes, similar to a corporation with common stock. It also offers limited liability to its owners and equal profit distribution based on ownership percentage. Disappointingly, the democratic approach to decision making results in a longer decision making process as participation from all association members is required. Conflicts between members can also arise that can have a big impact on the efficiency of the business. Co-operatives are often used when individuals or businesses decide to pool resources to achieve a common goal or satisfy a common need, such as employment needs or a delivery service.

Type of Corporation	**Advantages**	**Disadvantages**
Sole Proprietorship	· Easy and inexpensive to create · Flexibility and control to your liking · Few Government regulations · Tax advantages if struggling · Profits taxed once	· Unlimited liability, meaning business debts are personal debts · Limited source of financing · Limited resources
Partnerships (General/Limited Partn	· Easy to organize · Combined knowledge, skills and resources · Few Government regulations · Taxed once	· Unlimited liability for some partners* · Possible conflict development between partners · Shared profits

ershi ps)		
Corpo ratio n	· Limited liability · Easier to raise capital due to greater sources of funding	· Being taxed twice (as a legal entity and as an owner) · Greater Government regulations to adhere to · More expensive to set up · Extensive record keeping required
Limite d Liabil ity Com pany	· Simple to organize and operate	· Generally only available to a group of professionals such as

	· Flexible in nature · Taxed as a partnership	lawyers or accountants
S Corporation	· Limited liability for owners · Greater credibility for financing · No double taxation	· Greater Government regulations to adhere to · Restrictions on number and type of shareholders
Franchise	· Superior training and systems offered · Guidance on marketing, advertising, financing, accounting etc. · Franchise networks to share experiences (great knowledge base)	· One-time Franchising Fee for owning a franchise location · Recurring royalty fees as a percentage of sales or profits · Tight restrictions that limit control · Purchases must be made from specific suppliers · Contributing to marketing fund, but having no control over it · Selling franchise location requires approval from franchisor
Co-opera	· Democratic control · Limited liability · Equal profit distribution	· Longer decision making process · Participation of all members required · Conflict possibility between members · Extensive record keeping

t **i** **v** **e**		required

UNIT – 3

<u>Meaning of Entrepreneurial Behaviour</u>

Behaviour is a manifestation of what a person thinks, feels and acts. An entrepreneur is a creative person. Need for self actualisation as manifested in the need for achievement forces him to create something new, a new product, a new way of doing things, a new source of raw material, a new market etc. Behaviour is always caused and is never spontaneous. Behaviour is basically goal- oriented. Entrepreneurial Behaviour includes the goal-oriented acts or decisions of an entrepreneur. The entrepreneurial behaviour means the manners or way in which the entrepreneur deals with its total environment : internal and external. It is the way or approach to look at the physical and human resources and the society. The entrepreneurial bvehaviour is a view of or orientation towards risk-bearing, innovation, achievement, goal-setting, ethics, social responsibility, motivation, challenges and values cf human society, and other psychological elements.

Characteristics of Entrepreneurial Behaviour

The entrepreneurial behaviour is different from the capitalist's behaviour. The capitalists assume a traditional or conservative approach. He believes in "safe-playing" while investing his money in the enterprises. He is concerned mainly with his share of interest on his investment. On the other hand, entrepreneur loves to take risk and tends to establish a new enterprise and adopts a new technology, or a new product, or tries to find cut a new raw material. He is always looking out for a new thing or a new method. He is a high achiever. He is guided mainly by achievement motivation. Main characteristics of entrepreneurial behaviour may be summarised as follows :

(1) **Intitiative Behaviour :** It is the entrepreneur who takes or imitate the first move towards setting up of an enterprise. Entrepreneur basically is an innovator who carries out new combinations to initiate and accelerate the process of economic development.

(2) **Challenge accepting behaviour :** Entrepreneurs take problem as a challenge and put in their best for finding out the most appropriate solution for the same. They will first of all understand the problem and then evolve appropriate strategy for overcoming the problem.

(3) **Assertive Behaviour :** An assertive person knows what to say, when to say, how to say and whom to say. He believes in his abilities and ensures that others fall in line with his thinking, aimed at promoting the interests ofthe organisation.

(4) **Persuasive Behaviour :** A successful entrepreneur through his sound arguments and logical reasoning is in a position to convince others to do the works the way he wants them to do. It is not physical but intellectual force he will use for convincing others.

(5) **Effective Monitoring :** Entrepreneurs ensure that everything is carried out in their organisations as per their wishes. They ensure regular monitoring of the working so that the goals of the organisation are achieved in best possible manner.

(6) **Looking for Opportunity :** An entrepreneur is always on the look out or searching for opportunity and is ready to exploit it in the best interests of the organisation.

(7) **Persistence :** An entrepreneur is never disheartened by failures. He believes in the Japanese proverb 'Falls even times, stand up eight'. He follows Try-Try Again for overcoming the obstacles that come in the way of achieving goals.

(8) **Information Seeker :** A successful entrepreneur always keep his eyes and ear open and is receiptive to new ideas which can help him in realising his goals.

(9) Quality Consciousness : Successful entrepreneurs do not believe in moderate or average performance. They set high quality standards for themselves and then put in their best for achieving these standards. They believe in excellence, which is reflected in everything they do.

(10) Recognizing the importance of Business Relationships : Entrepreneur acts to build repport or friendly relationships with customers. He sees interpersonal relationships as a fundamental business resource. He places long-term goodwill over short-term gain.

(11) Commitment to Work : Successful entrepreneures arc prepared to make all sacrifices for honouring the commitments they have made. Whatever they commit, they take it as a moral binding for honouring their commitments, irrespective of the costs innolved.

(12) Independent Behaviour : Entrepreneurial behaviour posseyses strong need for independence and due to this desire they are motivated to start a business. They always concentrate to achieve their goals.

Psychological factors to affect the entrepreneurial behaviour.

The behaviour of an entrepreneur is dependent largely on his psychology and motives which are the main determinants of be. haviour. These motives are based on needs for survival and growth. The movements of an entrepreneur are affected by the psychological background. Many theorists Akouri, McClelland, Javillionar & Winter have given views related to psychological factors as follows :

(1) Achievement Motive : Achievement motive is most important for an entrepreneur. It is this motive which motivates people to do something different and extraordinary so that one may feel that he has achieved or created something which others are not able to do..lt motivates an entrepreneur to take an initiative for innovation. It also makes one personally responsible for his actions and performances. It helps to develop self-reliance and develops the spirit of risk-taking which is very -essential part of entrepreneurial behaviour, one will not establish a unit unless he is prepared to take risk.

(2) Desire to Influence Others : Strong desire of the need for power, helps a person to become a successful institution builder, Thus, it is necessary that an entrepreneur must have the ability of self-management with a strong will power. Thus, they possess a strong desire towards the need of influencing others.

(3) Desire for Independence : Entrepreneur possesses strong desire for independence and it is only due to this desire that they are motivated to start a new business. According to psychologists, the feeling of independence is acquired by them through the family atmosphere. Due to this they do not want to work under anyone rather they like to work independently.

(4) Innovation : This is an important psychological factor Of entrepreneurs. Generally, an entrepreneur does those acts which are not taken up by other persons. They transform the creative ideas into useful applications. Accordmg to Schumpeter, a person is an entrepreneur only when he is an innovator, engaging himself in an innovative behaviour. Thus, innovative behaviour is an entrepreneurial behaviour,

(5) Hope for Success : Entrepreneurs are always hopeful for future success. They work for being successful which enlightens them with the confidence, positive attitude and high energy level. Hope for success makes their behaviour strong and stable.

(6) Calculated Risk Taking : Entrepreneur is a person who is always in a position to accept challenging job, He works on those projects only, which are risky but have a probability of success through their efforts. He does not rely on those ventures, which totally depends on chance. In other words, the entrepreneur belives in calculated risk-taking.

(7) **Immediate feed back :** Entrepreneur wants immediate feedback of the progress of his entrepreneurial targets so that he can improve the way of achieving the targets and his behaviour changes according to the situations.

(8) **Self-Efficacy :** An entrepreneur has a drive for self-efficacy. They want to become the problem solver, instead of problem avoiders. They do not want to copy others but they want others to copy them. Further they feel proud of their achievements and live in the present.

(9) **Self-Expression :** The desire for self-expression appears to be a common thread and may help explain why so many men and women prefer to work for themselves than for someone else.

(10) **Self Confidence :** Entrepreneurs believe in themselves. They have confidence that they can outdo anyone in their field. They tend not to accept the status quo, believing instead that they can change the facts. Often, they insist the odds are better than the facts would justify. They have winning habits. On the basis of self-confidence, they become overachievers.

(11) **Different Way :** Although all people are different, entrepreneur is different from all others. They judge the world in terms of their own beliefs, values and expectations. A good entrepreneur behaves like human being rather than rational machine. They sce their work world differently. They differ in their psycho-personalities, needs, time periods, social surroundings and perception.

Meaning and Definition of Innovation

Innovation is the process of taking a creative idea and turning it into a useful product, service or work method. It implies doing new things, It includes introduction of new products, creation of new markets, application of new method of production, discovery of new and better sources of raw materials and developing a new and better form of industrial organisation. Innovation may be used on the application of knowledge produced by research. Innovation is different from invention. Invention implies discovery of new ideas, new products and new methods whereas innovation refers to the application of inventions to make new combinations and thereby produce satisfaction and profit. According to Paul E. Plsek, "Innovation is the first, practical, concrete implementation of an idea done in a way that brings broad-based, extrinsic recognition to an individual or organisation." In the words of Peter F. Drucker, "Innovation is the means by which the entrepreneur either creates new wealth-producing resources or endows existing resources with enhanced potential for creating wealth. '

Characteristics of Innovation

On the basis of above discussion, it can be concluded that :

(i) Innovation implies action, not just conceiving new ideas.

(ii) It is a process of changing, experimenting, transforming and revolutionising.

(iii) It is a key aspect of entrepreneurial activity,

(iv) It is a "creative destruction".

(v) It leads to technological changes and employment growth*

(vi) It is a pervasive attitude, feeling, an emotional state, an ongoing commitment to newness,

Relationship between Innovation and Entrepreneur

Increasingly, creativity and innovation are seen as being the key to survival in an ever-more competitive and global economy. In fact change and innovation are becoming a ‘way of life’ for most entrepreneurs. An entrepreneur always takes a personal responsibility for encouraging any type of innovative idea, product, or process in the enterprise. Peter Drucker has rightly observed that "Innovation is the specific tool of entrepreneurs, the means by which they exploit changes as an opportunity for a different business or a different service. It is capable of being presented as a discipline, capable of being learned and practised. Entrepreneurs need to search purposefully for the sources of innovation, the changes and their symptoms that indicate opportunities for successful innovation. kid they need to know and apply the Principles of successful innovation." Drucker is of the opinion that an entrepreneur is one who always searches for changes responds to it andexploits it as an oppor tunity. Innovation is treated as an instrument of entrepreneurship. R.M. Kanter says, "Winning in business today demands innovation" and such is the stark reality facing today s entrepreneurs. In the dynamic, chaotic world of global competition, entrepreneurs must create new products and services and adopt new technology, ifthey are to compete successfully, The organisation that is not creative and innovative may not survive. Thus, entrepreneurs are looking for ways to encourage and foster in creativity and innovation on both the individual and the venture level. Thus it can be concluded that innovation and entrepreneurs are indispensable to each other. Both are useless and incomplete in absence of one another.

Psycho-Theories and Entrepreneurial Behaviour

Entrepreneurial behaviour is influenced by many psycho-concepts such as perception, motivaticn, optimism, conditioning, cognition, self actualisation or other psychological thoughts, These psychological processes influence the thinking and behaviour of entrepreneur. Main psycho-theories of entrepreneurial behaviour may be d •scussed as follows

(1) Achievement Theory of McClelland : This theory was propounded by David Mc-Clelland in his book, 'The Achieving Society'. He states that people who persued entrepreneur like careers were high in need achievement. The n-achievement is called a desire to do well, not so much for the sake of social recognition or prestige but for the sake of an inner feeling of personal accomplishment. It is this motive of n-achievement that guides the action of entrepreneur. People with high achievement behave in an entrepreneurial way. They do things in a new and better way. They make decisions under uncertainty. Entrepreneurs with a high-need to achieve feel that their success or failure is due to their own actions. McClelland indicates that there are five major component to the need achievement trait. (i) responsibility for problem solving, (ii) setting goals, (iii) reaching goals through one's own effort, (iv) the need for and use of feedback, and (v) a preference for moderate levels ofrisk-taking. Thus people with high need for achievement are motivated to be an entrepreneur.

(2) Self-Monitoring Theory : Self-monitoring is a personality trait that measures an individual's ability to adjust his behaviour to external situational factors. This theory states that high monitor entrepreneurs can be more successful in entrepreneurial jobs and managerial positions where they are required to play multiple roles, They tend to display their true dispositions and attitudes in every situation. The high self-monitor entrepreneur is capable of putting on different faces for different audiences.

(3) Risk-Propensity Theory : Risk-propensity is the to which an individual is willing to take chances and make risky decisions. An entrepreneur with a high risk propensity might be villing to experiment with new ideas and gamble on new products He might also lead the venture in new and different directions Thus, risk taking-whether financial, social or psychological is an impatantpart ofthe entrepreneurial behaviour. (4) Motivation Theory : People differ not only in their ability to do, but also in their will to do or motivation. Motives are the mainsprings of action. Entrepreneurial motivation may be defined as a set ofmotives, needs, urges or desires such as need for power, to earn money or to be one's own boss, to dominate and influence others by earning industrial power etc. These behavioural dimensions motivate the people to start a new venture.

(5) Role Models and Support Systems Theory : Every entrepreneur has a choice of a role model. He follows and learns for the behaviour of his role model. Many new entrepreneurs need guidance and moral support. In addition to moral encouragement, the entrepreneur needs advice and counsel throughout his entrepreneurial behaviour. Each entrepreneur needs to establish both a moral and a professional support network. These contacts provide confidence, support, advice, and information. As one entrepreneur stated, "In your own business, you are all alone. There is a definite.need to establish support groups to share problems with and gain overall support for the new venture. "

What is the difference between Innovation and Invention ?

Innovation is not similar to invention. Main points of difference between invention and innovation may be summarised as follows :

(1) **Nature of Activity :** Invention is the creation of something new, whereas innovation is the economic exloitation of the new idea or resource; in other, words, innovation is the transformation of an idea or resource into useful commercial applications.

(2) **Results :** Invention results in new knowledge Whereas, innovation results in the products, services, or processes.

(3) **Position :** All inventors are not innovators, while all innovators are inventors.

<u>Social Responsibility</u>

The business or entrepreneur is a part of society. Business is performed in the society, for the society, with resources of the society. The society also provides the opportunity for development and expansion of the business. Hence, business has specific responsibilities for the local community and place, where the business is performed.

Every enterprise, are either in private or the public sector should make efforts to improve the conditions of the public of the surrounding areas, should arrange employment for unemployed and should help the needy person.

James and stoner said, "Values are a relatively permanent desire that seems to be good in them". Social Responsibility implies that business man should oversee the operation of an economic system that fulfils the expectations of the public. - W.Fredick

Social Responsibility has been defined by Andrews "By social Responsibility, we mean the intelligent and objective concern for the welfare of society that restrains individual and corporate behaviour from ultimately destructive activities, no matter how immediately profitable, and leads in the direction of positive contributions to human betterment, variously as the latter may be defined."

Ethics And Social Responsibility For An Entrepreneur Social Responsibility means eliminating corrupt, irresponsible or unethical behaviour which might harm to the community, its people and the environment.

1) Public Image. The activities of an entrepreneur towards the welfare of the society earn goodwill and reputation for the business. People prefer to buy products of a company that engages itself in various social welfare programs. Again good public image also attracts the honest and competent employees to work with such employers.

2) Employee Satisfaction. Employees are the part of the society. If you satisfy your needs, then you are doing social work.

3) Ethical Leadership. It is the belief that what entrepreneur does has a strong influence on employees. If manager cheats, Lies, steals or manipulates, then they are sending wrong signals to employees.

4) A social Entrepreneur is an individual or organization who seeks out opportunities to improve society by using practical, innovative and substantial approaches. Since last three

decades, HDFC contributes 7% of its income to support community needs. Mahindra Tech employees donated one day salary to help victims of Bihar floods. Wipro has set up a foundation named Azim Premji Foundation to help improve education of the elementary schools in rural India.

5) Environment Management. Managers and Organizations can do many things to protect and preserve the natural environment which includes plastic less business by giving paper bag, creating eco-friendly product, by eliminating production.

6) Consumer Awareness. Consumers have become very conscious about their rights. If you are giving high quality products at cheap rate, that is kind of social Responsibility

Causes of Growing Concern for Social Responsibility

- Social responsibility is a very effective exercise of public relations.
- Image building of a business house in a society.
- Two-way activities, CSR make the upliftment of society, which in turn will co-operate with business firm in achieving their business goals.
- To make the best use of natural resources so as to raise the level of national income and standard living of people.
- To create more and more employment opportunities for semiskilled people
- To protect the ecology of nation.
- To contribute to the economic development of backward region of the country.

<u>Social Responsibilty of an Entrepreneur Towards Different Sections of The Society</u>

1. Responsibility towards Employees:

- Fair wages and salaries
- Adequate Basic Facilities like safe drinking water, electricity, canteen, hygienic toilets.
- Skill development programmes.
- Good and safe working environment.
- Retirement benefits and pension schemes
- Collective bargaining
- Insurance cover
- Medical facilities

2. Responsibilty Towards Customers:

- Charge reasonable price for products or services.
- Supply of right quality of goods in right quantity.
- No use of manipulated or false advertisements.
- Avoid unfair selling practices.
- Fair guarantee of product

3. Responsibility Towards Shareholders:

- A fair return on investment.
- Safety of invested capital.
- Regular and complete information about the performance and progress of the company.
- Regular Payment if dividend

4. Responsibility Towards Suppliers, Creditors:

- Maintain healthy and co-operative inter-business relationship between different businesses. Provide accurate and relevant information to creditors.

- Payment of price of materials on time.
- Prompt payment of interest on borrowed funds.
- Producing original documents for credit processing.

5. ***Responsibility Towards Public in General:***

- Help the weaker section of the society.
- Creation of job opportunities.
- Improvement in living standards.
- Building of basic infrastructure like roads, sewerage.
- Health and educational development schemes.
- To make best use of society's resources for their welfare.

6. ***Responsibility towards Government:***

- Payment of corporate tax in correct amount with no manipulation of profit figures.
- To avoid corrupting public servants by offering bribe.
- To encourage fair trade practices.
- To avoid monopoly practices.
- To improve national income.

<u>Top Companies Follow CSR Practices In India</u> ***Mahindra & Mahindra***

Key CSR Areas: Focus on the girl child, youth and farmers through programs in the domains of education, public health and environment. Mahindra Pride Schools provide livelihood training to youth from socially and economically disadvantaged communities and have trained over 13,000 youth in Pune, Chennai, Patna, Chandigarh and Srinagar.

L&T

Key CSR Areas: Water and sanitation, education, healthcare and skill building. L&T partners with local governments on health programs focused on reproductive health, tuberculosis & leprosy control, integrated counselling & testing centres for HIV/ AIDS. L&T's community health centres are located at Mumbai, Thane, Coimbatore, and Chennai.

Infosys

Key CSR areas: Works with Infosys Foundation, headed by Sudha Murty, towards removing malnutrition, improving healthcare infrastructure, supporting primary education, rehabilitating abandoned women and children and preserving Indian art and culture. Infosys Foundation USA is focused on bridging the digital divide in America by supporting computer science education and training in underrepresented communities.

Jubilant Life Sciences

Key CSR Areas: The Jubilant Bhartia Foundation (JBF) focuses on elementary education, improving health indices, employability and promoting social entrepreneurship. Jubilant CSR programs are implemented around its manufacturing locations in six areas in India.

Bharat Petroleum

Key CSR Areas: Quality education (strengthening primary, secondary education and empowering teachers), water conservation, skill development (employment linked skill training to the underprivileged with an inclusive approach for women, unemployed youth and persons with disabilities), health/hygiene and rural development

Conclusion All the Entrepreneurs should consider ethics and social responsibility as their part of life. Doing business legally and ethically will lead a development to the country. The entrepreneur should do business without affecting the society. We all have an image of our better selves-of how we are when we act ethically or are"at our best". We probably also have an image of what an ethical community, an ethical business an ethical government, or an ethical society should be Creating ethical organizations and governments makes our society as a whole ethical in the way it treats everyone. The government also should take necessary steps for the development and welfare of Entrepreneurs.

Entrepreneurship Development Programme (EDP)

Entrepreneurship Development Programme (EDP) is a programme which helps in developing the entrepreneurial abilities. The skills that are required to run a business successfully is developed among the people through this programme. Sometimes, people may have skills but it requires polishing and incubation. This programme is perfect for them. This programme consists of a structured training process to develop an individual as an entrepreneur. It helps the person to acquire skills and necessary capabilities to play the role of an entrepreneur effectively. As per National Institute of Small Industry Extension Training, Hyderabad, an EDP is an effort of converting a person to an entrepreneur by passing him through a thoroughly structured training. An entrepreneur is required to respond appropriately to the market and he/she is also required to understand the business needs. The skills needed are varied and they need to be taken care in the best possible way. EDP is not just a training programme but it is a complete process to make the possible transformation of an individual into an entrepreneur. This programme also guides the individuals on how to start the business and effective ways to sustain it successfully.

Objectives of EDP

The objective of this programme is to motivate an individual to choose the entrepreneurship as a career and to prepare the person to exploit the market opportunities for own business successfully. These objectives can be set both in the short-term and long-term basis.

- Short-term objectives: These objectives can be achieved immediately.In the short-term, the individuals are trained to be an entrepreneur and made competent enough to scan existing market situation and environment. The person, who would be the future entrepreneur, should first set the goal as an entrepreneur. The information related to the existing rules and regulations is essential at this stage.
- Long-term objectives: The ultimate objective is that the trained individuals successfully establish their own business and they should be equipped with all the required skills to run their business smoothly.

The overall objectives of EDP are mainly to help in rapid industrialisation by supplying skilled entrepreneurs. At the same time, it also industrialises underdeveloped areas. The performance of small and medium scale industries are expected to improve by this and therefore providing a huge scope of employment generation in these sectors. This programme primarily aims at providing self-employment to the young generation.

An Entrepreneurship Development Programme primarily plays four roles to help an individual to become an entrepreneur. They are:

A. Stimulatory Role: It aims at influencing people in large number to be the entrepreneur. This includes:

1. developing managerial, technical, financial, and marketing skill
2. inculcating personality traits
3. promotes and reforms entrepreneurial behaviour and values

4. identifying potential entrepreneur applying scientific methods
5. motivational training and building proper attitude
6. strengthening the motive of a person and giving recognition
7. the valuable know-how of the local products and the processes help in selection of products, preparation of project reports

B. **Supportive Role**: It helps in the following ways:
1. registration of the business
2. procurement of fund
3. arrangement of land, power, water, shed etc.
4. support in purchase of right kind of machinery and equipment
5. supply of raw materials and common facilities
6. Providing tax relief, subsidy etc.
7. guidance in product marketing
8. support for management consultancy

C. **Sustaining Role**: It aims at providing an effective safeguard to businesses to sustain against the cut-throat market competition. This includes:
1. help in modernisation, expansion, and diversification
2. additional financing for further development
3. deferring interest payment
4. creating new marketing processes
5. helping access to improved services and facility centres

D. **Socio-economic Role**: It aims at upgrading the socio-economic status of the public and includes:
1. identifying entrepreneurial qualities in practicality
2. creating employment opportunities in micro, small, and medium industries on an immediate basis
3. arresting concentration of industries by supporting regional development in a balanced manner
4. focusing on the equal distribution of income and wealth of the nation
5. channelizing the latent resources for building an enterprise

The Govt. of India has established specialised institutions to boost up the rate of entrepreneurial development in India like NIESBUD in Noida, MSME-DI for small scale industries, NIMSME in Yousufguda, Hyderabad, EDI, NSTEDB, IED and CED in different states.

Role and relevance of entrepreneurial development programme

Role and relevance of Entrepreneurial Development Programme (EDP) in the process of economic development and growth of a nation is immense. Various EDPs are designed to develop and improve entrepreneurial skills and behavioural adjustment needed to go through the stresses of initial stages. Different programmes are designed for different trades, industries and big projects.

Basically the EDPs are meant to train and develop new entrepreneurs who act as catalytic agents in the process of industrialization and economic growth. It is the entrepreneur who organises and puts to use capital, labour and technology in the best possible manner for the setting up of his enterprise. The entrepreneur with his vision and ability to bear risk can transform the economic scene of the country. They play a vital role in initiating and sustaining the process of economic development of a nation. It is the EDP through which the entrepreneurs learn the required knowledge and skill for running the enterprise successfully which ultimately contribute towards economic progress in the following ways:

1. Creates employment opportunities:

The basis problems of most of the developing countries like India are poverty and unemployment. Entrepreneurship development programmes can help the unemployed people to opt for self-employment and entrepreneurial as a career. EDPs help solving the problem of unemployment by creating adequate employment opportunities in setting up of their own small and big industrial unit where the unemployed are absorbed.

In this way EDPs help the entrepreneur to get an opportunity to lead on independent and respectable life in the society and at the same time enable others to get gainful employment. Various programmes, schemes like PMRY (Prime Minister's Rozgar Yojana), NREP (National Rural Employment Programme) and IRDP (Integrated Rural Development Programme) etc. have been initiated by Government of India to eliminate poverty and solve the problem of unemployment.

2. Helps in achieving Balanced Regional Development:

Successful EDPs assist in accelerating the pace of industrialisation in the backward areas and helps in reducing the concentration of economic power in the hands of a individual. Government encourages to set up industries in the backward areas to remove wide gap of income and wealth between the rich and poor. The various concessions subsidies offered by the State and Central Governments prompted the entrepreneurs to up their own small and medium industrial units in the rural and backward areas. EDPs in setting up more and more industrial units in the backward areas lead to the develop of rural sector which helps in achieving balanced regional development.

3. Prevents Industrial Slums:

The towns and cities are highly congested and overcrowding due to the growth of industrial slums which results in overburdening of civic amenities and a lot of problems including adverse impact on the health of the people. EDPs help in solving the above problems by preventing the growth of industrial slums through dispersal of industrial units in different parts of the country including backward and rural areas. EDPs help entrepreneurs to know about the various schemes, incentives, subsides and infrastructural requirements for setting their enterprises, particularly in backward and rural areas. This checks migration of rural people to urban sector and thus controls the growth of industrial slums.

4. Use of Local Resources:

Plenty of locally available resources remain unutilized due to absence of initiative and lack of adequate knowledge by the entrepreneurs. Proper use of these resources will help to starve out a healthy base for rapid industrialisation and sound economic growth. EDPs can help in the proper use of locally available resources by providing proper training, guidance and education to the potential entrepreneurs.

5. Easing social tension:

EDPs help in channelizing on right lines the talent and energies of unemployed youth »1io feel frustrated after completing their education without a job or source of livelihood. Unemployment and frustration amongst the young and educated people lead to social unrest Lid tension. EDPs help in diverting the talent of the youth towards self-employment careers by establishing their own enterprises and thus creating employment opportunities for the unemployed. In this way EDPs are able to defuse the social tension and unrest among the youth.

6. Economic Independence:

The entrepreneurs through EDPs are able to achieve economic independence of a country by producing a wide variety of better quality goods and services at competitive prices. They also through export promotion and import substitution able to earn and save urge amount of foreign exchange which is essential for the growth and development of any economy.

7. Capital formation:

The various development banks like ICICI, IDBI, IFCI, SFC, SIDC and SIDBI take initiative in promoting entrepreneurship through assistance to various agencies involved in EDP and by providing financial help to ne entrepreneurs. It is impossible to start a new enterprise without sufficient funds. Entrepreneurs are the organizers of factors of production who employ their own and borrowed money for setting up of new ventures. All this results in the process of capital formation.

8. Improves the standard of living and per-capita income:

EDPs provide the necessary support to entrepreneurs by educating them about the test innovation and techniques of production to produce a large variety of quality goods id services at competitive prices. EDPs also help in establishing more enterprises which ad to provide more employment opportunities and help in increasing the earning of the people. It will result in increase in per-capita income and thus helps in the improvement of standard of living of the people.

9. Helps in the overall development of the nation:

Entrepreneur acts as a catalyst which helps in enhancing the various activities involved a business enterprise. In recent years EDP package, have become a vital strategy for harnessing the vast untapped human skills, and put them into industrial development. It results in the emergence of entrepreneurial opportunities in various fields which leads to all-around development in a country.

10. Helps in searching and exploiting opportunities

There are many opportunities for entrepreneurs in various fields like-Electronics, medicine, engineering, agriculture, food technology and packing, communication etc. EDPs help in searching such opportunities and provide necessary information, guidance and assistance in the search and exploiting these opportunities.

11. Enhancing managerial abilities

Entrepreneur development programmes help the entrepreneurs to enhance their organizing and managerial abilities so that they can run their enterprise efficiently and successfully. This is done through organizing educational management training and orientation programmes. Various specialized agencies like National Institute for Entrepreneurship and small Business Development(NIESBUD),New Delhi and Entrepreneurship Development Institute of India(EDII), Ahmedabad are engaged in entrepreneurship programmes.

Achievements of Entrepreneurship Development Programmes

The speed at which industrialization has taken place in recent years is due to the major role played by EDP's. Following are the major achievements of EDP's:

- EDP's played an important role in establishment, development and expansion of the practice-oriented development programme In India almost all the training programmes conducted are organized and developed under EDP's.
- EDP's have also developed and established various support systems necessary for the entrepreneurs. They strengthen and coordinate these support systems.
- EDP's have not only created a background for industrialization but have also

given momentum to it.

- These programmes have also contributed a lot to solve the problem of unemployment. EDP’s have helped to a great extent in this direction by starting self employment programmes and giving momentum to the speed of industrialization.
- Another achievement of these programmes is establishment and development of new enterprise which is a very difficult task in this competitive era. EDP’s have provided various inputs to establish new enterprises and also provided various entrepreneurial skills and qualities.
- Entrepreneurial education and training has spread because of entrepreneurial development programmes. This has resulted in increase in the knowledge, imaginative power, farsightedness, risk taking ability of the entrepreneurs etc.
- EDP’s have also contributed in project formulation. Choosing a right type of project is a difficult task as resources are limited. EDP’s have proved very useful in such situations.
- EDP’s have helped in balanced regional development by encouraging people to establish small industries in villages and backward areas.
- Another important achievement of EDP’s is availability of cheap and quality product to the consumer. Due to EDP’s new ventures have been established which have new technology and expertise which results in increase in competition.
- Many entrepreneurship development institutions have been established because of the EDP’s in India. The major among them are Management Development Institute, National Institute of Entrepreneur and Small Business Development (NIESBUD), Entrepreneurial Development Institute of India (EDII), Technical consultancy organization (TCO) etc.

Role of government in Organizing EDP’s Critical Evaluation

Government plays a very important role in developing entrepreneurship. Government develop industries in rural and backward areas by giving various facilities with the objective of balances regional development. The government set programmes to help entrepreneurs in the field of technique, finance, market and entrepreneurial development so that they help to accelerate and adopt the changes in industrial development. Various institutions were set up by the central and state governments in order to fulfill this objective.

Institutions set up by Central Government

1. Small industries development organization (SIDO)

SIDO was established in October 1973 now under Ministry of Trade, Industry and Marketing. SIDO is an apex body at Central level for formulating policy for the development of Small Scale Industries in the country, headed by the Additional Secretary & Development Commissioner (Small Scale Industries)under Ministry of Small Scale Industries Govt. of India. SIDO is playing a very constructive role for strengthening this vital sector, which has proved to be one of the strong pillars of the economy of the country. SIDO also provides extended support through Comprehensive plan for promotion of rural entrepreneurship.

2. Management development Institute(MDI)

MDI is located at Gurgaon (Haryana).It was established in 1973 and is sponsored by Industrial Finance Corporation Of India, with objectives of improving managerial effectiveness in the industry. It conducts management development programs in various fields. It also includes the programmes for the officers of IAS,IES, BHEL, ONGC and many other leading PSU’s.

3. Entrepreneurship development institute of India (EDI)

Entrepreneurship Development Institute of India (EDI), an autonomous and not-for-profit institute, set up in 1983, is sponsored by apex financial institutions – the IDBI Bank Ltd., IFCI Ltd., ICICI Bank Ltd. and the State Bank of India (SBI). EDI has helped set up twelve state-level exclusive entrepreneurship development centres and institutes. One of the satisfying achievements, however, was taking entrepreneurship to a large number of schools, colleges, science and technology institutions and management schools in several states by including entrepreneurship inputs in their curricula. In the international arena, efforts to develop entrepreneurship by way of sharing resources and organizing training programmes, have helped EDI earn accolades and support from the World Bank, Commonwealth Secretariat, UNIDO, ILO, British Council, Ford Foundation, European Union, ASEAN Secretariat and several other renowned agencies. EDI has also set up Entrepreneurship Development Centre at Cambodia, Lao PDR, Myanmar and Vietnam and is in the process of setting up such centres at Uzbekistan and five African countries.

4. All India Small Scale Industries Board(AISSIB)

The Small Scale Industries Board (SSI Board) is the apex advisory body constituted to render advise to the Government on all issues pertaining to the small scale sector.It determines the policies and programmes for the development of small industries with a Central Government Minister as its president and the representatives of various organization i.e. Central Government, State Government, National Small Industries Corporations, State Financial Corporation,Reserve Bank of India, State Bank of India, Indian Small Industries Board, Non government members such as Public Service Commission, Trade and Industries Members.

5. National Institution of Entrepreneurship and Small Business Development(NIESBUD),New Delhi

It was established in 1983 by the Government of India.It is an apex body to supervise the activities of various agencies in the entrepreneurial development programmes.It is a society under Government of India Society Act of 1860.The major activities of institute are:

i) To make effective strategies and methods

ii) To standardize model syllabus for training

iii) To develop training aids, tools and manuals

iv) To conduct workshops, seminars and conferences.

v) To evaluate the benefits of EDPs and promote the process of Entrepreneurial Development.

vi) To help support government and other agencies in executing entrepreneur development programmes.

vii) To undertake research and development in the field of EDPs.

6. National Institute of Small Industries Extension Training

It was established in 1960 with its headquarters at Hyderabad. The main objectives of national Institute of Small Industries Extension Training are:

i) Directing and Coordinating syllabi for training of small entrepreneurs.

ii) Advising managerial and technical aspects.

iii) Organizing seminars for small entrepreneurs and managers.

iv) Providing services regarding research and documentation.

7. National Small Industries Corporation Ltd. (NSIC)

The NSIC was established in 1995 by the Central Government with the objective of assisting the small industries in the Government purchase programmes. The corporation provides a vast- market for the products of small industries through its marketing network. It also assists the small units in exporting their products in foreign countries.

8. Risk Capital and Technology Finance Corporation Ltd.(RCTFC)

RCTFC was established in 1988 with an authorized capital of 15 crores rupees. The main objectives of RCTFC are provision of risk capital for the extension and expansion of entrepreneurial development and venture capital for the projects with high techniques for technology development and transfer.

9. Natioanl Research and development corporation (NRDC)

NRDC was established in 1953 under Department of Science and Industrial Research under Government of India. Its main objectives are:

i) Providing assistance in technology transfer

ii) Transfer of technology

iii) Establishing relations with various technology institutions and collecting various indigenous techniques developed by them.

10. Indian Investment Centre

This is an autonomous organization established by Central Government.Its main objective is to assist in promoting foreign cooperation with Indian entrepreneurs and providing necessary information to foreign entrepreneurs.

11. Khadi and village industries Commission(KVIC)

Khadi and Village Industries Commission established by an Act of Parliament in 1956.It is a service organization engaged in promotion and development of Khadi and Village Industries in rural areas. Its main objectives are:

i) Providing employment in rural areas.

ii) Improvement of skills

iii) Rural Industrialisation

iv) Transfer of Technology

v) Building strong rural community base and self reliance among rural people.

12. Indian Institute of Entrepreneurship (IIE)

It was established by the Department of Small Scale Industries and Agro and Rural Industries in 1953.It is autonomous organization with its headquarters at Guwahati. Its main objective is to undertake research, training and consultancy activities in the field of small industry and entrepreneurship.

13. Miscellaneous Organisation

In addition to above various organizations at all India level are assisting and are engaged in entrepreneur development. These include ICICI, IFCI, SIDBI, UTI, IDBI, IIBI etc.

14. National Alliance of Young Entrepreneurs(NAYE)

It has sponsored number of entrepreneurial development scheme in collaboration with various public sector banks. The main objective of the scheme is to encourage young entrepreneurs to explore investment and self –employment opportunities .It arranges for their training and assists them in procuring necessary finance.In 1975 NAYE also set up a Women's Wing to make women self-relaint and to raise their status.

15. Centre for Entrepreneurial Development(CED) Ahmedabad

It was sponsored by the Government of Gujrat and public financial institutions operating in the State.It conducts entrepreneurial development programmes at various centres.The important features of training programme are:

i) Training programmes were conducted after survey for opportunities was made.
ii) Appropriate linkage was established with supporting agencies supplying finance,factory sheds,raw materials, etc.
iii) Behavioural tests were conducted to select the entrepreneurs.
iv) Training programmes covered theoretical and practical aspects.
v) Full time project leader took follow up action after the training was over.

16. Institute for Entrepreneurial Development (IED)

It was set up by the IDBI in association with other financial institutions, public sector banks and the State Governments. The IEDs was set up to fulfil the entrepreneurial development needs of the industrially backward States in the country.

17. Technical Consultancy Organisation (TCOs)

A network of TCOs has been established by All India Financial Institutions and State Government throughout the country. These organizations have been set up to provide comprehensive package of services to entrepreneurs in general and to small business entrepreneurs in particular. Their main functions include the following:

i. Identifying potential industrial project.
ii. Preparing project reports,feasibility reports and pre-investment status.
iii. Identifying potential entrepreneurs.
iv. Providing technical and administrative support.
v. Conducting techno-economic studies of the projects.
vi. Conducting market research and surveys.
vii. Rendering advice to set up laboratories and design centre.

18. Public Sector Banks.

Public sector banks in association with NAYE have been conducting entrepreneurial development programmes. The main thrust of these banks has been to identify potential entrepreneurs in rural and backward areas. For example Punjab National Bank started entrepreneurial assistance programme in March 1977 in th States of West Bengal and Bihar. Similarly, Bank of India started entrepreneurial assistance programme since August 1972 in the States of Punjab, Rajasthan, Himachal Pradesh, J&K and the Union Territories of Chandigarh and Delhi.

The important Forms of entrepreneurial assistance are:

i) Identifying potential entrepreneurs
ii) Identifying viable projects.
iii) Assisting in preparation of project profiles
iv) Helping in project evaluation.
v) Arranging practical training.
vi) Financing the projects.

B) Institutions set up at State Level

There are a number of institutions establishes at state level for organizing, developing, developing, assisting and making successful entrepreneurial development programmes. Prominent among these are:

i) Small Industries Service Institute (SISI)
ii) State Financial Corporation (SFC)
iii) State Small Industries Corporation (SSIC)
iv) District Industries Centres(DIC)
v) Technical Consulting Organisation Ltd. (TCO)
vi) Industrial Directorates
vii) Commercial and Cooperative Banks
viii) State Industrial Development Corporation
ix) Industrial Estates
x) State Industries Corporation

The above mentioned State and Central level Institutions have provided a number of concessions and facilities to promote entrepreneur development in India.They have also played an important role in balanced industrial development in the country.

UNIT - 4

Introduction

An Entrepreneur plays a vital role in economic growth of a country. He collects and exploits the natural and human resources and then through innovation he utilizes these resources in an optimal manner. He provides or generates lot of employment amongst people and bring stability in economy.

Through establishing new industries and venture in far flung and backward areas, he plays a prominent role in export promotion and import substitution. An entrepreneur uses innovation and advanced technology in reducing cost of production and maintaining quantity of product as well as quality of product.

Thus, an entrepreneur does all those efforts which can pursue the pace of economic growth, employment creation, balancing regional development and maintaining economic stability.

The term economic growth implies growth in any economy. The rising way of trend per capita income and gross income in certain time period is called economic growth. Economic growth of a nation is never by accident. It is always a matter of design. It is brought about by persistent effort of the Govt. in general and of entrepreneur in particular. It is important because the society has not been able to sustain the well-being of its people without continuous growth, so economic growth is a requisite for growth and prosperity.

Actually, economic growth is a means to an end, and the end is human development. It contributes in poverty reduction when it expands the employment productivity and wages of poor people.

In the process of entrepreneur growth of a country, the entrepreneur plays a motivator role. The process cannot proceed onwards without the active support of the entrepreneur.

Joseph A. Schumpeter says that, “the rate of economic progress of a nation depends upon its rate of innovation which in turn depends upon distribution of entrepreneurial talent in the population.”

There are different types of development in an economy i.e., human development infrastructure development, social development, industrial development and economic development. An entrepreneur plays their role as catalytic agent in the process of economic development. In recent time, the role of an entrepreneur has been appreciating day by day.

Role of an Entrepreneur in economic growth as an Innovator

The word ‘Innovator’ we mean such “Entrepreneur who continuous to make some new changes or creations in his business, like production of new commodity, new technologies of production, new machinery, and equipment, new raw material for searching of new resources of semi- finished commodities, new management system, new organizational setup new markets etc. Innovating entrepreneurs bring about Revolution or improve the methods of production by executing new inventions.

An innovating entrepreneur is a person who searches new products, new raw materials, new markets and adopts new changes and improvements in the new ventures.

The entrepreneur is a promoter and innovator both. He is the agent of economic growth & changes in society.

The role of the entrepreneur as innovator is highly important in simulating economic stability, industrial awakening and social innovations.

According to Joseph Schumpeter, “An entrepreneurship is a creative activity and an entrepreneur is an innovator who introduces something new in an economy.”

According to him, innovation may be in:

i. Introducing a new manufacturing process that has not been tested and commercially exploited.

ii. Introducing a new product with which consumers are not familiar or introducing a new quality in an existing range of products.

iii. Opening a new market where company products were not sold earlier.

iv. Locating a new source of raw material or semi-finished products.

v. Developing a new combination of means of productions. Thus, it is clear that an entrepreneur is essentially an innovator.

A brief description of the role of the entrepreneur as an innovator is as follows:

1. To Create Novelty in Society -

The basic function of the entrepreneur is to create something new. He develops new products, brings out product diversifications and carries out of business technical innovations by Research and studies. As a result, Industrial Development takes place.

2. Production of Commodities and Services -

Since the entrepreneur is an innovator also, he is not only carrying out new inventions in his business activities but also makes the production of the products and services according to the needs of society. He perceives changes in economic and social life and takes initiations required in the changed atmosphere, by perceiving various economic, social circumstances. As a result, the wheel of economic progress goes on moving consistently.

3. To Use the National Resources for Productive Activities -

As an innovator, the entrepreneur has an important contribution in the economic progress of the nation by the establishment of new industries and generation of employment and use of national resources for productive activities to satisfy social and economic needs of the country.

4. Establishment of Successful Units -

The innovating entrepreneurs symbolize and creative awakening. They believe to go ahead on the new path, rather than move on the absolute path. Hence, they provide vitality to their business units. As a result, they run their business in a successful manner.

5. Organizing and Coordinating the Resources of Production -

As an innovator, the entrepreneur organizes and coordinates the resources of production, to maximize output, at the minimum cost. Entrepreneurs also contribute to increasing National Productivity, by their managerial capabilities and efficient utilization of unutilized resources.

6. Base of Industrial Development -

The innovating entrepreneurs have the readership quality to develop the resources of the enterprise, human capabilities, and generation of new ideas. New ideas emerge due to creativity but due to lack of leadership abilities, these do not become the base of industrial progress. The entrepreneur can build up the enterprising organization only by leadership, administrative capacities, and creativities.

7. Expansion of Organisations -

The entrepreneurs Incur substantial expenditure on research and studies to encourage innovations. As a result**,** scientific and business ideas are encouraged among people and their technical know-how is upgraded. Innovations emerge as a result of such research activities and creative ideas. Adoption of new techniques of production, in place of obsolete techniques, also become easier and production of new products and diversification is introduced to expand the small organization.

8. Accomplishment of Business Activities -

In a small business, the liability, innovations, and risks of a single person. But large scale business at National and International levels total risks beared by a group of persons, not by any individual. Hence, business activities are accomplished by the group of persons, by Organising in the form of establishment of companies, partnership firms are co-operative societies etc.

9. Consumption of New Products and Services to Society -

The entrepreneur is the creator and the innovator, so he introduces the new products, new ideas, new markets and new production techniques to the society and living standard is raised, but also execute the research and development activities, for that. As the outcome of all these, society gets the opportunity to consume a series of new commodities and services and consequently, the standards of living of the society rise substantially.

10. Economic Prosperity of the Nation -

Innovative entrepreneurs start new enterprises to go ahead by removing the hurdles and disturbances arising in their ventures. Besides, they also accept the challenges and as well as improve their own performance by introducing the innovations. They also contribute to the overall prosperity of the nation. The innovator entrepreneur has significant importance in the industrial progress of the nation.

11. To Make the Economic System Highly Dynamic -

The innovator entrepreneurs make the economic system of the country highly dynamic since they use new raw materials, new techniques, and machinery in production. They provide new products and services, adopt new internal and external Strategies and also used new distribution policies. So, the economic system becomes dynamic.

12. Existence of Business -

In the modern business world, innovator entrepreneurs are making new experiment and improvements in production techniques, machinery, equipment, Technology, finance, and Technical inputs. As a result**,** not only various complexities have emerged in the business, but it has also become essential that the firm continues to maintain the capacity to compete. The existence of the modern business is impossible without attaining entrepreneurial abilities, in this age of fast changes and innovations.

13. Dynamic Leadership to the Business -

The good entrepreneur posses two main qualities. The capacity to bear risks and to sponsor new units. But, in the modern age, the innovator entrepreneurs link the business with society and the environment. Hence, they establish new industries within their business, search the new opportunities and take decisions in the context of social values. So, business gets the dynamic leadership of entrepreneurs.

14. Catalyst Elements -

Wealth in the society is generated by the entrepreneurs and poverty gets reduced. Besides, the optimum utilization of resources and development of the self-sufficient society also become possible.

15. Social Responsibility and Satisfaction -

The entrepreneur as an innovator may perform social obligations and may provide satisfaction to the society by creating new values, activities, and utilities also.

KINDS OF ENTREPRENEURS AS INNOVATORS

The innovators are as following types:

1. Initiator Innovators

Initiator innovators are those entrepreneurs who themselves do not perceive the innovations, but he enters in the process of expansion of new innovations and participates in the diffusion process of development of the use of the innovations.

2. Prime Mover Innovators

Prime mover innovators are those entrepreneurs who create something new with some differences, like the production of new products, new methods of production, and new machinery and implements, new raw materials and search of the new market, etc. Such entrepreneurs engaged constantly to search for new improvements in their business. They are creators of new values.

3. Minor Innovators

Such entrepreneurs who slightly act as innovators do not take innovations at a large scale but ensure the best use of the resources of the society to uplift the society.

4. Satellite Innovators

Satellite innovators are such entrepreneurs who act as the supplier or the intermediary, but gradually start the business or the subsidiary industries independently.

5. Local Trading Innovators

The local trading innovator is the person who keeps his business activities **(**Trade, commerce, industries, and direct Services**)** Limited to a particular area. He has no courage to move to another place.

Role of an Entrepreneur in generation of Employment Opportunities Unemployment is a global phenomenon and has emerged as a burning problem of the day. Unemployment is a common problem whether it is backward economy, developing economy or even in developed economy.

This problem of unemployment is becoming serious day by day. An entrepreneur generates employment opportunities both directly and indirectly. Economic growth does not always lead to employment. It must be created in the field like agricultural sector, industrial sector, small scale industries, education and health, information technology.

Employment can be generated in organised sectors and unorganised sectors and their role in employment generation are as follows:

1. Establishment of New Business and Industries:

Somebody said truly that “Business is a game of skill which cannot play everybody.” For gene- rating employment, entrepreneur sets up small and large size of industries and business and provides employment to millions of people. Thus entrepreneurship is the best way to fight the evil of unemployment and generate employment opportunities in the country.

2. Increment in National Income:

National Income refers to produced product and services in a country in a specific year. The manufactured products and services are consumed in domestic level and exported to other countries. By introduction of innovation, product quantity and variety is improved and as the increase in population, demand is also increased, so as to meet out the demand of product. Production also increases and generates more employment amongst people.

3. Balanced Regional Development:

When the industrial developments are limited to few areas, in this situation, the only concerned area is developed condition. Through innovation, entrepreneurship develops both public and private sector and reduced economic disparities of nation. They get benefit and incentives which are given by government, when an entrepreneur starts industries in backward areas.

4. Diffusion of Economic Strength:

The whole world has been controlled by economic powers. We can divide the strength in two parts:

a. Physical Strength

b. Economic strength.

The main resource of economic strength is industrial and commercial activities which makes economies strong on development basis. But the rising trends of entrepreneurs helps in decentralising power and remove monopoly tendency amongst rich countries. Entrepreneurs establish new units in different areas of world and generate employment in unemployed mass.

5. Generating Employment:

For making the economic growth, entrepreneur establishes different types of industries and business and generates employment to millions of people.

6. Improvement in Living Standard:

By establishing new type of industries and using innovation, an entrepreneur produces necessary products & services and removes their deficiency from market. They produce branded and sound quality products at cheaper cost and make easy approach to customer and assist in increasing the living standard of people.

7. Economic Freedom:

An entrepreneur does all the efforts in creating the environment of economic freedom. For this purpose, entrepreneur encourages to produce more sound products/services within country facing the competition at international level.

He emphasises on production at minimum cost and standard full product, he adopts product diversification technique and through more production, fulfills internal demand and meet also external demand. By selling the products in foreign countries he earns foreign currency and assists in maintaining economic freedom in country.

8. Creativity and Innovation:

Creativity and Innovation are abilities of bringing renovation. Through innovation, an entrepreneur makes something new and creativity is the prime stage of innovation. Creativity is valueless when it is not to be converted into product and services.

9. Assistance in Development of Infrastructure:

Infrastructure plays an important role in economic development. Infrastructure includes insurance, banking, industry and transpiration facilities, energy.

10. Establishing New Industries and Business Units:

An entrepreneur sets up new type of business and industrial units and assists in transferring the production factor in productive function. Without active participation of entrepreneur, all factors are just like rock.

11. Innovation Promotion:

For innovation an entrepreneur emphasize on research & development and encourage innovation. By innovation, he makes new things, introduce new production techniques, plant, raw material, new technology, search new market etc.

Role of Entrepreneur in Supplementing And Complementing Economic Growth In recent decades, the role of an entrepreneur has been to supplement and accelerate the pace of growth and economic development in both the developed and developing countries When an entrepreneur sets up an industrial or service unit it helps in economic growth. Similarly, when economy grows it creates opportunities for further growth. Thus, every economic growth has a multiplier affect; one complements the other and one supplements the other. When an entrepreneur establishes a bank it complements other economic activities as it helps further growth. When any engineering and electronic unit is set up it requires components from large number of manufacturers. In most engineering, electronic and electrical industries like T. V. , refrigerators, computer growth of one large unit gives birth to a number of ancillary units. This is true not only for engineering and electronic industry but also for steel, textiles, chemicals, food processing and so on. Along with complementary development there is also supplementary development. When a spinning mill is set up it leads to development of thread units and cloth weaving units. When a computer hardware industry is developed it leads to the growth of software industry. The development of software industry led to its exports from India in a big way. Thus, one leads to growth of another activity.

The role of entrepreneurs not only complements but also supplements the economic growth of the country in the following manner:

1) Generation of employment. Entrepreneurs become self-employed and self-sufficient. They do not depend on the government jobs or private jobs and directly employ themselves by starting their own enterprises. In fact, they also privet jobs to many unemployed by setting up large and small scale industrial. Thus, entrepreneurs play an important role to reduce the unemployment problem in the country and pave the way for economic development.
2) Capital formation. Entrepreneur’s efforts to mobilize the capital results in motivating the investors to divert their ideal savings in the industrial enterprises. Investment of public saving in industrial sector helps the country to use financial resources for productive purposes. The growth rate of capital formation will be increased which is highly essential for rapid economic development of a country. It is in the sense that entrepreneurs grenade capital at a rapid rate and capital formation increases which is vital for the industrial development.
3) Increasing per capita income.
4) Improvement in physical quality of life.
5) Improvement in standard of living.
6) Growth of infrastructural facilities.
7) Initiating change in the economy.
8) Forward and backward linkages. It is the entrepreneur who initiatives change and this to maximize his profits by innovations. Setting up of an enterprise in accordance with the changing technology has several backward and forward linkages. For example, the establishment of a textile unit generates several ancillary units and expands demand for cotton, chemicals, dyes, etc.
9) Development of backward areas.
10) Economic Independence.

Role of Entrepreneur in bringing about Social Stability

Being an entrepreneur social, human being ultimately the aim is the development of a happy and prosperous society. He is also a part of this society. He gets inspiration from society and develops in society. So, he has to play a contractor role in the economic development of society. Two types of people live in society. The first category is of such persons who carry out positive and constructive activities and the second category is of destructive persons. The first category people do something distinctly visible. They aspire not only for their own happiness but also wish to see happy others and prosperous. The second type of people carries out destructive activities in society. They create a disturbance, instigate people against each other and become Furious on one pretext or the other, causing bad effects for society. The entrepreneur always desires the maintenance of social stability with good results.

For that, an entrepreneur fulfills the following roles:

1. Establishing Self Sufficient Society

The self-sufficient society may be established by the productivity revolution in areas of production in the country. For that, the entrepreneur increases the production in the business Enterprises, fulfill the requirements of the local community, encourage Savings and capital formation, contribute towards export promotion and import substitution, etc. So, the dream of the establishment of a self-sufficient society gets materialized.

2. Establishing Ethical Values of the Society

The entrepreneur establishes the ethical values for the society to ensure social stability. For that, he stresses maintaining moral values, ideals, and Standards in the conduct of persons associated with various business activities. The entrepreneur is a part of the whole value system of society.

3. Contribution to Social Development

Entrepreneurs are developing in the Society and Society is developed by entrepreneurs. **So**, he not only works for the development of the local society but a society of the whole world. He makes the best possible utilization of physical and human resources, with the utmost economy, providing employment to local people and also fulfilling his social responsibilities towards various groups of society.

4. Changes in Social Framework

The entrepreneurs bring out changes in the social Framework by innovative activities. They lead society towards progress by the introduction of new products, new markets, new techniques, new sources, and the establishment of new industries.

5. End of Evils

The empty mind is the devil's workshop. A Starving person can do any bad work**,** like**,** theft, dacoity, loot, murder, abduction **etc.** By the establishment of new industries and expansion of the existing industries and making the production of new products, the entrepreneurs may provide employment to such persons and may divert their attention towards creativity. It will raise the standard of living of such people, which will be helpful in removing several social evils. Employment is a path to the creation of moral values in society.

6. Less Economic Problems

Society still prevails many social evils existing in the big cities, like – class conflicts, polluted environment, slum areas, and social crimes **etc.** These may be reduced by the establishment of various business undertakings by the entrepreneurs. Besides, social evils like dowry and intoxication in the villages may also be curbed by the establishment of Enterprises and development of entrepreneurship tendencies in the villages and the attention of people can be diverted towards savings and capital formation, etc.

7. Increase in Employment Opportunities

The entrepreneurs increase the opportunities for employment. They help in increasing the employment opportunities through the establishment of new Enterprises and expanding the existing establishments.

8. Removal of Poverty

The entrepreneurs provide maximum opportunities for employment to the unemployed persons, both directly and indirectly through the development of new products and expansion of new Enterprises and the markets. As an effect of all these, poverty gets reduced in the country. The entrepreneurs enlarge the path of economic progress, through which the country gets rid of the vicious circle of poverty.

9. High Standards of Living

The Entrepreneurs have given of materialism in society through new techniques, new products, and inventions. As a result, the living standards of the people can be upgraded in society. It has contributed to a better quality of life.

10. Social Changes

Creative changes are being accepted in society always. The entrepreneur is a creative agent of Social Change. The traditional superstitions and misbeliefs come to end and social stability is established.

Thus, the entrepreneur always desires the maintenance of social stability with good result. So, the different Role of Entrepreneurs in Bringing Social Stability is important.

Role of Entrepreneur in Balanced Regional Development of Industries

An entrepreneur is a person who perceives for a new product or service and also finds out financial sources for establishing the business for production of the product and service. The entrepreneurs know, how to avail the opportunities, and to establish any viable industry in any viable area. So, Entrepreneurs in Balanced Regional Development of Industries, play a very big role.

The role of entrepreneurs in the balanced development of the industries may be explained as follows:

1. Knowledge of Market Conditions

An entrepreneur has full knowledge about the markets, like – where is the good market for a particular product, where particular product and services are to be produced, what will be the cost of production for a product at that place, to what extent the labour and capital will be available in the area, what is the likely demand for the commodity, what should be the price of the commodity, etc. Extend and type of competition and the measures to win the competition, etc. Entrepreneurs establish industries in those Areas, where most of the factors are favorable to him. As a result, the balanced development of industries becomes possible.

2. Advantages of Government Policies and Facilities

The government also committed for balanced regional development of industries. To achieve the goal, various types of policies have been formulated. Governments have also provided various types of facilities allotment of land at concessional rates, provision of basic infrastructural facilities at the allotted place, easy availability of various resources, finance facilities at reasonable rates of interest, exemptions from taxes, the supply of modern techniques and machinery on installment, good facilities for marketing, etc. The entrepreneur may come forward to avail these facilities for the establishment of new industrial units and expansion of the existing units. So, the balanced development of the industries becomes possible.

3. Utilization of Different Resources

The nature has bestowed all countries and areas with one or the other resources, free of cost, of course, in varying degrees. Besides, economic and physical resources are also available in all areas. The entrepreneurs use various resources in the production of various commodities and services, since he possess entrepreneurial qualities. As a result, balanced regional development of industries takes place in the country.

4. Constructive Changes in Social Structure

Several constructive changes have occurred in the social structure, due to the role of the entrepreneur. The society has become industry oriented, misbeliefs have reduced, several obsolete traditions have come to an end. As a result, the entrepreneurs do not hesitate to bear risks and establishing industries in far flung areas.

5. Activeness in All Areas

The efforts of the entrepreneurs cause spread of activeness in all areas of life. They provide opportunities for leading free life to people, as well as to make the society self sufficient.

6. Evolution of Multiform

Nature has several diversities, but uniformity in its various elements may also be observed. The entrepreneurs assess these diversities and use of them for the prosperity of human being, various capabilities and qualities, like**,** intelligence, sharp memory, foresightedness, dedication, courage, knowledge of various new techniques, awareness towards the opportunities, knowledge of market conditions**,** etc. As a result, uniform development of industries becomes possible and regional imbalances also can be reduced.

7. Establishing Self Sufficient Society

The entrepreneurs have an important role in the establishment of a self sufficient society, the reason being that they fulfill the requirements of the society and also increase the Exports.

8. Help in Removing Regional Disparities

The entrepreneurs have an important role in removing the geographical disparties in the economy. Entrepreneur may available various facilities to etablish industries in such areas, like, no industry districts. Besides, the government also attract private entrepreneurs for establishing industries in backward areas. **For that**, land and capital provided to them at concessional rates. Exemption in taxes and various types of subsidies are also provided for the establishment of industries in the backward areas. All these efforts are helpful in the development of backward areas.

Thus, in balance regional development of industries, entrepreneurs are playing a very important role.

Role of Entrepreneur in Export Promotion

An entrepreneur plays an important role in export promotion and import substitution.

Export Promotion refers to that effort which is done by an entrepreneur for removing imbalance by increasing export and decreasing import. It may be defined as the govt. policy designed to encourage the exporters to export more goods from the country than previous or it refers to policies and measures which can result into maximum increase in the exports of a country.

Objectives of Export Promotion:

1. Correction of unfavourable balance of trade
2. Reduction of foreign loans
3. Achievement of self-reliance
4. Exporting new products
5. Defraying the cost of defence imports.
6. Ensuring successful planning.

Export promotion reduces unfavourable balance of trade, decrease imports and increase exports. It also increases valuable foreign currency reserves. There are various facilities, incentives, and subsidies which are provided by central govt. and state govt. in the field of export promotion. The Government offers the benefits of incentives, concession and subsides.

Role of an entrepreneur in export promotion are as follows:

1. Removing the Trade Imbalance:

The entrepreneurs play an important role in case of removing the trade imbalances. More production is the right way of export promotion. If an entrepreneur wants to promote the export, he can do with the more production, standardisation, brand, low production cost.

"More production with low production cost with higher standard quality." By this way, an entrepreneur helps in removing the trade imbalance. Under trade balance only goods are included, services are not the part of trade. But in increasing production, entrepreneur can sell surplus production to other nation and adjust the due amount.

2. Reduction in Import:

An entrepreneur plays an important role in reduction of import. He imported raw material, manpower, machinery, tools, equipment, expertise and fished goods from other nations at high cost. In this situation entrepreneur should exploit natural resources by using domestic manpower and reduced cost of production. It would be reduced import in future.

3. Economic Development:

Economic independence is the symbol of economic development. Entrepreneur can produce more output and meet out the internal and external demand, and earn foreign currency. To fulfill the respective purpose both private and public sector should enhance all infrastructure facilities (energy, industry, transportation, communication and Banking) which is helpful in achieving the targets.

4. Increment in Foreign Currency Fund:

An entrepreneur plays an important role in increasing foreign currency fund. We get foreign currency from the export promotion. If govt. is promoting the export policy, in this situation, entrepreneur collect the foreign currency fund by producing more and sound products and services.

5. Introduction to Innovation:

An entrepreneur should adopt innovation by introducing new combination of goods. By adopting innovation entrepreneurs promotes new product, goods and product exchange and diversification of product in venture.

6. Advance Technology:

An entrepreneur should adopt advance technology for standardization of product with the less cost of production. By this way, entrepreneur gets improved advance technology, by adopting advanced plant, machinery, equipment etc.

7. Appreciation in Production and Productivity Level:

An entrepreneur can play a vital role in appreciating production and productivity level. To meet this purpose, entrepreneur establish project in Export Oriented Unit or Export Processing Zones or free Trade Zones (FTZ). Such units may be engaged in manufacturing, software development, horticulture, agriculture, aquaculture, animal husbandry etc.

EOU and EPZ are industrial estate where export oriented units are taken various incentive. If investment is done in 4 cases, govt. gives facility like less tax or no tax or rebate in tax 100% exemptions; and other facilities.

i. Export Oriented Units (EOU)
ii. Export Processing Zone (by Central Govt.)
iii. Special Economic Zone (SEZ)
iv. Trade Free Zone (TFZ)

Govt. provides the following facilities to above export oriented projects:

i. Single window system for paper formalities
ii. Raw material at cheaper price.
iii. Market and transportation facility
iv. Plant & Machinery
v. Credit facility
vi. Low rate of interest on loan

If there is an increase in production, employment and removing trade imbalances, govt.

launches policies like EOU, EPZ and SEZ, then export promotion can be done.

8. Low Production Cost:

If entrepreneur exploit natural and human resource efficiently, it will give their return in high production at low cost instead of import at high rate and high cost of production.

9. Enhancing Foreign Competition Capacity:

If entrepreneur use the internal resources for production with sound quality, he can sell surplus out to other country and make a challenge in front of foreign nation at international level by sound, cheaper, durable and standard products.

10. Increasing Export:

Entrepreneurs are required to play an important role in export promotion. Export promotion reduces unfavourable balance of trade (i.e., only goods are included and services which are ignored or all visible items are included). It also increases valuable foreign currency reserves.

For motivation and increasing export promotion, govt. provides specific facilities and incentive to an entrepreneur. Both Central Govt. and State Government are provided concerned facility and incentives in the field of export promotion. There should be increasing number of old and new entrepreneurs lacking benefits of incentives, concessions and subsides. In this way Govt. has launched few programmes such as EOU, EPZ, FTZ, SEZ.

EOU — Export Oriented Unit EPZ — Export Promotion Zone FTZ — Free Trade Zone

SEZ — Special Economic Zone

11. Introduction to Industrial Culture and Corporate Service:

An Export Processing Zone (EPZ), free Trade Zones (FTZ), Special Economic Zone (SEZ) established by Central and State Govt. are industrial estates where export oriented units take various facilities such as tax exemptions, duty drawback, no import duties, no quantitative restrictions.

There are some important facilities provided to units in FTZ or EPZ:

i. Suitably developed plant and buildings.
ii. Single point clearance of new projects within 45-60 days.
iii. No license needed for import of capital goods etc.
iv. Duty free import of capital goods and equipment.
v. Complete exemption from income tax.
vi. Assured power supply.
vii. Export finance at confessional rate of interest.
viii. Market facilities
ix. Single window system for documentation formalities.

Export processing zones have been established at the following places:

i. Kandla free Trade Zone
ii. Santa Cruz Electronics Export Processing Zone.
iii. Export Processing Zone at Chennai.
iv. Export Processing Zone at Cochin.
v. Export Processing Zone at Noida (U.P.)
vi. Export Processing Zone at Falta (W .B.)
vii. Export Processing Zone at Vishakhapatnam (Andhra Pradesh).

12. Rising trend of internal trade.

13. All benefits to customers such as reasonable and durable product, less price product and standard quality.

At last but not the least, we conclude that an entrepreneur plays a vital role in export promotion and import substitution by establishing developing and expanding industries which can produce such goods which is easily used as import substitution.

Role of Entrepreneur in Import Substitution

Entrepreneur is the most important factor in the economic development of the country. He plays a very important and catalytic role in activating the factors of production leading to the overall economic development. The entrepreneur organises and utilises the various factors and sets productive machinery in action. The availability of entrepreneurs, therefore, is the precondition of economic growth.

According to Prof. Schumpeter, the supply of entrepreneur depends on the rate of profit and social climate. It is profit that induces the prospective entrepreneur to get into the business and start new activities or expand the existing activities. Profit, therefore, is a factor which induces the entrepreneur to organise and utilise the factors of production for development.

Entrepreneur is an innovator with a certain achievement motive and that achievement motive may also mean something more than money. Social climate also plays its role in attracting prospective entrepreneur to innovate, assume risk and face the music of uncertainty.

According to Prof. Schumpeter, there is high degree of risk and uncertainty in economic world and in this context, entrepreneurial behaviour is important as development is a discontinuous process which itself proceeds with spurts.

Entrepreneurial behaviour has a role in ensuring the change required by the development process. Entrepreneur brings innovation or technical know-how to introduce new products and new combinations of production factors. Economic system has a reservoir of unused technical inventions which can be early utilised by the entrepreneurs. According to Prof. Schumpeter, "It is no part of his function to find or to create new possibilities. They are always present, abundantly accumulated by all sorts of people."

Entrepreneur also mobilises capital source to have a command over factors of production. Prof. Schumpeter rightly observed that entrepreneur needs credit because credit promotes industrial development which in turn delivers new goods. So, resource mobilisation efforts of entrepreneur also ensure the better good effective utilisation of resources available in the country which further celebrates the pace of economic development. The role of entrepreneurs in import substitution can be assessed in the following ways:

1. Saving of Foreign Exchange:

Entrepreneurs are also producing goods and services which can be used for those products which are being imported from foreign country. By producing substitute products and services, entrepreneurs try to save valuable foreign exchange. At a later stage, consumer becomes habitual of substitute products.

2. Creation of Employment Opportunities:

When entrepreneurs produce the goods and services in the country which can be used as a substitute of the imports, employment opportunities are generated in the country and utilisation of capital also becomes possible.

3. Increase in National Income:

Import substitution efforts also help to save foreign exchange which ultimately leads to increase in national income. Any increase in national income improves the well-being of the society. It also enables the country to optimize the use of available resources in the country.

4. Self-Reliance:

Import substitution reduces the dependence on imports from foreign country. Various entrepreneurial activities for increasing production and services not only reduce the dependence on imports from foreign countries, but also reduce the foreign exchange crisis. It also motivates other potential entrepreneurs to get involved in these activities.

5. Accelerating the Pace of Industrialization:

Import substitution efforts accelerate the pace of industrialization in the country. Entrepreneurs are generally encouraged by the incentives and subsidies to work for import substitution efforts. They invest more capital to enlarge the scale of production. In this way, they try to supply quality goods and services to the society and thereby restricting the imports and thus, saving the foreign exchange.

Suggestions to Improve Import Substitution:

Following suggestions are to be implemented to make the import substitution more effective:

1) Priority should be given to production of those goods which are not being produced in the country. For this purpose foreign collaboration should be encouraged in each and every desired segment.
2) Incentive for import substitution should be allowed on the lines of cash incentive scheme.
3) Concessional funding arrangement should be given to those production units which are engaged in production of goods under import substitution.
4) Import duty should be reduced with reference to goods under import substitution.
5) Exemption in custom and excise duties should be given in case of raw materials used for production of goods under import substitution.
6) Concessional tariff policy should be formulated for import of coal etc.
7) Necessary exemptions should be allowed in income tax, sales tax and additional depreciation for production of goods under import substitution.

Role of Entrepreneur in Forex Earnings

Forex earnings (i.e. foreign exchange earnings) has been playing a prominent role in growth and development of any economy. Forex earnings means arrival or introduction of foreign currency. For increasing the foreign earning the Govt. has launched LPG policy (Liberalization, Privatization and Globalization). Along with time to time industrial policy is also introduced and amended. To make the economy more competitive, increasing production, productivity and efficiency, an entrepreneur adopts ultra-modern technique and technologies.

The primary object of new industrial policy is to create confidence in the Indians and foreign industrialists.

Increasing space of global village ensures free movement of man, material and money from one country to another country. Saving of foreign exchange is also necessary to check the vicious circle in import-export. Improving entrepreneurial behaviour leads to higher level of production and increases the earning of foreign exchange.

In this context, role of entrepreneurs can be assessed in following ways:

1. *Production of Products and Services*:

Entrepreneurs produce the goods and services. They are using their surplus production for exports. Export efforts enable them to identify the further scope of exports of other products. Thus, exports create temptation among the entrepreneurs to produce a variety of products and services for earning more foreign exchange.

2. Minimize Foreign Dependence:

Imports are always costly in terms of foreign exchange as well as in terms of trade. Entrepreneurs have to play their role in this context. Entrepreneurs through their innovative behaviour can easily produce goods and services which can be treated as a substitute for imported items. By this process, they can minimize foreign dependence for the supply of goods and services in the country.

3. Production of Import Substitution Items:

The Government of India has completely banned the import of some commodities, whereas import of some other goods and services has been declared as restricted items. In such conditions, entrepreneurs may fulfil the need of earning foreign exchange by producing commodities included in list of import substitution.

4. Innovative Approach:

The entrepreneur is always ready to take the advantages of all favourable opportunities. He carries out production by suitably identifying the opportunities and also starts providing new range of services in the foreign market.

5. Increase in Exports:

Entrepreneurs search viable opportunities in diversified export items. In some cases, Government also provides incentives for the production of exportable items. The combined effect of these measures increases the level of export.

6. Industrial Progress:

Concept of global village has created an environment of competition and cost effectiveness. Entrepreneurs ensure a speedy industrialization and target the large scale production. In this way they can easily compete with foreign producers and get the foreign market under their control.

Sources of Forex Earnings:

The main sources of forex earning in India are as follows:

1. Rapid increase in our exports.
2. Heavy remittance of foreign currency by NRI for investment motive.
3. Entry of foreign entrepreneurs in large number in India with large foreign capital and latest technology.

4. Arrival to foreign capital in India (i.e. foreign direct investment)
5. Profit from industries which are established by Indian entrepreneurs in foreign country.
6. Indian employees who are involved in private and Govt. services in abroad.

Effect of Forex Earnings on Economy

1. Balance of Payment.
2. Reduction import.
3. Increasing export.
4. Introduction to foreign technology.
5. Advance technology based productivity.
6. Rising trend of production and productivity.
7. Low cost of production and control on price level.
8. Industrial Development.
9. Control on Monopolies Restrictive Trade Practices.
10. Increasing competitive Tendency.

INFORMATION SYSTEM MANAGEMENT (305)

Chapter 1. Information in the company

The concept of *information*

All individuals, companies and, in general, all organisations are continuously capturing data, many of which are of no significance to them at all. However, other data are available that would afford them a better understanding of their own environment and of themselves. These data – what we know as *information* – enable them to make more accurate decisions. For this reason, the right amount of information at the right time is a key factor for every organisation.

Company managers take decisions, prepare plans and control their company's activities using information that they can obtain either from formal sources or through informal channels such as face-to-face conversations, telephone calls, social contacts, etc. Managers are challenged by an increasingly complex and uncertain environment. In these circumstances, managers should theoretically be able to define and obtain the type of information they require. However, this is not what happens in practice; rather, the way managers perform their work depends on the available information that they have access to. Most decisions are therefore made in the absence of absolute knowledge, either because the information is not available or because access to it would be very costly.

Despite the difficulties in obtaining information, managers need relevant information on which to base their planning, control and decision-making functions.

Although the terms *data* and *information* are sometimes used indiscriminately, they do have different meanings. Data are non-random symbols that represent the values of attributes or events. Hence, data are facts, events and transactions stored according to an agreed code. Data are facts obtained through reading, observation, calculation, measurement, etc. The amounts and other details on an organisation's invoices, cheques or pay slips, etc, are referred to as *data*, for example. Data are obtained automatically, the result of a routine procedure such as invoicing or measurement processes.

Fig. 1.1. Transformation of data into information

Information is a set of data transformed in such a way that it helps to reduce future uncertainty and, therefore, contributes to the decision-making process. Information is data transformed in a way that makes sense to the person who receives it; in other words, it has a real or perceived value for that person when he or she acts or takes decisions. Information, moreover, is data that have been interpreted and understood by the recipient of the message. The relationship between data and information is similar to that of raw materials and the finished product.

Information will be meaningful insofar as it provides useful raw material for taking a specific decision.

Fig. 1.2. Decision making: transformation of information into action

The process of reflecting on and understanding information is what allows the message to have different meanings for different people. This process also implies that the data analysed, summarised or processed to produce messages will only become information if its recipient understands its meaning. For data to be transformed into information, there must be an awareness of what the person receiving the message will use it for, his or her training, position in the organisation and familiarity with the language and calculations used in the message.

While all managers need information, they do not all need the same type of information. The kind of information required will depend on a range of factors: their level in the hierarchy, the work they are carrying out, confidentiality, urgency, etc. Indeed, the usefulness of information is a debatable point, and what for one person is information, for another is data. In an organisation, for example, when information is transferred from one organisational level to another its meaning may change significantly, such that at one hierarchical level it is regarded as significant information, whereas at another level it is simply data (Menguzzato and Renau, 1991).

Information is the recipient's knowledge and comprehension of data. Information reduces uncertainty and affords the recipient something he or she did not know previously.

Information is one of many company resources, alongside capital, raw materials and labour, since no company is viable without information. Regarding information as a scarce resource obliges us to consider the issue of information economics, in other words, how to establish the necessary relationship between the value of information and its cost.

According to Menguzzato and Renau (1991), information costs can be estimated by taking the following into account:

– The information content required.
– How urgently the information is needed.
– The amount of information needed.
– How accessible the information is.

In contrast, information value is more difficult to determine. The concept of *expected value of perfect information* (evpi) can be used to estimate information value. This concept may be defined as the difference between the average expected result with perfect information and the average expected result with the available information. The cost and the value of the information must be compared in order to find out how to use this scarce resource, in what amount, and what benefits might be expected from using it.

Information is an essential factor for the company in that the possession or otherwise of opportune information will be a determining factor in the quality of the decisions it adopts, and as a result, of the strategy that it might design and put into practice at any given moment.

Well-prepared information can go a long way to avoid problems stemming from environmental uncertainty, either because of lack of clarity in certain aspects, or due to the huge amount of accumulated data when a decision has to be taken urgently.

Characteristics of information

Good information provides value. Experience shows that good information should present the following qualities:

Relevance

Relevance is a decisive quality. Relevant information is what increases knowledge and reduces uncertainty surrounding the problem under consideration. Reports and messages frequently contain irrelevant sections that lead to difficulties and cause frustration. Many erroneous managerial decisions are a result of data overload. The right information is not taken from an excessive accumulation of data, which tends to cause a general feeling of impotence vis-à-vis the problem, but rather it depends on getting hold of the relevant data. This characteristic is heavily influenced by the qualities explained below.

Accuracy

Information must be sufficiently accurate for managers' purposes. No information is totally accurate, and spending more on information in pursuit of greater accuracy does not always result in more valuable information.

The degree of accuracy should be coherent with the importance of the decision to be taken and will vary according to the decision-maker's level in the hierarchy. The degree of information accuracy required will depend on the hierarchical level in question.

Completeness

In an ideal world, all the information required to take a decision would be available; however in reality this is not possible. Information is considered to be completed if it informs us on the key points of the problem we are analysing.

Source trustworthiness

Trust in the information source increases when it has a proven track record. To increase the trustworthiness of the message, managers use reports from various sources, particularly where strategic decisions are concerned.

Communication with the right person

Each manager in the company is assigned a specific area of activity and responsibility and must receive information to undertake the tasks he or she is responsible for. However, this process does not always function as well as it should, and information may not reach the right level in the organisation. For instance, a superior might not provide all the information to the person who needs it, and vice versa; a subordinate may hold back information in an attempt to make him or herself indispensable. Information providers must be aware of information needs in order to ensure it goes straight to where it is required.

Punctuality

Good information is that which is delivered just when it is needed. To a certain extent, the need to obtain information quickly can jeopardise its accuracy, although today's data processing methods can produce accurate information very rapidly. Vital information for the company may become worthless if it takes too long to obtain, or delays occur in processing and communicating the information.

Although the punctuality of regularly produced information is important, how often information is produced should be related to the type of decision or activity it is required for. Often, companies routinely produce reports at fairly arbitrary intervals (daily, weekly or monthly) following traditions or calendar conventions without taking into account the time cycle of the activity involved.

Detail

Information should contain the minimum number of details for effective decision making. Every superfluous character or data entails extra storage efforts, more processing, more assimilation of difficulties and probably inferior decisions. The level of detail should vary with the level in the organisation: the higher the level in an organisation, the greater the degree of aggregation and synthesis. At times, particularly as lower levels, information must necessarily contain a lot of detail if it is to be useful, although the general rule of minimum possible detail for coherence with efficient information use should be followed. Given the need to be concise and to direct attention to where it is required, reports often purposely highlight items whose performance deviates significantly from a fixed standard or budget. An example of this type of report is seen in the accounting technique of budgetary control in which actual expenditure, measured item by item, is compared with the budgeted or desired expenditure. Small variations in these reports may be accepted, but differences exceeding tolerance levels are highlighted. These exceptions are presented to managers, thus enabling them to carry out their control function more quickly.

Comprehension

Comprehension is what transforms data into information. If the information is not understood it cannot be used and therefore it cannot add value. Many factors intervene in understanding information:

– User preferences. Some people prefer information in graphs or charts, while others prefer a narrative description. Some prefer presentations with statistics and figures, while others do not understand them. Research has shown that some people assimilate specific facts in detail, whereas others evaluate the overall picture without paying attention to the finer points. Inevitably, these variations mean that the same message can be interpreted in different ways.

– Previous knowledge. Comprehension is the result of memory in association with the received message.

– Environmental factors. Group pressure, available time and trust in the information system all influence comprehension.

– Language. Information is codified in signs or messages.

Information needs

We live in a world of information. Every day potential readers are presented with a multitude of books, journals and newspapers. However, human capacity is limited and we can absorb only a tiny amount of all this information. There are no clear procedures to help us to identify all information of interest quickly.

Information needs refer to the information required to take decisions correctly and to carry out the tasks deriving from them.

Three large sets of information needs are associated with the three stages in the strategic management process:

– A strategic diagnosis should be undertaken when a strategy is drawn up; in other words, an internal analysis and an environmental analysis – both general and specific – must be carried out. Information is an essential element in this strategic diagnosis stage.

Information is needed on the main strategic environmental factors: cultural, financial, political, competition, technological. This information should attend to the evolution of these factors, as well as their present state.

An internal analysis requires information generated by the company itself as a result of its activity. This information can be classified according to the *company's functions, namely, marketing, production, finance, human resources, R&D and management*.

– Each member of the company involved in implementing the strategy must be aware of his or her particular responsibility, and must receive information on the tasks he or she has to perform – and how to perform them – in order for the strategy and its component plans to be effectuated. In other words, those responsible for accomplishing these actions need information about what they have to do and how to do it. This information is usually passed down from higher to lower levels.

– Strategy control; efficient control requires knowledge on the outcomes of the actions undertaken to effectuate the plans, and how the different environmental components are evolving, in order to verify whether the strategy is developing appropriately and whether any changes are influencing its viability.

Some of the information used to draw up the strategy will also be required in the control stage in order to compare the strategy targets with the results being obtained. Information on the results of implementing the plans will also be needed at this stage. This information must be delivered at the right time so that when any deviations are detected in the control, opportune measures can be taken to correct them and achieve the target sets.

We can therefore consider three sets of information needs in the management process, each one of which will require different information and will be obtained in different ways.

It is extremely important to restrict the information to what is actually needed, as there is a risk of information excess, and everything that goes beyond the strictly necessity impoverishes rather than enriches the system, since it affects the cost of obtaining information. Information economics aims to determine the optimum amount of information for a specific problem, based on comparing the marginal cost of the information and the value of the sample or additional information. We know what type of information we want to obtain; we now examine the sources of information that can be used to obtain it.

Sources of information

Information is an essential, strategic resource that can be obtained from numerous sources. In this section, we distinguish between internal information relating to the environment within the company, and information about its external environment. Many of the data captured by information systems refer to the functioning of the organisation and are used to produce internal information. This internal information provides management with knowledge about how the company is functioning and whether or not it is achieving its objectives. Most internal information comes from the accounting system and statistical analyses (sales, production, etc.). Other internal information sources such as surveys and interviews with company members provide quantitative information on, for instance, workers' motivation levels or other indicators that are not easily quantified.

Company managers also need information on the environment: sales volume of their most direct competitors, potential client segments for the company's product lines, geographical distribution of its shareholders, etc. A company can only be successful if it adapts to the demands of its external environment. The environment is represented by a number of groups that vary in their capacity to influence the company's fulfilment of its objectives. Below, we identify these interest groups and the different types of information about them that the company requires:

– Customers: marketing, sales, levels of satisfaction.
– Distributors: marketing and logistics (distribution).
– Competitors: market penetration, innovations, product quality.
– Suppliers: transaction conditions.
– Trade unions: salaries and employment stability.
– Shareholders: company performance.
– Financial institutions: financial conditions and investment opportunities.
– Government: legal and political developments.

The company must be informed constantly about each of these external groups and, at the same time, some of these groups (e.g., shareholders and the government) must also receive information from the company.

Information on the environment can be obtained from the following sources:

– Personal information sources, which provide information through contact with sales staff, customers, suppliers, distributors, bankers, etc.
– Impersonal information sources, which range from general publications (e.g., reports on the current situation, bank and official entity reports, specialised journals) to specific studies (e.g., market research, opinion studies, consultants' reports).
–

Chapter2. Essential aspects

The concept of the information system

All systems can be divided into subsystems. Because the company behaves as a system, its different elements can be broken down into subsystems. According to the organisation theory literature, the company can be divided into the following systems: commercial, operations, financial, personnel, and information. The information system is related to all the other systems and the environment. The purpose of the company's information system is to gather the information it needs and, following necessary transformations, ensure that it reaches the members of the company who require it, whether for decision making, strategic control, or for implementing decisions adopted by the company (Menguzzato and Renau, 1991). A manager's performance therefore depends on his or her skills in exploiting the information system's capacities in order to obtain positive business outcomes.

For the purposes of this chapter we adopt the definition of an *information system* given by Andreu, Ricart and Valor (1991). According to these authors the information system is a formal set of processes that, working from a collection of data structured depending to the company's needs, gathers, processes and distributes the information necessary for the company's operations and for its corresponding management and control activities, thereby supporting, at least in part, the decision-making processes necessary for the company to perform its business functions in line with its strategy.

This definition, therefore, only includes the formal information system, which is the part of the information system that all the company's members are familiar with and know how to use. This does not mean that informal information systems are not important, but simply recognises the limitation that they are, by their very nature, more difficult to study, plan and manage, at least from a cohesive and holistic point of view. Informal information systems are not the result of a designed process; rather they provide chance information. We must not, however, ignore the existence of informal information channels, and the speed and efficiency with which they can operate, on occasions spreading rumours through the organisation more quickly than information that follows the standard channels.

The above definition refers to the functions and strategies of the company; by this, we aim to transmit the idea that a company's information system must serve its business approach. In the end, the information system is only one of the many elements that the company designs and uses to achieve its objectives, and as such, it must be explicitly coordinated in line with these objectives.

To complete this definition of an *information system*, we now attempt to clear up any confusion between information system and *computer system*. The computer system consists of a complex interconnection of numerous *hardware* and *software* components, which are essentially determinist, formal systems in that specific *input* always gives the same *output*. Information systems are social systems whose behaviour is largely influenced by the objectives, values and beliefs of individuals and groups and by the performance of technology. The way an information system behaves is not determinist and does not follow the representation of any formal algorithmic model.

COMPUTER SYSTEM **INFORMATION SYSTEM**

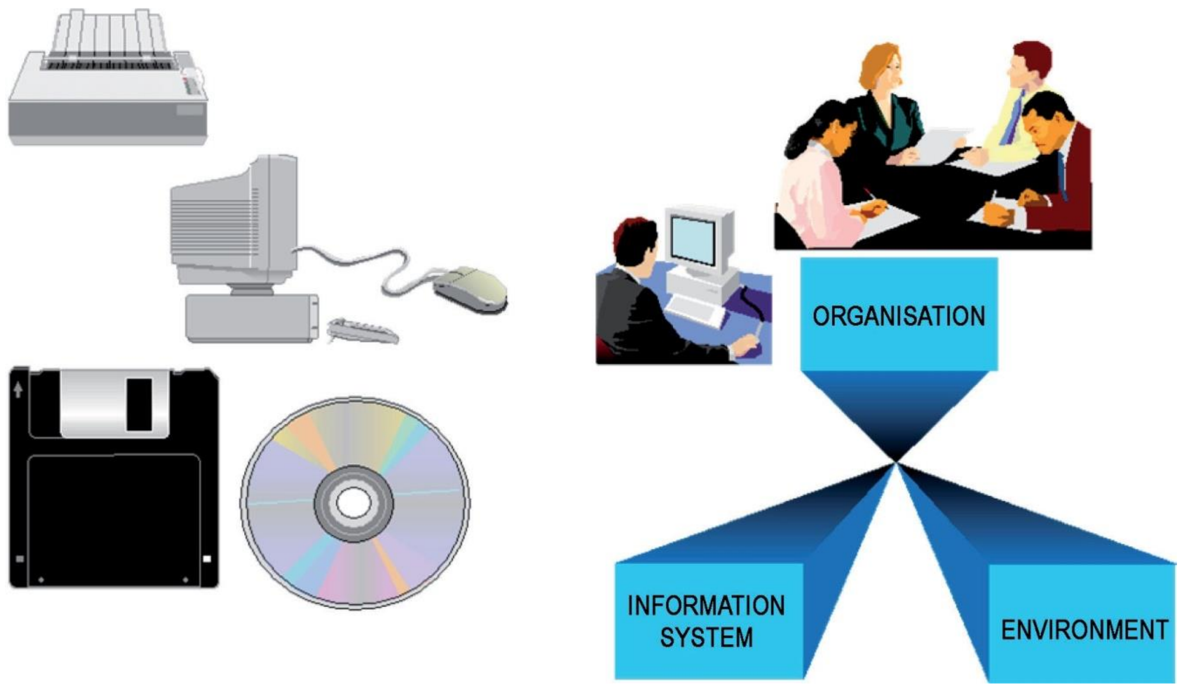


Fig. 2.1. Computer system-information system

Today's company information systems have to deal with a huge quantity of data and provide information structured in different ways to multiple decision- makers in the company. The role of the computer system is therefore vital to the company's information system. Given the major role of information systems, we believe that today's organisations cannot be efficiently and effectively managed without information systems that incorporate a series of information technologies. Information technology has therefore become a fundamental aspect in managing both small and large companies and enables them to seek out competitive advantages.

But an information system is more than just a computer system. It is inseparable from the organisation-environment system, and in the decision-making process we cannot expect that all the necessary information will be predetermined, formalised and computerised. Information circulates throughout the whole organisation like a current flowing through formal and informal channels and both horizontally and vertically. The information system is the organisational structure that has to manage these information flows with the maximum efficiency and effectiveness in order for the company to carry out its functions in accordance with its business plan or strategy.

The essence of every information system is that it provides the means by which the necessary information is delivered at the right moment and with the right structure to the members of the company who require it, whether for taking decisions, for strategic control or for implementing decisions that have been adopted.

Most of the problems that arise within business information systems are related to organisational, social or human factors rather than technical problems, which are quite scarce. Managers should therefore focus on the appropriate strategic and tactical application of their information systems.

Information system components

Information systems comprise hardware and software, telecommunications, databases, human resources and procedures (García Bravo, 2000).

Hardware

Nowadays all companies use computers, usually personal computers (pcs). Large organisations employ diverse computer systems including *mainframes*, *minicomputers and most commonly*, *pcs*. However, recent advances in the technical specifications of pcs now means that they perform many of the tasks initially done by minicomputers, and the difference between these two categories is becoming increasingly blurred.

The three computer types have a similar arrangement. The component controlling all the system's units is the central processor, which carries out the instructions given by a program. Other devices are used to introduce data (keyboard and mouse) and produce the system's *output* (printers).

Software

There are two types of computer programs: system software and application software. System software programs are used to manage the computer system's resources and simplify programming. Applications, like spreadsheets or word processors, directly help the user to do his or her work.

Databases

Many company information systems are used as a vehicle for delivering databases. A database is a collection of interrelated data, such as an organisation's human resource or product databases.

The customer database is extremely valuable to the company since it can be used to inform clients of new products or to develop new products that meet their needs. A database must be organised so it can be accessed according to its content; for example an order may be given to retrieve the names and addresses of customers that were invoiced for totals in excess of one million in the previous year. Databases are managed by software systems known as *database management systems* (dbms).

Telecommunications

Telecommunications are the means by which information is transmitted electronically over long distances. Nowadays, computer systems are generally connected by telecommunications networks. Various network connections are available to suit the needs of different companies. In a small company, pcs are connected by local area networks (lan), enabling their users to communicate and share data, tasks and equipment. Wide area networks (wan) are used to connect computers at greater distances, either within the company or in a different location. Internet, the 'network of networks', links up an immense variety of networks from diverse fields worldwide.

These connections enable pc users to access the company's databases and other computerised resources.

Human resources

Two types of human resources can be distinguished: information systems specialists and end users. Information systems specialists include systems analysts, programmers and operators. End users are the people who use the information system or the output they generate, in other words, the large majority of an organisation's members.

Procedures

Procedures are the policies and methods that must be followed when using, operating and maintaining an information system. Procedures must be used, for example, to establish when to run the company's payroll program, to determine how many times it should be run, who is authorised to do so and who has access to the reports it produces.

Functions of the information system

Companies or organisations develop information systems to help to perform the tasks they are specifically designed to do. For instance, a hospital will have a medical records system, police departments will hold criminal records, all companies will have a payroll system, supermarkets will use inventory systems, offices will have office automation systems, etc.

All information systems carry out a series of functions that may be classified as follows:

– Data capture and collection.
– Storage.
– Information processing.
– Distribution or dissemination of information.

Data capture and collection

This function consists of capturing both external (related to the environment) and internal (generated within the company) information and sending it through the communication system to the entities within the information system responsible for organising it to avoid duplication and useless information (noise). The person or people who capture the information will depend on what type of company they work for. Sales staff, purchasers, managers at different levels in the hierarchy or members of the company in direct contact with organisations in the environment can all act as information gatherers. The data capture and collection process should be more intense in the areas or sectors of the environment and the company that are subject to the greatest changes.

Once the information has been collected and filtered, and redundant information removed, it is stored.

Storage

The following questions require an answer:

1. How should information be stored?

By classifying it according to a particular criterion or at different points.

2. What type of system should be used to store information?

The system can vary from the traditional filing system to a computer processed database.

The use of one system or another will depend on the amount of data to be stored, how frequently it will be used, the number of users and whether or not access is restricted.

3. How should the user access to the stored information be managed?

The information may be stored in different services and departments, or in a single location to which all users have access. The company will decide which of these two options is most appropriate, depending on how specific the information is. Access to or retrieval of the information can take many forms; for example passwords may be used to access a database, enabling only authorised personnel to access the information when required.

Information processing

The purpose of information processing is to transform the stored information into useful information that will be meaningful to the person who requires it. This is a key function of all information systems. Information processing is essentially carried out by the computer subsystem. The spectacular development of computers has meant that on the one hand, the volume of stored and processed data is constantly increasing, and on the other hand, the falling cost of hardware has led to a generalised use of computers.

Distribution and dissemination of information

Not only must the information system provide the information each user requires, but it must also disseminate information to other people within the company. Different members of the company need to be aware of certain information about the company and the environment in order to respond more quickly and efficiently to everyday situations that require problems to be solved or decisions to be taken.

The information system and the value chain

In this section we contextualise and analyse the role of information systems within the value chain model. The value chain covers all the activities a company undertakes in order to offer a product or service. Value chain activities fall into two main categories: primary and support activities. Primary activities are more closely related to creating value. Support activities allow primary activities to take place by providing the necessary inputs and infrastructure. These activities link together to form the value chain.

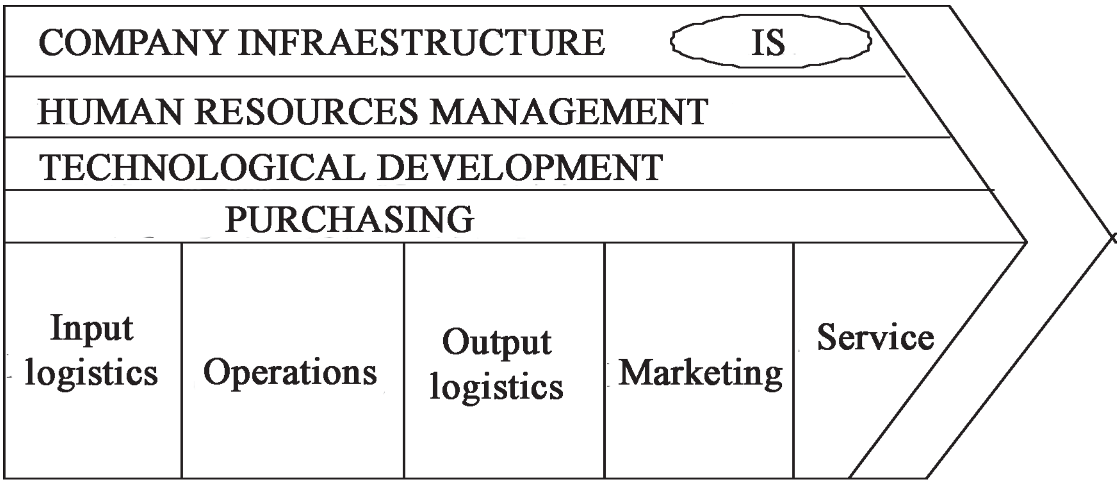


Figure 2.2. Value chain model

The primary activities are shown in the bottom part of figure 2.2 and include:

– Input logistics: the procurement of raw materials and supplies from suppliers.
– Operations: the transformation of raw materials into finished products with the appropriate quality, time and cost conditions.
– Output logistics: the transport of products to customers.
– Marketing: to detect customers' needs and procure orders.
– Service: activities designed to maintain the conditions of use for the sold product.

Support activities are presented at the top of figure 2.2 and include:

– Company infrastructure: the organisational framework that impacts all primary activities in a generalised way. These include all managerial activities, such as drawing up strategies, planning and control.
– Human resource management: all activities related to the selection, training and motivation of the company's staff.
– Technological development: all activities designed to procure and subsequently manage technologies.
– Purchasing: procurement of the elements needed to carry out the production process.

According to Andreu et al's definition, the information system forms part of the support activity known as company infrastructure. This tells us that all the value chain activities need support based on the information system. Because all the support activities sustain each other, the information system's role is to interact with all the company's activities, whether basic or support.

We now explore how information technologies can have a profound effect on each one of these activities, sometimes by simply improving efficiency, and at other times by changing the activity in a fundamental way:

Supply logistics

Information technology can have major repercussions on the supply of materials to manufacturing points. Some large chain stores are directly linked to several of their suppliers, particularly in the clothing industry. This link improves deliveries and reduces stock volumes, and affords greater flexibility to respond to changing demand almost immediately.

Operations

Many Spanish banks offer what is known as household or family accounts. Essentially, these accounts are traditional savings accounts with an added service: a regular summary of the account's transactions arranged by concept (outgoings such as rent, electricity, telephone, school fees, courses and so on, and income, usually the monthly salary). The client receives the equivalent of a balance sheet for a given period. The more transactions the client makes through the bank, the greater the value of the service; if all transactions are made through the same account, the summary will give the client a thorough analysis of his or her income and expenditure. Preparing these reports is a relatively simple task for the bank: the only information needed is reliable data on the type of transactions made.

Another example is that of cashpoint machines or atms, which have changed radically in recent years. A cashpoint service was previously considered to give competitive advantage, but now it has become necessary in order to compete and remain in the sector and all banks offer the same type of service.

Information technologies can also affect operations; one case is that of a cable news company which now offers a new line of financial services including instant financial information (foreign exchange rates, for example).

Dispatch logistics

Information technology has a major impact on the way in which products and services are delivered to customers, for example, connections to travel agency booking systems.

Marketing and sales

One agrochemical company has designed an on-line crop planning service for its main customers. With just a standard telephone line and their PC, farmers can consult agricultural databases with information on crop prices, the conditions necessary to grow the crop and the prices of fertilizers, pesticides, etc. They are then helped to reach a decision by a range of models and systems, which they can experiment with and adapt to their own growing conditions (climate, soil, etc.,) to study the implications of different crop rotations and planting programmes. The model helps the farmers to choose fertilisers, insecticides and other chemicals, and also to maximise discounts by grouping their purchases.

Marketing and sales activity, somewhat forgotten during the initial decades of the IT revolution, is now the area where these technologies are having the greatest repercussions.

After sales service

One lift manufacturer has installed black boxes similar to those used in aviation in its new line of products. This is a response to the numerous occasions when customers call the company's technical service without explaining how the breakdown in the lift has occurred. The maintenance engineer can now connect the device to the company's computer, find out the cause of the breakdown and then repair the lift *in situ*, thereby reducing repair costs and increasing customer satisfaction by solving the problem on the first visit.

Company infrastructure

Management control: a financial services company used to pay its sales team a commission for each product they sold. The result of this policy was that the sales team were highly motivated to make the initial sale but had no incentive to make sure that clients were satisfied and kept their money in the same place (extremely important for the managers of a financial services company). With a new integrated client database, the company has reduced the commission on the initial sale, and now pays a new commission if clients remain with the company and increase the assets they hold with it. This new approach (only possible with new technology) has brought the company's strategy and the sales team's incentives into line much more effectively.

Some airlines use a network to monitor the situation of each of their planes in any given moment. Information on the plane's position and passenger list, and the passengers' connection times, enables airlines to take better decisions by speeding up delayed flights or delaying takeoff where connections have to be made with other flights. The company therefore avoids income losses due to passengers continuing their journey on their competitors' flights if they miss their own connections.

Human resources

An oil company has installed desktop terminals for all the members of its management board, to give complete on-line access to all personnel records of the top four hundred employees in the company. These records provide data such as performance over the last five years and a list of positions that each person has held. The company claims that this capacity has facilitated its most important personnel decisions.

The systematic examination of a company's added value chain is an effective way of finding advantageous it applications.

All the value chain activities, whether basic or support activities, need and generate information. The information system compiles information generated by different activities that is later needed for other activities to function. The information system distributes this information to each activity (see fig. 2.1). From this perspective, the information system plays an important role in coordinating the various value chain activities. This role involves coordinating:

– between basic activities (e.g., ensuring that orders reach the production department);
– between basic activities and support activities (e.g., any control activity);
– between support activities (e.g., monitoring personnel involved in support activities).

The information system therefore plays a central role in ensuring the smooth working of interactions among value chain activities.

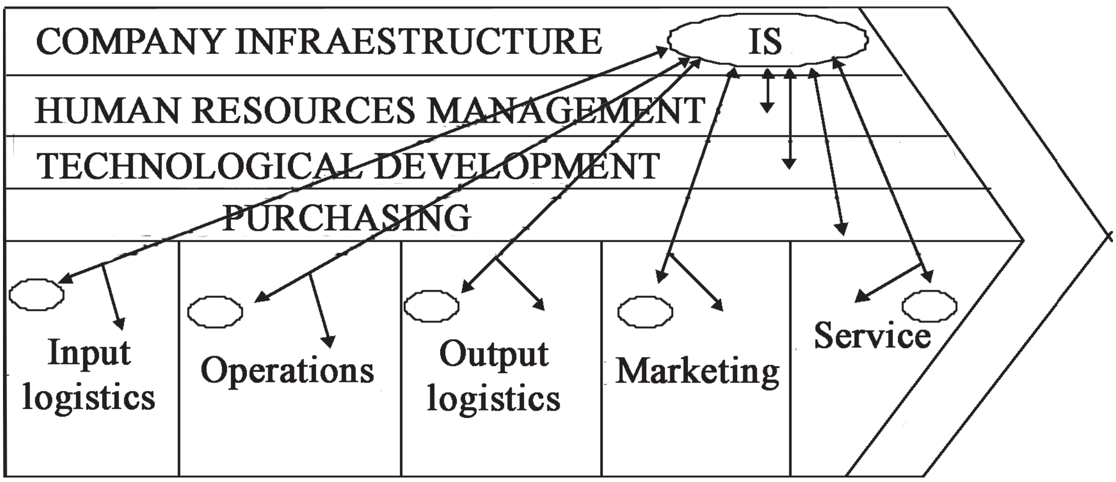


Figure 2.3. Model of the value chain with the information system

The information system is also highly relevant to the links between the value chain activities. For example, the systematic compilation of customer complaints by the information system can help to guide quality control procedures during the manufacturing process. The links between activities in the value chain can be improved through the information system. Exploitation of the links between activities can, in some cases, bring about a reconfiguration of the value chain, leading to new approaches to the same business and even to notable competitive advantages. Thus, the information system influences the design of the organisation's structure.

The information system compiles and distributes the information necessary for taking decisions or implementing initiatives throughout the whole value chain when this information is generated in other activities of the chain. For example, sales information may be relevant in taking decisions on after sales service; it may also be useful in designing the most appropriate service actions for a given set of circumstances.

By considering the information system as an integral part of the company's infrastructure, the information that it manages – although it is generated or used by specific activities – does not belong to any activity in particular but rather to the company as a whole. However, it is possible that some value chain activities need to produce, process and use considerable volumes of information that are not required in other areas of the company.

To provide for these circumstances, there are information systems or subsystems that are limited to specific activities; these are not part of the basic information system that is integral to the company's infrastructure. These information system or subsystem processes may also use or generate relevant information for other activities, so long as the quantity of this information is relatively small.

Some applications belonging to specific functional subsystems of the organisation are:

– Marketing: sales forecasts, sales planning, customer and sales analysis and evolution, campaign effectiveness...
– Manufacturing: production and schedule planning, cost control and analysis...
– Logistics: planning and control of purchasing, distribution, inventories, transport routes...
– Personnel: staff vacancies, evaluation (performance analysis), personnel administration (payroll...)
– Accounting and finances: accounting, costs, financial analysis...
– General management: strategic planning, resource allocation...

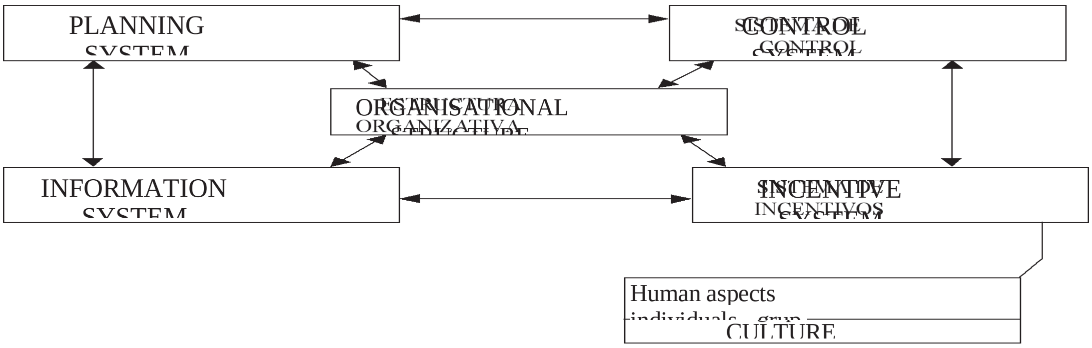
The information system and the company infrastructure

Every person in the company needs or generates information, and therefore no person in an organisation can be totally detached from its information system. The company's information system cannot be associated with any one of its activities in particular. It is not a new department, nor is it accountable to any one of the traditional functional departments. An information system project must have the commitment of all the representatives of the company's hierarchical structure. It is not a data processing centre, a misconception often held by some members of the company, including managers; a data processing centre is just one information resource, one area of information activities.

A broad vision of the organisation must be taken when designing a company's information system. If the system is to work properly managers must actively guide the process, since they are the ones with a global vision of their company. The company's management must take responsibility for adapting their organisation, structure and personnel to changes in the environment. If these changes involve a shift towards technological development, the responsibility for adopting new technologies in the company lies with its management, who must match the information technology to the company's needs. The impact of information technology on business is so vital that managers must always take full responsibility for guiding the company's information technologies and information system. However, many managers have traditionally been somewhat ill disposed to technological changes and have shunned their responsibilities in this area. This reticence is due to the fact that many top-level managers began their professional careers before the wide scale introduction of computer technology. As a consequence, they are not comfortable dealing with **it** issues, and have frequently delegated this area of responsibility to technical personnel, who although they are experts in their field, do not generally have much interest in the company's business activities.

In order to manage information technology and the information system, management must learn and advance in the organisational learning process, which entails incorporating, assimilating and exploiting information technology and the information system as a strategic tool. They must understand the role of the company's information system and how it works in harmony with other management systems. The information system is one of many elements in the company's infrastructure and must be consistent with other systems such as planning, control, incentives or the organisational structure.

The information system must be coherent with other systems that make up the company's



infrastructure, all of which must work in a coordinated manner with each other. The company's infrastructure is designed in accordance with its target objectives.

Fig. 2.4. Internal structure of the company's infrastructure

The figure represents the internal structure of the company's infrastructure. Information systems are an integral part of the whole infrastructure in the company. There is a complete, direct interdependence among all the systems; in other words, it would be a mistake to think that the information system and the control system are only interdependent through the organisational structure. They are, in fact, directly interdependent, in the same way that the information system and the planning system are. It is important to remember that the information system comprises a set of elements that must be coherent and coordinated with all the other systems within the company's infrastructure.

The set of systems should be coherent both internally, and with the company's objectives, which it must expressly contribute to achieving. This dual coherence has various implications:

On the one hand, internal coherence implies that a balance must be established in order to respect the interdependencies between the systems. This balance is not easy to achieve, but it can often be reached by making subsequent adjustments through compromises among the objectives of all the systems involved. On the other hand, coherence between the various systems and the company's objectives can only be achieved if the systems' design thoroughly and explicitly takes these objectives into account.

This concept of *balance between systems* is crucial and has a number of consequences. When any changes are to be introduced into any element of the whole, an imbalance will occur which, at the same time, will set off a 'balance recovery' process with potential implications for the other systems involved. In sum, it is difficult to successfully introduce changes in one element (e.g., the informationsystem) if theimplicationsofthesechangesforothersystems– inother words the company's infrastructure – are not taken into account. Consequently, any changes made must be highly balanced to minimise the resulting imbalances and spread them out over time, thus allowing the rebalancing tendency of the whole to solve the problem of its own accord. The best strategy for introducing changes will depend on each company and on the corresponding balance at any given moment, although human aspects, both group and individual, also have a part to play.

Managers with responsibilities for changes in the company's information system should take the following aspects into account:

– Resistance to change. There is generally a natural resistance to change within organisations. Because changes in the information system can entail modifications to the structure, culture and policies of the organisation, there is frequently considerable resistance to changes in the development of information systems. However, the company's managers must drive and lead these changes even though the process may be more complicated and slower than initially envisaged.

– Adapt technology to the organisation. The information system is there to serve the company and its objectives and, therefore, the technology the system uses must be adapted to the organisation. The information system must provide the necessary information to perform all the business functions in the company and to that end, the most appropriate technologies should be chosen.

– Understand the limits of information technology. We generally use technology to solve organisational and human problems, but we should always remember that correct, beneficial computer use depends on the user's intelligence and know-how. Experience shows that the companies that derive the greatest benefit from their information systems are not always those with the most technologically sophisticated systems; rather they have understood how to integrate the information system into the company's strategy so as to achieve its objectives, and have good communication channels between managers and it technicians. The information system is interdependent with the other systems in the company. The harmonious balance established among all these systems does not only depend on the information system.

Chapter 3. Information system
categories

Introduction

Given the complexity of information processing and the varying degrees or levels into which data and processes can be structured, depending on the problem or issue, several categories of information systems are required to deal with all the organisation's information needs.

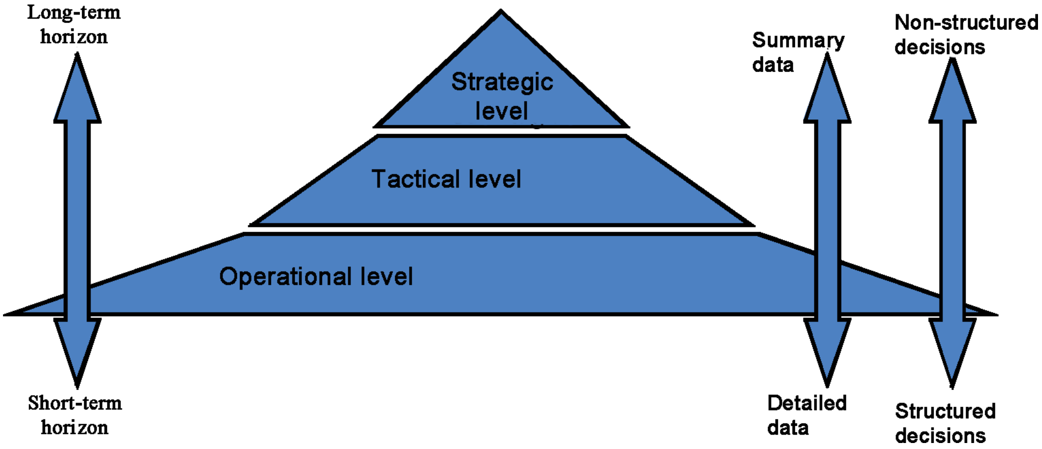


Fig 3.1. Levels of management

Different types of information systems must be developed to meet the whole gamut of information needs in a company: systems for processing transactions, management information systems and decision support systems (Arjonilla and Medina, 2007). The various information system categories remain coherent through their integration in a common data architecture.

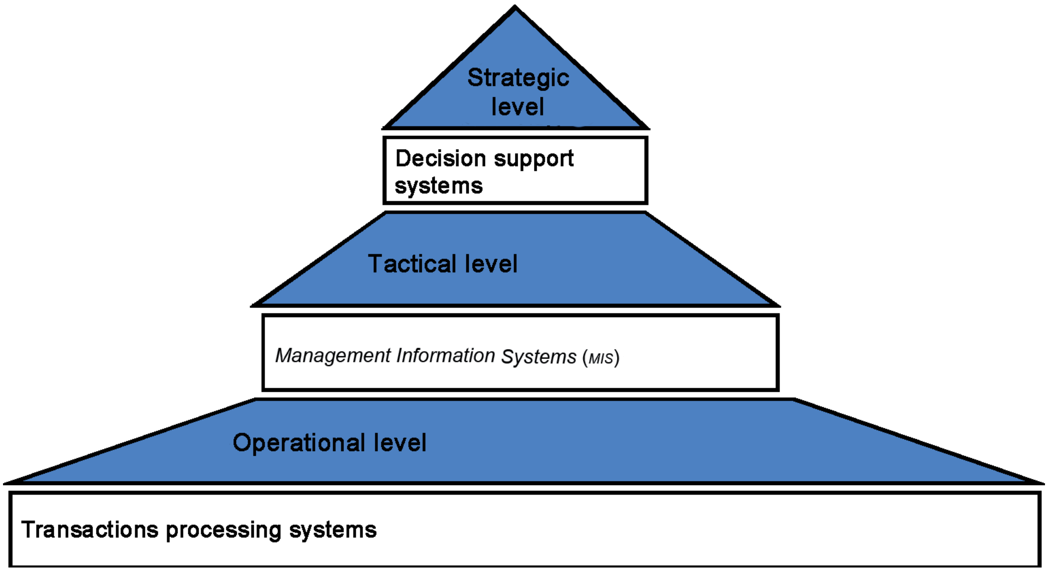


Fig. 3.2. Information system categories

Transaction Processing Systems (tps)

Transaction processing systems are the cornerstones of a company's information system and compile their daily business operations. Many companies cannot operate without this type of system. As operations are carried out in the company, transaction processing systems gather, process and store data and reflect business transactions such as sales, purchases, payments, etc.

Transaction processing systems are the most defined or structured information processes in the organisation, automating the central core of its operations. Their purpose is to improve the company's routine activities. The most common transactions include invoicing, payrolls, production and reception of orders. Companies aim to carry out these activities quickly, systematically and efficiently. All these activities are carried out at the operative level in any organisation and have similar common characteristics:

– These operations are repeated many times in companies.
– The way these transactions are carried out is very similar in all companies.
– The activities can be separated into well understood stages (procedures) that can be described in detail.
– There are very few exceptions to the standard procedures.

Theabovecharacteristicsallow routines tobeestablished for managingtransactions. The large volume of transactions at an organisation's operational level leads many companies to try and develop more efficient and effective ways of processing the data generated through this type of activity.

Transaction processing systems are faster and more accurate than the manual procedures used to perform the same routine activities. A transaction processing system replaces manual procedures with computer-based procedures to perform well structured routine tasks.

Transaction processing system output may take the form of transaction documents or database queries.

a) Transaction documents

Many transaction processing systems produce transaction documents, such as invoices, purchase orders or payroll lists. These documents may be classified as action documents or information documents.

a-1. Action documents

Action documents imply that some kind of action is taken. For example, an airline ticket guarantees that a seat on an aeroplane is reserved, or a bank has to pay out money when a cheque is presented.

a-2. Information documents

Information documents confirm that a transaction has taken place or informs about one or various transactions. For example, a bank transfer slip with details of the transfer, or a breakdown of credit card payments that accompanies the credit card bill.

b) Database queries

A wide variety of information can be extracted from a database using a database management system and user-oriented fourth generation languages. These queries can provide lists of all transactions processed during a specific time period, or error reports with a list of erroneously processed transactions.

Management Information Systems (mis)

These can be defined as information systems that provide information for users with similar needs. The main purpose of Management Information Systems is to provide managers with the information they need to take decisions and solve problems. Management Information Systems are supported by corporate databases, which include data generated by transaction processing.

Every organisation has to take decisions on many issues that arise on a regular basis, whether weekly, monthly, or quarterly, for which certain information is required. One example is the monthly breakdown of sales figures on a client by client basis. Because the decision-making processes are clearly defined, the information needed to take decisions can easily be identified. An administrative information system can therefore prepare regular reports on which to base these decisions; these reports are prepared and presented in a previously designed format. Thus, these systems provide support for structured decisions, since administrators know beforehand which factors should be taken into account in the decision-making process and the Management Information System provides clearly structured reports with all the necessary information to take these structured decisions.

The content of these reports can be enhanced by including the concept of management by exception. In this case, the information processor compares real performance with previously established standards, and when performance falls outside acceptable limits, the manager's attention is drawn to the fact. Management by exception can be incorporated into Management Information System reports in four ways:

1. by preparing a report only when exceptions occur

2. by using the report's sequence function to highlight exceptions. The report's entries can be arranged in ascending or descending order, according to one or more key areas, such that entries requiring greater attention appear at the top of the list. For example, a sales report could be arranged in descending order of sales for each

client during a specific time period; clients purchasing the largest volumes would therefore appear first. Another example would be sales volumes per item, in which an ascending order would place the products with the lowest sales volumes in a given period at the top of the list, thereby alerting the user to least successful items.

3. by grouping exceptions together. In this case, the reports are prepared so the user can find exceptions in certain areas according to a particular criterion. For example, a report could present clients' outstanding invoices in columns arranged by due date, either within one month, over 30 days, over 60 days or over 90 days. This makes it easy for managers to identify outstanding invoices for specific periods in a single column.

4. by showing deviation from the norm. Results of actions are compared with forecast actions and any difference is presented as a deviation. For example, a report could compare data on real product sales by geographical area with sales forecasts and present the difference in the deviations column.

In the 1960s attempts were made to develop an information system that would automatically meet all the company's information needs by means of an administrative information system known as the mis (Management Information System). The mis represented a formal commitment by executives to make IT available to all managers. The idea of the mis was to maintain a continuous flow of information to managers.

Figure 3.1 illustrates the relationship between the mis, the company's management and the environment in which it operates.

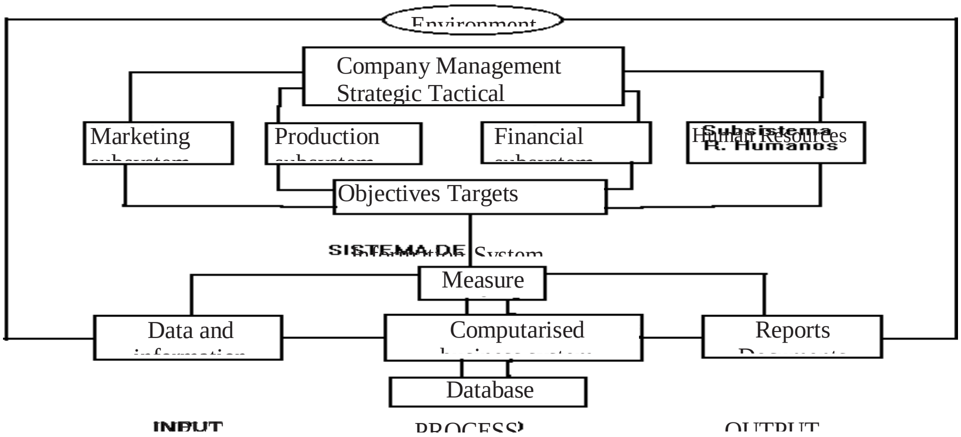


Figure 3.3. The mis-company management relationship.

The environment is represented at the top of the figure, the central section represents the company management and the company's various subsystems, and mis appears in the bottom section. Information and data flow from the environment to company management and to the mis. In addition, management sends information and data to the mis (mis inputs), which are processed by information processors specially designed to provide output in the form of documents and reports to management groups at strategic, tactical and operational levels, as well as to the environment. The database contains data from the accounts information system and also incorporates data from the environment.

Managers define the company's objectives, and set targets, plans and standards (centre of Figure 3.1). These plans and standards provide another type of input to the MIS, establishing the bases on which control and feedback can operate.

The software uses the database to produce its regular reports. The mis output should be relevant information sent in the right way to the right person at the right moment. This information must be carefully selected to help the decision-making processes at strategic, technical and operational levels (management). This output is used by those responsible for resolving the company's problems.

This information is normally compiled in:

1. Strategic level reports to provide managers with the information they need to plan activities such as defining and reviewing the company's objectives, setting long-term targets (more than three years) and establishing company policies.

2. Tactical (and status) situation reports to enable management to draw up new or revised short-term plans (from 1 to 3 years) on a continual basis, and to perform their planning and control functions efficiently so that the subsystems can be properly coordinated.

3. Operational reports with daily information to keep managers fully informed of the company's current situation, thus enabling them to carry out their control functions. In addition, much of the information the company sends to the environment is provided by the mis in the form of invoices to clients, and salary and tax payments.

Because the mis hosts an information system structured in accordance with certain previously determined decisions, it cannot be used to make decisions when an unexpected problem arises. The idea behind the mis is to help interpret the information needed to take previously defined decisions, and particularly at the strategic level, information needs are not easily identified.

Given the limitations of an information system like the mis in supporting non- programmed decisions, information system designers needed to look at the problem from a completely different angle (Menguzzato and Renau, 1991). Rather than being structured from the perspective of the person who interprets predetermined information needs, the information system should be conceived to give the greatest possible flexibility to the decision maker. In this way, instead of previously establishing what type of decisions are to be taken, information should be arranged according to its origin and type, based on decision-makers' general knowledge, so the necessary information is available to them when they have to take a decision. The design of the company's database is therefore crucial: it must enable information to be used rationally, and must allow the information system to be properly integrated. The company database must be flexible enough to be structured according to the particular needs of different decision-makers. This reveals the need for more interactive systems that help the decision maker to take non-structured or only slightly structured decisions.

Decision Support Systems (dss)

Not all company decisions are recurrent, and some have to be taken infrequently or perhaps only once. Decision support systems provide a tool to deal with less precisely structured or defined problems that arise sporadically. dss help managers who have to take non-structured decisions. A decision is understood to be non- structured if there are no clear procedures in place to take the decision, and it is not possible to identify beforehand all the factors that need to be considered in the decision.

It must be said that all information systems support decision making, even if only indirectly. dss have been expressly developed to support the decision- making process. These systems facilitate dialogue with the user when he or she is considering alternative solutions to a problem, and the system provides database access and models constructed to present information.

Decision support systems are interactive, and aim to expand human reasoning capacity to resolve specific non-structured decision-making problems (Gil, 1997). This type of system focuses on the decision-making processes and must provide relevant facts relating to the decision easily, quickly and accurately It must also offer interactive access to processing media that can be used creatively and that allow the user to explore a range of alternatives, and provide the information necessary to respond to the problem. When managers use a dss, they consider a number of possible scenarios by asking "What would happen if...?" For example, a manager who is deciding what price to set for a new product can use the marketing area of the decision support system. The system will have a model that combines various factors such as product price, the cost of materials, advertising costs, all of which affect profit forecasts for product sales over a five-year period. By varying the price of the product in the model, the manager can compare forecast results and select a price accordingly.

Unlike administrative information systems, decision support systems can help to make decisions for which a procedure cannot be fully programmed in a computer. To this end, some of the dependent relations between factors and their consequence are shown by computer models, and value judgements are introduced when the manager interacts with the system. Spreadsheets, which can help to manage data by representing them in columns and rows in a table, are frequently used to construct simple decision support systems.

The main purpose of decision support systems is to help the decision maker in the decision-making process. Unlike transaction processing systems and administrative information systems, dss are not structured or formalised, since they are generally used for *ad hoc* processes and therefore they need to be flexible and adaptable. The key aspect of a dss is that it supports decision making in situations where computer data processing capacity is needed in conjunction with the criteria or rationale of the decision maker.

The main emphasis of dss lies in its support function, and not the automation of decisions. The computer's task is to provide access to data and offer the chance to test alternative solutions, but it must not replace the manager's criteria. In other words it does not attempt to offer responses or impose a sequence of predefined analyses; rather it is the user who chooses how to tackle the problem and in the final instance, takes the decision.

A DSS uses data from the organisation's transaction processing system and administrative information system as well as data from external sources. In fact, the data required to generate information can come from a range of sources, not only the database as in the case of the transaction processing system and the administrative information system. Moreover, a dss can store and later reprocess previously obtained data. The user interacts with the system by making requests, creating or modifying models to adapt them to variations and to help understand the problem, managing data and designing the format and content of reports, which may include text, structured information or figures.

In using these systems it is essential to determine what information is necessary. In well structured situations this information can be identified beforehand, but this becomes complicated in non- structured environments. Once the manager has certain information, he or she may realise that more information is necessary; in other words certain information reveals a need for further information.

In these cases neither the format nor the content of the system's reports can be designed previously. Decision support systems must therefore be more flexible than transaction processing systems or administrative information systems. The user must be able to define the content of each report he or she wants. The manager's own criteria therefore play an important role in taking decisions on non-structured problems. While dss help managers, they are no substitute for the manager's own criteria.

One example of a non-structured decision is the decision banks had to take over whether or not to install atms. They had to calculate the cost of both manual and automatic services, the degree of customer acceptance, their competitors' response, etc.

Problem resolution with dss

dss are interactive information systems that help the decision maker deal with fairly unstructured problems by offering analytical models and access to databases. These systems are designed to help in the decision-making process. One of the main features of these systems is their flexibility. Personal dss should be easy to use: the tools should be oriented to the final user for this purpose. On the other hand, an organisation's dss, used widely by different members of a company, should be the result of a well planned process. All dss should be easy to use. Within its area of application, a dss should offer the user a way to apply models and databases interactively that enhances the support it gives to deal with the problem the user faces.

So, what is the essence of dss? In what type of business situations should the dss approach be considered?

The way people in an organisation tackle a problem will vary according to how structured the problem is; in other words, it will depend on the extent to which predefined procedures are in place to take decisions on the matter in hand.

Principally, dss help to take decisions on semi-structured problems, where some phases in the decision process often require considerable computer support. This is because a model, which can contain hundreds of relationships, is applied to a database that frequently contains a large amount of data; the decision maker intervenes in the selection of this data. dss can also be used to take decisions on non-structured problems. These decisions can also be taken with the support of expert systems, although with a very limited field, such as the decision to approve a loan application.

The main tasks facing managers involve a high level of ambiguity; in other words they generally have to deal with non-structured or semi-structured problems.

Possibilities of Decision Support Systems

A model is a representation of something, designed for a specific purpose. It is usually an abstraction or a simplification of a phenomenon. A model represents the relationships between the aspects resulting from the phenomenon. A model is constructed by adopting a series of suppositions or assuming a series of premises about the dependence between variables. Various alternatives can then be analysed by changing some variables and seeing what would happen if the premises were modified and then comparing the results (What would happen if...?"). For example, what would happen if we changed a product's sale price? What value would a variable need to have to achieve a certain result? What volume of sales would we need to obtain a given net profit?

Using a spreadsheet as a decision-making support system

The spreadsheet program is widely used in the work environment and is now the standard software used to manage information in the business world. Despite this widespread use, we believe that a low percentage of users take full advantage of the spreadsheet's potential. The spreadsheet could be better exploited by applying the logic used to construct models with different scenarios. In many cases, poor use of the spreadsheet leads to considerable loss of time and on occasions, the program cannot be used to carry out some types of analysis.

The purpose of the spreadsheet is not to perform complicated mathematical operations; a calculator is sufficient for that. The spreadsheet comes into its own precisely when the result of the first calculation appears, which should lead on to an analysis of this result. The spreadsheet can also help achieve greater productivity when it is used to perform regular repetitive operations. The spreadsheet also includes logical functions and search functions that allow the user to delegate more mechanical decisions to the computer such as, for example "if this value is lower than that one, then multiply by x".

Hence, when we are about to start a task with the spreadsheet, we can have two aims:

– to construct a model for decision-making support, in which case our target should be to achieve maximum possible flexibility.
– to mechanise a repetitive process that we have to do on a regular basis, repeating the same calculations, which should aim to be both convenient and secure.

When constructing a spreadsheet, it is essential to know exactly what our objectives are; this will help us take the right approach to achieve our objectives.

Using a dss in the decision-making process

The general, the decision-making process has four stages. During the first stage, known as the intelligence stage, the environment is explored in order to find or define the problem. During the second stage, the design stage, various alternatives are drawn up for comparison during the selection stage. The solution is then applied and improved where necessary. Each one of these stages can provide feedback to a previous stage in order to redefine the problem or select a better solution, for example.

dss can help at different stages of the decision-making process.

Spreadsheets are usually used to construct simple decision-making models. They do, however, have limitations. Their data-handling capacity is limited and they cannot work with very large databases.

Executive Information Systems (eis)

dss mainly support planning tasks, whereas the essential feature of the powerful eis tool is their support for control activities. An executive who uses an eis has a greater capacity to analyse all aspects of the company's operations and to seek out problems and opportunities.

Since companies timidly began to adopt Information Technologies (it), there has been a growing conviction that it cannot easily be applied to managerial tasks: the more complex and ambiguous the activity is, the less useful computer-based tools prove to be.

This conviction can easily be verified in the real business context. Computers are now widely used by administrative staff and increasingly by middle management. However, the image of a general manager of a large company busily working in front of a computer screen does not easily spring to mind. A top-level executive's daily routine is inevitably assumed to be a round of meetings, telephone calls, conferences, conversations, business lunches, etc. Research shows that the executive's activity is more oriented to verbal communication, and highly analytical reports and documents are relatively unimportant (Rockart and Treacy, 1982). However, there is a widespread interest in linking up high-level management with computer tools.

The evolution of information systems

Since its beginnings, it has clearly been conceived as a source of solutions for business management. The stages described below show the path of its development:

– First to appear were the Transaction Processing Systems (tps), which replaced manual procedures for clearly structured routine tasks with faster and more accurate computer-based procedures. Some of the most common transactions now performed by tps are invoicing, accounting and payroll management.

– At the end of the 70s, the concept of the mis (Management Information System) attempted to meet all the company's information needs at the strategic, tactical and operative levels, structured according to specific predefined decisions. However, in practice these systems have not been useful to top-level managers, because they generally have to deal with new situations that require non- structured decisions for which information needs are not previously established. For this reason, mis are particularly suitable to cover the information needs of lower-level managers.

– Once it had become clear that comprehensive strategic information system models were not viable, Decision Support Systems (dss) were introduced.

These provided solutions for particular decision-making contexts, and in the end have proved to be more suitable for certain company staff areas.

The idea of providing regular and relevant information to high-level managers has attracted the attention of information system researchers since it was first introduced into organisations (Applegate, Cash and Mills, 1988). Different types of computerised information systems have pursued this ambitious goal. Both mis and dss were first offered as systems to fulfil these needs. However, many researchers have found that both mis and dss, while useful for other levels in the firm's hierarchy, fail to satisfy the information needs of top-level management.

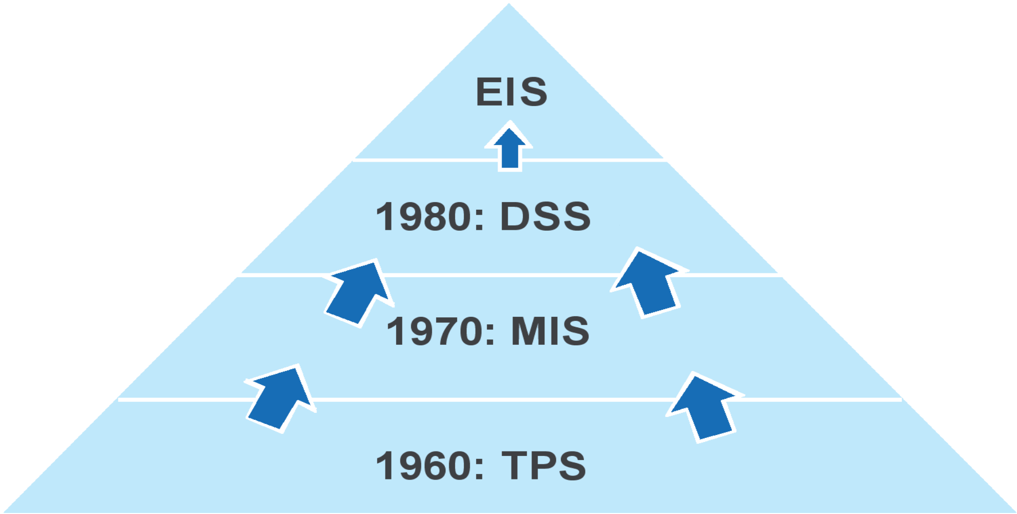


Fig. 3.4. Evolution of company information systems.

Given that the undertakings and responsibilities of management differ substantially from those of other people in the company, their tasks clearly cannot be seen as a mere extension or intensification of the work done at lower levels in the company hierarchy, for whom as we have seen, suitable computer based solutions are available. As a result, executives need specific computer support, which differs from the support provided for other members of the organisation.

It is in this context that Executive Information Systems (eis) appeared as the next candidate to provide top-level managers with the information they need. These systems have been designed to offer reliable information to executives about key indicators of the workings and operations of their organisations.

Executive Information Systems (eis): concept and characteristics

An eis can be understood as a computer-based information system designed specifically for use by top-level company managers, providing internal and external information that they can use as a support in performing their work.

Although definitions of eis vary, there is a general consensus on the characteristics they all share, which we now detail below:

a) Capacity to access and manage information

eis must gather the internal and external information that is relevant to the executive, and must therefore be able to access and manage information from a range of sources and in different formats, and handle quantitative and qualitative, structured and non-structured information.

An eis provides direct access to information without the need for intermediaries.

b) Presentation of information

The information must be presented to the user in a meaningful and manageable way, which involves combining data from different sources in the same report or on the same screen, and filtering and condensing a wide range of information. As well as its capacity to aggregate information, an eis must also allow the executive to explore more deeply and obtain additional more detailed information on a specific aspect if he or she considers it necessary.

The presentation of information must be adapted to the user's personal preferences, for example by offering choices on how the system can alert the executive to deviations in any variable.

c) Orientation to Critical Success Factors (csf)

The eis must provide information on key business variables, and must be flexible enough to adapt to possible changes occurring in the business, guaranteeing that the system remains oriented to critical success factors. For this reason, the design of the eis must allow for constant evolution. The eis must be able to accurately determine the user's information needs in order for it to have the right orientation; to a large extent, its success or failure depends on this capacity.

d) Capacity for communication and time organisation

An eis must also act as a support for communication, through electronic mail, and in organising the executive's work in the diary or calendar that usually comes with the system.

e) *Ease of use*

These systems must match the user's profile, in this case, people who do not usually have any it training and moreover do not have the time to acquire it. This means that they must be easy to use and allow direct, intuitive access to their features. The eis learning curve should be no longer than a few minutes.

eis are one of the most promising tools that technology has made available to companies. They allow an executive to understand and analyse the forces acting in the company and in the market without moving from his or her own desk. Executives can use eis in two ways: to read information about the current situation and forecasted trends, and as a tool to perform personalised analysis.

Executives use eis in two completely different ways: *a*) to access information on the current situation and on foreseeable business trends; and *b*) to perform personalised analyses of available data. We now turn briefly to these two usages.

a) Access to information

When executives have "read-only" access to the latest data or reports on the situation of key variables, they can examine the information but do little, or perhaps nothing, in terms of processing the data. This type of access may be widely used in sectors where market conditions change quickly, where executives have to keep up with a lot of reports, or where hour-by-hour monitoring of operations is important.

b) Personalised analysis

Naturally, executives can use the computer not only to gain exclusive access to information, but also as an analytical tool. The type of analysis will vary from one executive to another. Some will simply calculate new ratios or extrapolate current trends for application to future scenarios. Others will highlight trends of particular interest on figures or graphs to gain an additional visual perspective. Some work with simulated models to determine where capital investments will be most productive. What is important is that the eis allows the executive to consider, change, extend and operate data according to procedures that are meaningful to him or her at a personal level. For this method to be efficient, executives will inevitably spend a lot of their own time and effort in defining the data they need and learning what the computer can do. Users will need at least some initial training and assistance with the computer languages involved.

Sales and Distribution Management (315)

UNIT 1

Introduction to Sales Management

Originally, the term 'sales management' referred to the direction of sales force personnel. But, it has gained a significant position in the today's world. Now, the sales management meant management of all marketing activities, including advertising, sales promotion, marketing research, physical distribution, pricing, and product merchandising. The American marketers association (AMA's) definition, takes intoconsideration a number of these viewpoints. Its definitions runs like: the planning, direction, and control of the personnel, selling activities of a business unit including recruiting, selecting, training, assigning, rating,supervising, paying, motivating, as all these tasks apply to the personnel sales-force.

Sales management, personal selling and salesmanship are all related. Sales management directs the personal selling effort, which in turn, is implemented largely through salesmanship.

The term personalselling and salesmanship are often used without distinction. However, there are vital differences between two terms. Personal selling is a broader concept than salesmanship. Salesmanship is one of the aspectsof personal selling. Salesmanship is one of the skills used in personal selling, it is not all of it. 'Salesmanship is the art of successfully persuading prospects or customers to buy products or services from which they can derive suitable benefits, thereby increasing their total satisfaction'. Salesmanship is seller initiated effort that provides prospective buyers with information, and motivates them to make favourable decisions concerning the seller's products or services.

The sales management activities are performed by the sales managers who are responsible to manage all the sales activities within and outside the company or the organization. Within the organization includes developing a formal and informal environment to ensure effective communication of Sales goals, targets and strategy not only within the sales team but within the other departments too. Outside the organization the sales managers are responsible for maintaining a healthy relationship with the customers and providing them better services. The role of Sales managers not only ends here but continues with making the sales strategies, target assigning and price modification and to design and plan modules to face market challenges.

“Sales management: The attainment of sales force goals in an effective and efficient manner through planning, staffing, training, directing, and evaluating organizational resources.

Sales management refers to the efforts of a business to maximize the benefits a company and its customers receive from its sales force. A sales manager establishes goals, meets quotas and hires a staff of the best sales people possible.

EVOLUTION OF SALES MANAGEMENT Broadly speaking evolution of Sales Management developed under the following four phases:

1. Pre-industrial revolution period.
2. Production oriented period.
3. Sales oriented period.
4. Customer oriented period.

Pre-Industrial Revolution Period Small-scale industries/crafts existed prior to Industrial Revolution period. The owner/craftsman turned entrepreneur, looked after all areas and functions of management. These areas are production, finance and design and development. Sales and marketing was never a serious problem in those days since demand far exceeded supplies. Selling was only a part-time job for these entrepreneurs. This job is mostly confined to demonstration or display of their craftsmanship.

Production Oriented Period Industrial Revolution in 1760s heralded this period. Mass production technique introduced during this period, increased the production level manifold. Following were the characteristics of this period: Prevailed in developed nations in the West till 1930s. Focus was on manufacturer and production capacity. Emphasis was laid on production process which yielded volumes. Marketing meant "sell what is produced". Environment was that of a "sellers market".

Sales Oriented Period Economic recession of 1930s was the starting point where demand declined. Following are the characteristics of this period: Prevalent in developed nations in the past. However still prevalent in developing nations. Focus is on sales and sales promotion with emphasis on sales volume. Marketing means "product does not sell by self-it has to be pushed. Customers are to be manipulated." Environment is highly competitive where "supplies are in excess and production capacity is more.

Customer Oriented Period: Globalization and liberalization have further increased the competition manifold. Following are the characteristics of this period: Prevalent in developed nations after 1960s. Developing nations are also following this approach by 1980s. Focus is on "customer satisfaction." Emphasis is on "problem solving" on customer "needs" and "wants“ to achieve customer loyalty. . Marketing means customer satisfaction before, during and after sales. Environment is that of “buyers market” having severe competition.

‘Personal Selling’ is a highly distinctive form of promotion. It is basically a two way communication involving not only individual but social behavior also. It aims at bringing the right products to the right customers. It takes several forms including calls by company’s sales representative, assistance by a sales clerk, an informal invitation from one company executive to another. It is employed for the purpose of creating product awareness, stimulating interest, developing brand preference, negotiating price etc.

The increase in complexity of products has increased the importance of personal selling. Manufacturers of highly technical products such as computers, electronic typewriters, digital phones, microwave kitchen appliances, remote control equipment’s etc. depend more heavily on personal selling than do grocery or toiletry products

Consumers want all sorts of goods and services but inertia may keep them from buying. Sales efforts stimulate the consumption process by reducing people’s inherent reluctance to make purchase decision. In fact sales person act as catalyst in the market place. When the nature of the product is such that the buyer needs special information in order to use it properly, sales representative acts as a consultant to consumer, to apprise them of products technicalities and usage. Sales person also work out the details of manner and timing of given physical possession.

SCOPE OF SALES MANAGEMENT

(1) **Planning:** a business cannot be taken as a chance. Every salespeople or person concerned have to see for the future, in a planned way like what must be done? And who will do it? The plan must be based on extensive market research, and the facts must be verified at every stage. The plan should also be evaluated, after investigating the total-market, for a particular type of product. Flexibility must be provided by establishing a specialists production line, to allow for variation in production. The plan should also be subject to continued review. The details of the plan should be discussed, with all the departmental heads, concerned, and their sub-ordinates, who bear responsibility for fulfilling their parts of the plan.

(2) Co-ordination: Co-ordination is all pervasive and permeates every function of the management-process. For example, ill planning, departmental-plans are integrated into a master. Plan, ensuring adequate co-ordination. Similarly, organising starts by co-ordination wholly, partially inter-departmental and inter-personnel matters. Co-ordination also helps in maximum utilisation of human-effort by the exercise of effective leadership, guidance, motivation, supervision, communication etc. The control-system also needs coordination. Co-ordination does not have any special techniques. Nevertheless, there are sound principles, on which to develop skills. It has a special need to help the staff, to see the total picture and co-ordinate their activities, with the rest of the team. The sales manager has to encourage direct personal-contact, within the organisation, particularly where there is lateral-leadership. Harmony, and not discord, should be the guiding mantra. In addition, one has to ensure free flow of information that is selective to the objectives of the business. No personal problems, arising from businessoperations are to be ignored, but solved through a freeexchange of ideas. This is especially true in the case of the sales-force of any organisation.

(3) Controlling: the sales manager has to check regularly, that the sales activities are moving in the right direction or not. He guides, leads, and motivates the subordinates, so as to achieve the goals planned for the business. He has to take steps to ensure that the activities of the people conform to the plans and objectives of the organisation. The controlling system should be such that one can study the past, note the pitfalls and take corrective measures, so that similar problems may not occur in the future. The controller has to ensure that the set targets, budgets and schedules are attained or followed in letter and spirit. There must be procedures to bring to light the failure to attain a target. The control-system has to (i) prepare sales and market forecasts; (ii) determine the level of sales-budget; (iii) determine the sales-quotas for each salesman; (iv) determine, review and select distribution-channels; (v) organise an efficient sales force; (vi) establish a system of sales-reporting; (vii) establish a system of statistical sales-credit; (viii) establish stockcontrol system(s); (ix) review of performance of the salesforce; and (x) establish periodical testing programmes. In a big organisation, each salesman is assigned a territory (not so big that it cannot be adequately covered). Each salesman has a target, set for specific ‘period. From the weekly and monthly sales-reports, the control system is established, that will prepare records whether a particular salesman is working efficiently or not.

(4) **Motivating:** Motivation is essentially a human resource concept. It aims to weld together distinctive personalities into an efficient team. For this, knowledge of human psychology is needed, as a means of understanding behaviour patterns. This is especially important in the case of the sales-force. Only motivated sales-persons can achieve company’s goals.

Importance of Sales Management

Sales management is one of the key components that every business which relies on sales must practice. Sales management is the training and management of a sales staff, and the tracking and reporting of the company's sales. It is important to a business because if the principles of sales management are practiced correctly, it can increase your company's sales.

Goal Setting

- To achieve sales goals, your company needs to set sales numbers or goals for the staff. One way for a company to achieve and maintain growth is to increase its sales numbers. Sales managers can set sales goals that will promote growth and are attainable by the sales staff. Many sales managers use cash bonuses or other incentives to motivate staff to achieve the goals. Sales goals for staff can also be set to match the strengths of each staff member.

Tracking

- Sales management enables management to track the overall sales of the company as well as the individual sales of each employee. Using sales tracking, management is able to tell if the company is on track to meet its goals or if individual members of the sales team are not producing enough sales. By keeping the sales force constantly up to date on the status of their sales, you can help them to adjust their sales techniques and productivity to achieve the company's sales goals.

Reporting

- Using sales management, a company can produce sales reports that can be used to track the performance of its sales force over different periods. For example, you can use sales reports to compare the sales of the company on different years over the same period. The sales reports can determine the direction your company must take based on the results. For example, if the sales reports determine that your company is experiencing substantial growth year after year, it may indicate that expansion is a possible direction for the company.

Sales System

- As a company grows, it can become more difficult to track and manage the sales process without a system in place. Sales management provides companies with a system to train and manage employees while streamlining the sales process from the individual sales employee to the customer. This is beneficial because if there is a problem at any point of the sales process that may affect the company's bottom line, it can be quickly identified and corrected.

Role and Skills of Sales Managers

Role of the Sales Managers

Planning Functions: Lays down sales objectives, policies and strategies. Prepare a sales plans and programme to implement sales strategies. Design and administer suitable sales organization. Designing sales territories & deciding the size of sales force. Formulation of personal selling objectives. Organizing sales forces selection, recruitment socializing (orientation) and placement. Training and development, career planning, transfers and promotion.

- There are two opinions on the success of sales managers.
- Sales abilities are inborn qualities

- Sales abilities are developed. Some of the sales abilities like gift of gap, pleasing manner, extrovert nature are inborn. However, others like analytical ability, negotiation skills, leadership, etc. are developed.

Skills of a Successful Sales Manager

People skills include abilities to motivate, lead, communicate, coordinate, team-oriented relationship, and mentoring

- **Managing skills** consist of planning, organizing, controlling and decision making
- **Technical skills** include training, selling, negotiating, problem-solving, and use of computers
- **Following five abilities are identified**:
- **Leadership and Supervision**: Leadership and Supervision Motivating salesmen in competitive environment need, more than anything else, the leadership qualities. Leadership means the ability to influence subordinate willingly doing their work meticulously. This involves proper delegation of authority, effective supervision through direction and control, better communication skills etc. By effective supervision, work is distributed based on capabilities and aptitudes of each
- **Planning and Conceptual Skill**: Planning and Conceptual Skill Market manager must be able to foresee these changes in advance and alert his management to take corrective actions in time to attain and sustain competitive advantage in market. Furthermore, such changes must be incorporated in the planning by updating or amending plans.
- **Self-direction and Self control**: Self Direction and Self Control Sales executives are the "live wire" in an organisation and are the revenue earners. Being at the centre stage of activities, sales manager must know what company expect from him. Whether defined or not, he must assign his own duties and responsibilities and act accordingly. Being a specialist in his field, he does not look up to anyone in his organisation to guide and control him. As and when market conditions change, he rewrites his own agenda and assumes responsibility of new tasks, self-assigned by himself.
- **Organising abilities**: Organising Ability Sales manager must be a good organiser and real “GO-GETTER". He must organise an effective team, make a

structure suitable for a given situation, recruit and select proper salespersons to manage different territories & products, delegate authority, co-ordinate and control their activities, motivate and compensate their work, recognise their efforts and acknowledge good work. He is to develop his team giving them adequate monopoly and freedom of action and at the same time maintain strict control on their activities keeping in mind, that the organisational objectives are not lost sight of.

- **Time-management**: Time-Management Time is the scarcest of all resources. One has to balance his time between planning functions, and operating functions properly. SM must also find time for meeting his salesmen, customers and distributors. Also find time to meet his superiors at corporate headquarters, as well as do liaison functions with other departments.

Types of Sales Managers

The role of a sales manager is to oversee and motivate the sales staff. According to the American Society for Training and Development, sales managers most often come up through the ranks and get promoted following a successful sales career. Each manager brings a different set of strength and skills to the job. As a sales manager, you may fall into a certain type, but to be truly effective, you should incorporate the characteristics of each of the various types of managers.

Hands-On

At first, you may be more inclined to operate as a hands-on manager because of your own effectiveness in sales. The hands-on manager is on the sales floor, in meetings with clients and involved in closing sales. While you may get the job done, you may not be fulfilling your duties to your sales staff by providing them with the support and training they need to excel.

Reactive

Without a clear plan and definite rules for your sales staff, you could end up being tagged as a reactive sales manager. When you find yourself putting out fires, responding to customer complaints and reporting to the executive office more than participating in planning sessions with your sales staff, you may be developing a reactive style of management that could lead to burnout.

Coach

The coach acts as a teacher and mentor for the sales staff and stands back to watch each salesperson's presentations. This type of manager allows salespeople to make mistakes and follows up with regular sessions to go over the sales approach, guiding salespeople and listening to their problems. If you want to be a coaching manager, you have to prepare to lose some of your numbers while you remain in the background. This could makes your own bosses unhappy if they don't understand the approach.

Tyrant

The tyrant sticks to the facts, continually bombarding salespeople with numbers, quotas and threats. The tyrant is demanding, constantly pushing the sales staff for results. Managing a sales staff through fear can get results in the short run, but salespeople usually come to resent the tactic. When you need team support for your staff to rally around a common goal, they might be reluctant to give you the support they don't receive from you.

Cheerleader

The cheerleader is a motivator who's often seen as a positive force by the sales staff. As a cheerleader, you may give your staff sufficient praise but have trouble pointing out problems or areas that need developing. The cheerleader runs contests and gives prizes for exceptional sales efforts, but such incentives can be hard to get from top management.

Controlling

The controlling manager resembles the hands-on manager in some ways, but where the hands-on manager is energetic and involved, the controlling manager micromanages salespeople and doesn't let them take the initiative. If you find yourself becoming a controlling manager, you need to learn to delegate or you will burn out and alienate your sales staff.

Evolving

An evolving manager seeks new ways to build sales and experiment with novel techniques to motivate the sales force. If this is your style, you need to balance the innovation with consistency to avoid being seen as wishy-washy. Don't leave your staff wondering what work will be like next week when you try yet another new approach to sales management.

PERSONAL SELLING

Sales management, personal selling and salesmanship are all related. Sales management directs the personal selling effort, which in turn, is implemented largely through salesmanship. The term personal selling and salesmanship are often used without distinction. However, there are vital differences between two terms. Personal selling is a broader concept than salesmanship. Salesmanship is one of the aspects of personal selling. Salesmanship is one of the skills used in personal selling, it is not all of it. 'Salesmanship is the art of successfully persuading prospects or customers to buy products or services from which they can derive suitable benefits, thereby increasing their total satisfaction'. Salesmanship is seller initiated effort that provides prospective buyers with information, and motivates them to make favourable decisions concerning the seller's products or services.

'Personal Selling' is a highly distinctive form of promotion. It is basically a two way communication involving not only individual but social behavior also. It aims at bringing the right products to the right customers. It takes several forms including calls by company's sales representative, assistance by a sales clerk, an informal invitation from one company executive to another. It is employed for the purpose of creating product awareness, stimulating interest, developing brand preference, negotiating price etc.

The increase in complexity of products has increased the importance of personal selling. Manufacturers of highly technical products such as computers, electronic typewriters, digital phones, microwave kitchen appliances, remote control equipments etc. depend more heavily on personal selling than do grocery or toiletry products manufacturers.

Ever growing competition from domestic and foreign sources have also increased the importance of sales persons in the marketing effort of a firm. In personal selling, company's sales persons are often referred to as sales representative, salesman or sales girl, they remain on the company's payroll or work on commission basis or both to push the product in the market by positively motivating the prospective customer through oral presentation or demonstrating the product in question.

Consumers want all sorts of goods and services but inertia may keep them from buying. Sales efforts stimulate the consumption process by reducing people's inherent reluctance to make purchase decision. In fact sales person act as catalyst in the market place. When the nature of the product is such that the buyer needs special information in order to use it properly, sales representative acts as a consultant to consumer, to apprise them of products technicalities and usage. Sales person also work out the details of manner and timing of given physical possession.

PERSONAL SELLING OBJECTIVES

The qualitative personal selling objectives are long term and concern the contribution management expects personal selling to make in achieving long-term company objectives. These objectives generally are carried over from one period's promotional program to the next. Depending upon company objectives and the promotional mix, personal selling may be assigned such qualitative objectives as

1. To do the entire selling job (as when there are no other elements in the promotional mix).
2. To "service" existing accounts (that is, to maintain contacts with present customers, take orders, an
3. To search out and obtain new customers. d so forth).
4. To secure and maintain customers' cooperation in stocking and promoting the product line.
5. To keep customers informed on changes in the product line and other aspects of marketing strategy.
6. To assist customers in selling the product line (as through "missionary selling").
7. To provide technical advice and assistance to customers (as with complicated products and where produc
8. To assist (or handle) the training of middlemen's sales personnel. ts are especially designed to fit buyers' specializations).
9. To provide advice and assistance to middlemen on management problems.
10. To collect and report market information of interest and use to company

management.

Theories of Selling

1 **AIDAS Theory of Selling** Prospect goes through Five Stages i.e. Attention, Interest, Desire, Action and Satisfaction Sales Presentation must be structured in a manner that that leads the prospect in the right sequence Securing Attention: Receptive State of mind Sales Person to have a reason to conduct the interview Conversation openers Remarks about the Prospect

AIDAS Gaining Interest: Intensify the prospect's attention Searching the most effective selling appeal Questions to clarify attitudes and feelings towards the product Kindling Desire: Kindle the prospect's desire to Ready-to-buy point Conversation running along the main line towards the sale Taking care of External interruptions and Objection handling

AIDAS Inducing Actions: Closing the sales buy judging the prospects reaction Straightforwardly asking for the order vis-à-vis dropping the hints Building Satisfactions: Reassuring that the decision was right Customer to have an impression that salesperson merely helped in deciding

2"Right Set of Circumstances" Theory Everything was right for the sale Situation Response Theory Particular circumstance in a selling situation cause the prospect to respond in a particular way Salesperson needs to present PROPER STIMULI or APPEALS so that desired response is resulted Seller oriented Theory External Factors vis-à-vis Internal Factors Focus on the external factors at the expense of Internal Factors.

3 Maslow's Hierarchy/Psychologyin Selling

One of the foundational need theories in psychology is Maslow's Hierarchy of Needs. Abraham Maslow introduced his five levels of human need in a 1943 paper. He indicated that people have five basic needs, which they address in order of priority. Physiological needs are first, followed by safety and security, social belonging, self-esteem and self-actualization. This theory has huge value in selling in that salespeople get to know prospects and ask questions to discover their needs in a buying situation. Realizing where people are coming from on the Maslow pyramid is a part of a seller's emotional intelligence. For instance, car buyers may be most concerned with basic survival or security and want an economic, dependable vehicle. Others buy cars for social or esteem reasons.

4 **Buying Situation Theory** The buyer's needs or problems receive major attention, and the salesperson's role is to help the buyer to find solutions. This theory purports to answer the question: What thinking process goes on in the prospects's mind that causes the decision to buy or not to buy? The name "buying formula" was given to this theory by strong.

The theory is based on the fact that there is a need or a problem for which a solution must be found which would lead to purchase decision, as shown below:

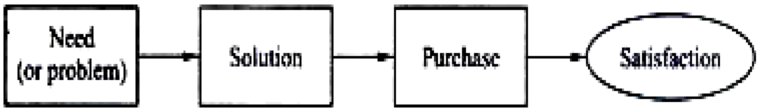


Fig. 21.1

Whenever an individual feels a need, he is said to be conscious of a deficiency of satisfaction. The solution will always be a product or service or both and they may belong to a producer or seller. The buyer develops interest in buying a solution.

In purchasing, the "solution" involves two parts:

1. Product or service or both,

2. The brand name, manufacturer or the salesperson of the particular brand name:

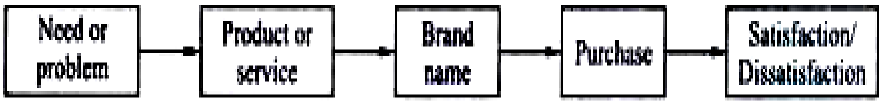


Fig. 21.2

The product or service (Brand name) must be considered adequate to satisfy the need and the buyer must experience a pleasant feeling or anticipated satisfaction. This ensure the purchase.

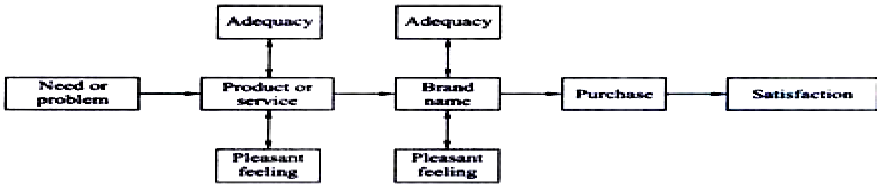


Fig. 21.3

Sales Forecasting

It is the process of estimating future **sales**. Accurate **sales forecasts** enable companies to make informed business decisions and predict short-term and long-term performance. Companies can base their **forecasts** on past **sales** data, industry-wide comparisons, and economic trends. It is easier for established companies to predict future sales based on years of past business data. Newly founded companies have to base their forecasts on less-verified information, such as market research and competitive intelligence to forecast their future business.

Sales forecasting gives insight into how a company should manage its workforce, cash flow, and resources. In addition to helping a company allocate its internal resources effectively, predictive sales data is important for businesses when looking to acquire investment capital.

Sales forecasting allows companies to:

- Predict achievable sales revenue;
- Efficiently allocate resources;
- Plan for future growth.

Sales Forecasting Methods

Modern Managers have several different methods available for Sales Forecasting.

Popular methods are:

1. **Jury of Executive Opinion Method**
2. **The Sales force Estimation Method**
3. **Time Series Analysis Method**

Jury of Executive Opinion Method:

In the Jury of executive opinion method of Sales Forecasting, appropriate managers within the organization assemble to discuss their opinions on what will happen to sales in the future.

Since these discussion sessions usually resolve around hunches or experienced guesses, the resulting forecast is a blend of informed opinions.

A similar, forecasting method, which has been developed recently is called the DELPHI Method. Delphi Method also gathers, evaluates, and summarizes expert opinions as the basis for a forecast, but the procedure is more formal than that for the jury of executive opinion method.

The **Delphi Method** has the following steps:

STEP 1 – Various Experts are asked to answer, independently and in writing, a series of questions about the future of sales or whatever other area is being forecasted.

STEP 2 – A summary of all the answers is then prepared. No expert knows, how any other expert answered the questions.

STEP 3 – Copies of summary are given to the individual experts with the request that they modify their original answers if they think it necessary.

STEP 4 – Another summary is made of these modifications, and copies again are distributed to the experts. This time, however, expert opinions that deviate significantly from the norm must be justified in writing.

STEP 5 – A third summary is made of the opinions and justifications, and copies are once again distributed to the experts. Justification in writing for all answers is now required.

STEP 6 – The forecast is generated from all of the opinions and justifications that arise from step

SALES FORCE ESTIMATION METHOD:

The Sales Force Method is a sales forecasting technique that predicts future sales by analyzing the opinions of sales people as a group. Salespeople continually interact with customers, and from this interaction they usually develop a knack for predicting future sales. As with the jury of executive opinion method, the resulting forecast normally is a blend of the informed views of the group. The sales force estimation method is considered very valuable management tool and is commonly used in business and industry throughout the world. This method can be further improved by providing sales people with sufficient time to forecast and offering incentives for accurate forecasts. Companies can make their sales people better forecasters, by training them to better interpret their interactions with the customers.

TIME SERIES ANALYSIS METHOD:

The time series analysis method predicts the future sales by analyzing the historical relationship between sales and time. Although the actual number of years included in a time series analysis will vary from company to company, as a general rule, managers should include as many years as possible to ensure that important sales trends do not get undetected.

Other complex sales forecasting methods include:

- Statistical Correlation Method
- Computer Simulation Method

Design and Management of Sales Territories

A sales territory consists of existing and potential customers, assigned to a salesperson A **sales territory** is the customer group or geographic district for which an individual salesperson or sales team holds responsibility. Territories can be defined on the basis of geography, sales potential, history, or a combination of factors. Companies strive to balance their territories because this can reduce costs and increase sales.

The purpose of a sales force coverage (or sales territory) metric is to create balanced sales territories. There are a number of ways to analyze territories. "Most commonly, territories are compared on the basis of their potential or size. This is an important exercise. If territories differ sharply or slip out of balance, sales personnel may be given too much or too little work. This can lead to under- or over-servicing of customers."

Operationally defined, a sales territory is a grouping of customers and prospects assigned to an individual salesperson. Many sales executives refer to sales territories as geographical areas. But, in contrast, in some companies particularly in which technical selling style is predominant, geographical considerations are ignored and sales personnel are assigned entire classes of customers, regardless of their locations. When sales personnel sell mainly to personal acquaintances, as in selling property, insurance, and investment securities; little logical base exists for dividing the market geographically.

REASONS FOR ESTABLISHING TERRITORIES

The primary reason for establishing sales territories is to facilitate the planning and controlling of the selling function.

(i) To obtain thorough coverage of the market: Sales territories help in proper market coverage. A salesperson's calling time is planned as efficiently as possible in order to ensure proper coverage of present as well as potential customers. Coverage is likely to be more thorough when each sales person is assigned to a properly designed sales territory rather than when all sales personnel are allowed to sell anywhere. With proper coverage of the territories, the company can more closely reach the sales potential of its markets.

(ii) To Establish Salesperson's Job and Responsibilities: Sales territories help in setting the tasks and responsibilities for the sales force. Salespeople have to act as business managers for their territories. They have the responsibility of maintaining and generating sales volume in their territories. Once all call frequencies are calculated and assigned, it is easier to determine the total wor1doad and then to break it down into equal assignments among salesmen. When an equitable workload is assigned on the basis of call frequencies, better results are obtained. An equitable workload assignment creates greater interest and enthusiasm among the salesmen

(iii) To evaluate sales performance: Sales territories help in the evaluation of sales performance of a company. Actual performance data can be collected, analyzed, and compared with expected performance goals. Even present sales figures can be compared with past figures to judge the performance over the years. Individual territory performance can also be compared to district performance, district performance compared to regional performance; and regional performance compared to the performance of the entire sales force.

(iv) To Improve Customer Relations: Properly designed sales territories allow sales people to spend more time with present and potential customers and less time on the road. Customer goodwill and increased sales can be expected when customers receive regular calls. Since the salesman's visits are decided under a call frequency schedule programme, he comes in contract with his customers on the basis of a regular schedule. Such regular contacts enable both the salesman and the customer to understand each other well and get their difficulties solved in respect of the supply of, and demand for, goods, and also raises the general reputation of the company which the salesman represent.

(v) To Reduce Sales Expenses: Sales territories are designed to avoid duplication of effort so that two or more salespersons are not travelling in the same geographical area. This lowers selling cost and increases company profits. Sales territories also result in such benefits as fewer travel miles and fewer

(vi) To co-ordinate selling with other marketing, functions: A welldesigned sales territory can aid management in performing other marketing functions. Sales and cost analyses can be done more easily on a territory basis than for the entire market. Marketing research on a territory basis can be used more effectively for setting quotas and establishing sales and expense budgets. If salespeople are to aid customers in launching advertising campaigns, distributing point of purchase displays, or performing work related to sales promotions, the results are usually more satisfactory when the work is assigned and managed on a territory-by-territory basis rather than for the market as a whole. overnight trips.

Benefits of Sales Territories

- Increase market / customer coverage
- Control selling expenses and time
- Enable better evaluation of sales force performance
- Improve customer relationships
- Increase sales force effectiveness
- Improve sales and profit performance

Unit-2

Sales Organisation

Sales organization consists of human beings or persons working together for the effective marketing of products manufactured by the firm or the products purchased for resale. Sales organization co-ordinates the efforts of members of a group to bring about a desirable result. It provides an efficient, economic and flexible administrative set up to ensure timely movement of products from the warehouse to the ultimate consumer. Thus it provides satisfactory job to buyers and sellers.

A sales organization has a number of departments. It has a planned and well co-ordinated structure. It performs the functions of planning, organizing and controlling marketing and distribution of products. Sales organization is a foundation for effective sales planning and sales policies. Systematic execution of plans and policies and programmes of a sales organization control all the sales activities. As such it ensures maximum efficiency and profitability without losing consumer service and satisfaction.

Importance of Sales Organisation:

1. Blood circulation of a human body keeps a man alive and in sound health. Similarly the sales strengthen the organisation. The more is the sales, the more is the profit.
2. Increasing sales means progress of the firm. If the sales fall down, it is fatal, because sales are the life blood of the business, as the blood is to a human body.
3. Consumers are the kings. Manufacturers produce goods for consumers. They must be satisfied in the market which is full of competitors with products for similar use. So suitable products are necessary, and for this an organisation is necessary.
4. To move the products from the factory to the consumers, the sales organisation is necessary— demand creation.

5. To handle the orders promptly i.e., from the stages of enquiry to order at full satisfaction to consumers.

6. Collection of dues is also important. Several drops make an ocean; at the same time milking cows should not be neglected.

7. To keep good public relations by redressing the complaints if any, and to create a good image of the firm.

Structure of the Sales Organisation:

The following factors are to be taken into consideration while designing the structure of a sales organisation:

1. Nature of the market
2. Sales policies of the enterprise
3. Nature of the product
4. Number of products
5. Availability of financial resources
6. Level of distribution system
7. Size of the company
8. Price of the product
9. Ability of the professionals
10. Position of competitors' Products.

SALES FORCE RECRUITMENT & SELECTION

Sources of sale force recruitment

Inside the company	**Outside the company**
	- Direct unsolicited applications
- Company Sales Personnel	- Employment Agencies
- Company Executives	- Salespeople making calls on
- Internal Transfers	The company

		- Employees of customers
		- Sales executive clubs
		- Sales Force of non-

Sales Force required = Sales potential/ Average contribution of a sales executive.

SALES FORCE RECRUITMENT AND SELECTION PROCESS

RECRUITMENT PROCESS

(a) Conducting a job analysis

(b) Preparing a job description

(c) Developing a set of job qualifications

(d) Attracting a pool of applicants

SELECTION PROCESS

(a) Initial screening interviews

(b) Application forms

(c) In-depth interviews

(d) Reference checks

(e) Physical examinations

(f) Tests

Execution and Evaluation of Sales force Training

Proper training can prepare salespeople to meet with customer expectations

New salespeople spend a few weeks to several months in training

Companies view sales training important for protecting their investments in their salesforce

Sales Training Process consists of:

- Assessing sales training needs
- Designing and executing sales training programs
- Evaluating and reinforcing sales training programs

- Assessing Sales Training needs
  - Sales training needs are assessed both for
    - Newly hired sales trainees, and
    - Experienced / existing salespeople
  - Methods used for assessing training needs are:
    - First level sales managers' observation
    - Survey of sales force and field sales managers
    - Customer survey
    - Performance testing of salespersons
    - Job description statements
    - Salesforce audit (as a part of marketing audit)
  - Objectives of sales training:
    - Increase sales, profits, or both
    - Increase sales productivity
    - Improve customer relations
    - Prepare new salespeople for assignment to territories
- Content of Training Programme
  - Content for new sales trainees is broader . It includes:
    - Company knowledge
    - Product knowledge
    - Customer knowledge
    - Competitor knowledge
    - Selling skills / sales techniques
  - Examples of specific content for experienced salespersons are:
    - New product knowledge
    - Introduce change in sales organisation
    - Negotiating skills
  - Content depends on the aims of training programme

SALES TRAINING METHODS

- Selection of suitable methods for a training programme depends upon the topic and audience
- Training methods are grouped into five categories:
  - Class room / Conference training

- Behavioural learning / Simulations
- Online training
- Absorption training
- On-the-job training

Briefly review of the training methods

1) CLASS-ROOM / CONFERENCE TRAINING GROUP

- The training methods in this group are: (1) lecture, (2) demonstration, and (3) group discussion

a) Lecture

Used when more information is presented in a short time to a large number of participants

May lead to boredom due to less active participation

b) Demonstration

Used for giving product knowledge

c) Group discussion

Useful when participants include experienced and inexperienced salespersons

A panel discussion consists of a small group of people who discuss a specific topic

2) BEHAVIOURAL LEARNING / SIMULATION GROUP

This group consists of three training methods: (1) role playing, (2) case-studies, and (3) business games

(3) Role playing

Useful method for teaching sales technique / process

Typically, one trainee plays the role of a salesperson and another trainee acts as a buyer

b) Case studies

a. Beneficial for understanding consumer behaviour, and building problem solving abilities

b. Case teaching includes open discussion, group discussion and presentation

c) Business games

a. Helpful in learning impact of decision making

b. Generates enthusiasm and competitive spirit

3) ONLINE TRAINING GROUP It includes:-

(a) Electronic performance support systems (EPSS),

(b) Interactive multimedia training,

(c) Distance learning

- It takes 50 percent less time and costs 30-60 percent less, and more convenient than other training methods
- Useful for getting basic knowledge like products and customers
- Electronic performance support system (EPSS) makes information available immediately, in a personalized manner
- Interactive media training is used for retraining salespeople who can repeat or skip material as desired
- Distance learning is a personal training method, which is interactive

4) ABSORPTION TRAINING / SELF STUDY GROUP

a. It includes supplying audio cassettes, product manuals, books, articles, and CD-ROMs to salespeople, who read (or absorb) these materials without feedback
b. Useful for introducing basic materials or strengthening previous training
c. On-the-Job Training Group
d. Most companies use this method as it places a sales trainee in a realistic sales situation
e. Typically, a junior salesperson is assigned to a senior salesperson for some period of time
f. In mentoring , a junior / new employee gets information, advise and support from mentors / experienced persons
g. Job rotation is used to groom salespeople for management positions

1. ORGANISATIONAL DECISIONS FOR SALES TRAINING

Organisational decisions, which are parts of designing sale training programme, are:

a. Who will be the trainees?
b. Who will conduct the training?
c. When should the training take place?
d. How long should the training be?
e. Where should the training be done?
f. What will be the budgeted expenditure for the training?

6) EXECUTION OF SALES TRAINING PROGRAMME

a. Usually sales trainer or sales training manager is responsible for entire process of sales training

b. Execution / implementation includes preparing time-table, arranging internal / external trainers, making travel arrangements of participants, arranging conference hall and teaching aids, and so on

c. A good practice to make a final check one / two days prior to start of training programme

d. Obtain feedback from the sales trainees at the end of the programme

REINFORCE SALES TRAINING

Behaviour of most salespeople would not change unless there is reinforcement to sales training

In many companies reinforcement or follow-up trainings are not done

a) **Training methods used for reinforcement are**:

i. Refresher training consists of continuous training to overcome deficiencies of experienced salespeople and retraining of salespeople whose job requirements have changed

ii. Web-based or online methods to reinforce formal training sessions

iii. Senior salespeople or first line sales managers coaching new salespersons

MOTIVATING THE SALESFORCE

(i) Motivation is derived from Latin word “ movere ”, which means “ to move ”

(ii) Motivation is the effort the salesperson makes to complete various activities of the sales job

(iii)10-15 percent salespeople are self-motivated

4) Majority of salespeople are not adequately motivated

5) Importance of motivating salespeople is recognised, because financial performance of the company depends upon the achievement of sales volume objective

SELECTING A MIX OF MOTIVATIONAL TOOLS

a) Sales manager should know each salesperson and understand his / her specific needs

b) For designing or selecting a mix of motivational tools, a compromise between differing needs of customers, salespeople, and the company management becomes necessary

c) Motivational tools are divided into (1) financial, and (2) non-financial . These are shown in the next slide

MOTIVATIONAL TOOLS IN A MOTIVATIONAL MIX

Financial Motivation Techniques:-

1) Salary
2) Commission/Incentive
3) Bonus
4) Combination
5) Sales contests
6) Benefits in kind ("fringe benefits")
7) Time-rate pay
8) Piece-rate pay
9) Commission
10) Shares and options
11) Pensions

Non-financial methods of motivation:-

1. Promotion
2. Sense of accomplishment
3. Personal growth opportunities
4. Recognition
5. Job security
6. Sales meetings
7. Sales training programmes
8. Job enrichment
9. Supervision
10. Financial compensation plan

COMPENSATION OF SALES PERSONNEL

A good compensation plan should consider objectives from the company's and salespeople's viewpoint

OBJECTIVES OF COMPENSATION PLAN FROM THE COMPANY'S VIEWPOINT

- To attract , retain , and motivate competent salespeople
- To control salespeople's activities
- To be competitive , yet economical : It is difficult to balance these two objectives
- To be flexible to adapt to new products, changing markets, and differing territory sales potentials
- Connect Individual with Organization
- Influence Work Behavior
- Organizational Choice
- Influence Satisfaction
- Feedback
- Reinforcement

OBJECTIVES OF COMPENSATION PLAN FROM SALESPERSON'S VIEWPOINT

To have both regular and incentive income

- Regular income by fixed salary to take care of living expenses
- Incentive income for above average performance To have a simple plan, for easy understanding
- This is in conflict with the objective of flexibility
- To have a fair payment plan
- Fair or just payment to all salespeople is ensured by selecting measurable and controllable factors

DESIGNING AN EFFECTIVE SALES COMPENSATION PLAN

Designing a new compensation plan or revising an existing plan consists of the following steps:

1) Examine job descriptions
2) Set up specific objectives for salespeople
3) Decide levels of pay / compensation
4) Develop the compensation mix
5) Decide indirect payment plan or fringe benefits
6) Pretest, administer, and evaluate the plan

DECIDE LEVELS OF PAY / COMPENSATION

- It means the average pay or money earned per year (or month)
- It is important to decide levels of pay for all sales positions
- It is decided based on the following factors :
- Levels of pay for similar positions in the industry
- Levels of pay for comparable jobs in the company
- Education, experience, and skills required to do sales job
- Cost of living in different metros and cities
- Annual average pay levels vary between industries, within the same industry, and sometimes within the company
- Firms decide a range of average pay , instead of a specific pay
- Salespeople earn pay depending on their and company performance

DEVELOP THE COMPENSATION MIX

- Widely used elements of compensation mix are: (1) salaries, (2) commissions, (3) bonuses, (4) fringe benefits (or perquisites)
- Expense allowances or reimbursements like travel, lodging, etc are not included
- Basic types of compensation plans are:

1. Straight salary
2. Straight commission
3. Combination of salary, commission, and / or bonus

- 68 percent companies use combination plan and balance 32 percent firms use straight salary or straight commission

1. Straight – Salary Plan

Characteristics:

100 percent compensation is salary, which is a fixed component No concern for sales performance or salesperson's efforts

This plan is suitable for sales trainees, missionary salespeople, and when a company wants to introduce a new product or enter a new territory

Advantages:Salespeople get secured income to cover living expenses

Salespeople willing to perform non-selling activities like payment collection, report writing

Simple to administer

Disadvantages:

No financial incentive to salespeople for more efforts and better performance. Hence, superior performance may not be achieved

May be a burden for new and loss-making firms

2. Straight – Commission (or Commission Only) Plan

Characteristics:

- It is opposite of straight-salary plan
- Most popular commission base is sales volume or profitability
- Commission rate is a percentage of sales or gross profit
- This plan is generally used by real estate, insurance, and direct-sales (or network marketing) industries

Advantages:

1. Strong financial incentive attracts high performance, removes ineffective salespeople and improves results
2. Controls selling costs and requires less supervision

Disadvantages:

1. Focus is on sales and not on customer relationship
2. Salespeople may pay less attention to non-selling activities

1. Combination Plan

Characteristics:

1. Combines straight salary & straight commission plan
2. Four types of combination plans used by companies:

a) Salary plus commission : suitable for getting improved sales and customer service

b) Salary plus bonus: a bonus is a lumpsum, single payment, for achieving short-term objectives. This plan is used for rewarding team performance

c) Salary plus commission plus bonus: suitable for increasing sales, controlling salesforce activities, and achieving short-term goals. Also suitable for selling seasonal products like fans

d) Commission plus bonus: Not popular. Used for team selling activities for selling to major customers

Advantages:

- Flexible to reward and control salesforce activities
- Security for living costs and incentives for superior performance for salespeople
- Rewards specific sales performance
- Different plans for different sales positions / jobs

Disadvantages:

- Complex and difficult to administer
- May not achieve objectives if not properly planned, implemented and understood
- Indirect payment plan , also called fringe benefits or perquisites, help in attracting and retaining people, but have now come under government tax in India

Sales Quotas

A sales quota is a quantitative goal assigned to a sales unit for a specific period of time. A sales unit may be a sales person, territory, 151 branch office, region or distributor. Sales quotas are used to plan, control and evaluate selling activities of a firm. As standards for appraising selling effectiveness, quotas specify desired performance levels for sales volume, expenses, gross margin, net profit, selling and non-selling activities, or some combination of these items. Sales quotas provide a source of motivation, a basis for incentive, compensation, standards for performance evaluation of sales person and uncover the strengths and weaknesses in the selling structure of the firm. Quotas are devices for directing and controlling sales operations. Their effectiveness depends upon the kind, amount, and accuracy of marketing information used in setting them, and upon management’s skills in administering the quota system. For effective results, quotas are designed on the basis of information derived from sales forecasts, studies of market and sales potentials, and cost estimates. Accurate data are important to the effectiveness of a quota system, but, they are not sufficient; judgment and administrative skills are required of those with quota setting responsibilities. Soundly administered quotas based on thorough market knowledge are effective devices for directing and controlling sales operations.

PURPOSE OF THE SALES QUOTA

(i) To provide standards for evaluating performance: Quotas provide a means for determining which sales personnel, territory, other units of sales organization, or distributive outlets are doing average, below average, or above average job. They are yardsticks for measuring sales performance. Comparisons of quotas with sales performance identify weak and strong points, but management must dig deeper to uncover reasons for variations.

(ii) To furnish goals and incentives for the sales force: Quotas provide salespersons, distributive outlets and others engaged in selling activities, goals and incentives to achieve certain performance level. Many companies use quotas to provide their sales force the incentives of increasing their compensation through commissions or bonus if the quota is surpassed and/or recognized for superior performance. Needless to say, to be true motivators, sales quota should be perceived as being realistic and attainable and to an extent surpassable.

(iii) To control salespeople's activities: Quotas provide an opportunity to direct and control the selling activities of sales persons. Sales persons are responsible for certain activities e.g. customer calls per day, calling on new accounts, giving a minimum number of demonstrations and realization of firm's account. If the sales people fail to attain these quotas, the company can take corrective action to rectify the mistake.

(iv) To evaluate the productivity of sales people: Quotas provide a yard-stick for measuring the general effectiveness of sales representatives. By comparing salespersons' actual results with set quotas the areas of activities are determined where the salesforce need help for improving productivity.

(v) To control selling expenses: Quotas are also designed to keep selling expenses within limits. Some companies reimburse sales expenses only upto a certain percentage of sales quota. Others tie expenses to the salesperson's compensation in order to curb wasteful expenditure. Expense quota helps companies to set profit quotas.

(vi) To make effective compensation plan: Quotas play an important role in the company's sales compensation plan. Some Indian companies follow the practice that their salespersons will get commission only when they exceed their assigned quotas. Companies may also use attainment of the quotas in full or in part as the basis for calculating the bonus. If the salesperson does not reach the minimum desired quota, he will not be entitled for any bonus.

(vii) To evaluate sales contests results: Sales quotas are used frequently in conjunction with sales contests. Companies mostly use 'performance against quota' as the main basis for giving away awards in sales contests. Sales contests are more powerful incentives if all participants feel they have a more or less equal chance of winning by basing awards on percentage of quota fulfillment which is a common denominator. Hence, it causes average salesperson to turn into above average performers.

TYPES OF QUOTAS

Differences in forecasting and budgeting procedures, management philosophy, selling problems, and executive judgment, as well as variations in quota-setting procedures, cause each firm to have somewhat unique quota. Ignoring small differences, however quotas fall into four categories:

(i) **Sales volume quota:** The most commonly used quotas are those based on sales volume. This type of quotas are set for an individual sales person, geographical areas, product lines or distributive outlet or for only one or more of these in combination. Sales volume quotas are also set to balance the sales of slow moving products and fast moving products or between various categories of customers per sales unit. The sales volume quota may be set in terms of units of product sales, or rupee sales or both on overall as well as productwise basis.

(ii) Financial or budget quotas: Financial or budget quotas are determined to attain desired net profit as well as to control the sales expenses incurred. In other words, it is set for various units in the sales organisation to control expenses, gross margin, or net profit. The intention in setting financial quota is to make it clear to sales personnel that this jobs consist something more than obtaining sales volume. It makes personnel more conscious that the company is in business to make a profit. Expense quotas emphasize keeping expenses in alignment with sales volume, thus indirectly controlling gross margin and net profit contribution. Gross margin or net profit quotas emphasize margin and profit contributions, thus indirectly controlling sales expenses.

(iii) Activity quotas: Good performance in competitive markets requires the salesforce to perform the sales as well as market development related activities. The latter activities have long term implications on the goodwill of the firm. To ensure that such important activities get performed, some companies set quotas for the salesforce in terms of various selling activities to be performed by them within a given period. Finally the company must set a target level of performance for the sales persons.

(iv) Combination Quotas: Depending upon the nature of product and market, selling tasks required to be performed as well as selling challenges facing the company, some companies find it useful to set quotas in combination of the two or three types discussed above. Rupee sales volume and net profit quotas or unit sales volume and activity quota in a combined manner are found in common use in a large number of consumer and industrial products companies in India.

CHARACTERISTICS OF A GOOD QUOTA SYSTEM

(i) Realistic attainability: If a quota is to spur the salesforce to maximum effort, the goal must be realistically attainable. If it is too far out of reach, the salespeople will lose their incentives.

(ii) Objective Accuracy: Regardless of what type of quota management uses, it should be related to potentials. Executive judgement is also required, but it should not be the sole factor in the decision.

(iii) Ease of understanding and administering: A quota must be easy for both management and the salesforce to understand. Also, the system should be economical to administer.

(iv) Flexibility: All quota systems need adequate flexibility. Particularly, if the quota period is as long as a year, management may have to make adjustments because of changes in market conditions.

(v) Fairness: A good quota system is perceived as fair to the people involved. The workload imposed by quotas should be the same for all sales people. However, this does not mean that quotas must be equal. Differences in potentials, competition, and ability of the salesforce do exist.

SALES CONTESTS

A special selling campaign offering incentives in the form of prizes or awards beyond the compensation plan called sales contest. The purpose of sales contests is to provide extra incentives to increase sales volume, to bring in more profitable sales volume, or to do both. Corresponding to Herzberg's motivation-hygiene theory; sales contests aim to fulfill individual needs for achievement and recognition-both motivational factors. In terms of Maslow's hierarchy of needs, sales contests aim to fulfill individual needs for esteem and self-actualization both higher-order needs. In addition, sales contests develop team spirit, boost morale by making jobs more interesting, and make personal selling efforts more productive.

OBJECTIVES OF SALES CONTESTS

Sales contests are aimed to accomplish the following objectives:

I. To obtain new customers.
II. To secure larger orders per sales call.
III. To push slow moving items, high-margin goods, or new products.
IV. To overcome a seasonal sales slump.
V. To sell a more profitable mix of products.
VI. To improve the performance of distributors' sales personnel.
VII. T o promote seasonal merchandise.
VIII. To obtain more product displays by dealers.
IX. To get reorders.
X To promote special deals to distributors, dealers, or both.

Contest prizes

There are four kinds of contest prizes: cash, merchandise, travel, and special honors or privileges. Cash and merchandise are the most common prizes. Many sales contests feature more than one kind of prize, for example, travel for large awards and merchandise for lesser awards. Some contests give participants the option of accepting one prize rather than another.

1. Cash: The cash as an incentive weakens as an individual's unfulfilled needs; which are pushed farther up in the need of hierarchy. Once basic physiological needs and safety and security needs are satisfied whatever potency money retains as an incentive relates to unfulfilled esteem and achievement needs. Non-cash prizes fill these needs better than cash. If the compensation plan provides sales personnel with sufficient income to meet basic physiological needs and safety and security needs, a cash prize is a weak incentive unless it is a substantial sum-say, 10 to 25 percent of an individual's regular annual income. A cash prize of Rs. 100 means little to most sales personnel, and they exert token efforts to win it. .Another objection to cash prizes is that winners mix them with other income, and thus have no permanent evidence of their achievements.
2. Merchandise: Merchandise is superior to cash in respects. Winners have permanent evidence of their .achievement. The merchandise prize is obtained at wholesale, so it represents a value larger than the equivalent cash. For the same total outlay, too, more merchandise prizes than cash awards can be offered; hence, the contest can have more winners. Merchandise prizes should be those items; which salespersons and their families desire. One way to sidestep this problem is to let winners select from a variety of offerings. From the psychological standpoint, people feel good when they are permitted to assert their individuality and take their choice. A number of merchandise incentive agencies, some of them providing a. complete sales contest planning service, specialize in finishing prizes. Agencies issue catalogs with prices stated in points rather than in money.
3. Travel: Travel awards are popular. Few things can be glamorized more effectively than a trip to a luxury resort or an exotic land. The lure of a trip of a lifetime is a strong incentive, especially for the person to escape the job's routine. Travel awards generally provide trips for winners and their spouses, this being advisable both to obtain the spouse's motivational support and to avoid the spouse's opposition to solo vacation trips by the salesperson.
4. Special honours or privileges: This award has many forms: a letter from a top executive recognizing the winner's superior performance, a loving cup, a special trip to a home office meeting, or membership in a special group or

dub has certain privileges. Winners, in addition, receive publicity through house organs and in home town newspapers. These awards provide strong incentives, as, for example, they do with life insurance salespersons that push to gain membership in the million-dollar club. Mainly firms employing sales personnel who are almost independent entrepreneurs use the special honor or privilege award. Such awards, however, are appropriate wherever management desires to strengthen group identity and build team spirit. This type of award appeals to the salesperson's belongingness and social relations needs, which, according to Maslow, an individual strives to satisfy after fulfilling basic physiological needs and safety and security needs. It also appeals to esteem and self-actualization

Evaluation of Sales Personnel

Four steps that control the sales force activities are

1. Establishing Performance Standards.
2. Recording Performances
3. Evaluating Performance Standards
4. Taking Action

- Comparing actual performance with standards:
- The most difficult step in sales force control is evaluation step- The comparing of actual performances with standards.
- The same standards cannot be applied to all Sales personnel.
- It is possible to take Territorial differences into account by setting individual performance standards for each territory.
- Evaluating performance of sales personnel requires judgment & deep understanding of market factors & conditions

SDM- UNIT III

OBJECTIVE OF MARKETING INTERMEDIARIES

Learning Objective

- How to formulate Channel Objectives
- To understand Linkage between Channel Design and Channel Objectives.
- How channel design differ from firm to firm?

In the last lesson we read about the marketing channel, here we will discuss what are the channel objectives.

Objectives of Marketing Intermediaries

1. FORMULATING THE CHANNEL OBJECTIVES

Formulation of channel objectives is the first step in designing a channel system. The objectives clarify what is sought to be achieved by having the channels. All firms seek to realise certain common objectives by having the channel. In addition, they may also have some specific objectives depending on their unique circumstances.

Channel Objectives will Decide Channel Design Channel objectives will determine the channel design the firm should adopt.

Objectives, Firms Commonly Seek from Channels

- Effective coverage of the target market.
- Efficient and cost-effective distribution.
- Ensuring that consumers incur minimum exertion in procuring the product.
- Helping the firm to carry on manufacturing uninterrupted, confident that the channels will take care of sales.
- Partnering the firm in financing and sub-distribution tasks.

We can take an example of Hindustan Lever to explain it better.

Lever lays down the objective that Lifebuoy should be available in more than 80 per the villages of India; its channel design takes shape in line with this objective. Similar is the case, when FACT, the fertiliser firm, lays down the objective that in the home market of any company, no farmer should have to travel more than 3 km to buy its products.

We can take this forward a little more and state that marketing objectives determine channel objectives, and the latter determine the channel design. Usually, with the channel objectives, the broad contours of the channel design also get fixed. In the Lifebuoy example, given the channel objective to cover 80 per cent of the villages, the channel design has to naturally ensure a very intensive network of dealers spread through every nook and comer of rural India. As a corollary, a multi-tier channel, consisting of C&F agents, re-distribution stockists, retailers,

and village-level shops, will have to be the choice. In fact, HLL uses almost every village shop to sell Lifebuoy.

Above chart gives several illustrations of the linkage between channel objectives channel design. It will be clear from the chart that the channel design/ channel strategy of a firm flows directly from its channel objectives.

In the case of Castrol, for example (cited in the chart), engine oil is a convenience good and a medium involvement product.

Castrol knows that if a customer does not find engine oil at a given outlet, he may switch to another brand. Castrol accord- ingly stresses ‘reach and ‘speedy delivery’ in its channel strategy. And, once these two factors are set as the main channel objectives, it automatically leads to the channel design, which Castrol has adopted.

CHANNEL OBJECTIVES DIFFER FROM FIRM TO FIRM; CONSEQUENTL Y, THEIR CHANNEL DESIGNS DIFFER

We see that often channel designs of firms differ from one another. Even within a given industry; different firms have different channel designs. This is so because their channel objectives differ. Even in respect of those objectives, which are by and large common for all firms, we can see variations in emphasis from firm to firm. For example, intensity of market coverage sought from the channels and extent of convenience to be provided to the customer will vary from firm to firm. The weightages will flow from the marketing objectives of the respective firms.

The textile industry example: National Textile Corporation (NTC), Reliance Industries, Bombay Dyeing, DCM and Mafatlal are all textile firms and all of them operate in the same market. Yet, their channel designs vary from one another. This is so because their channel marketing objectives differ from one another. NTC's objective is to cater to the lower middle class, with textiles of reasonable quality at reasonable prices. It goes in Points to Ponder for a channel design, which is appropriate for this objective. At urban segments is the objective of Reliance. Premium product and premium price are the implications here. Evidently, the char

has gone in for a chain of exclusive Vimal showrooms. Though NTC has also set up some showrooms, it relies mainly on conventional trade. Reliance has set up 2,000 odd showrooms, covering all metros and Class I towns of India; it has located them in the shopping areas of the concerned towns; it has fabulously displayed its fabrics in these showrooms; the showroom is one main strategic strength of the company; Firms like Bombay Dyeing and DCM fall somewhere on the line between the positions taken by NTC and Reliance at the two ends. All these firms have obviously selected their channel design, based on their respective channel objectives.

Intensity Level	Objective	Number of intermediaries
Intensive	Achieve mass market selling. Convenience goods	Many
Selective		Several
		One

Conclusion

We have understood the channel objectives, how it is framed. The channel design depends upon objectives and it differs from firm to firm.

FUNCTION OF MARKETING CHANNEL

Learning Objective

- To understand distribution functions.
- Functions performed by Marketing channel.

In this lesson we will study the functions of marketing channel.

What is the Work of the Marketing Channel?

The work of the channel includes the performance of several marketing flows. We use the term flows rather than functions or activities to emphasize that these processes often flow through the channel, being done at different points in time by different channel members. In institutional settings, one often hears of the need to carry inventory; to generate demand through selling activities; to physically distribute product; to engage in after-sales service; and to extend credit to other channel members or to end-users.

Important flow that permeates all the value-added activities of the channel: the flow of information. Information can and does flow between every possible pair of channel members, in both routine and specialized ways. Retailers share information with their manufacturing suppliers about sales trends and patterns through electronic data interchange relationships; when

used properly, this information can help better manage the costs of performing many of the classic flows (e.g., by improving sales forecasts, the channel can reduce total costs of physical possession through lower inventory holdings). So important is the information content that logistics managers call this the ability to “transform inventory into information.” Manufactur- ers share product and salesmanship information with their distributors, independent sales representatives, and retailers, to improve the performance of the promotion flow by these intermediaries. Consumers can give preference information to the channel, improving the channel’s ability to supply valued services. Clearly, producing and managing information well is at the core of developing distribution channel excellence.

In addition, not every channel member need participate in every flow. Indeed, specialization in the performance of channel flows is the hallmark of an efficiently operating channel. For example, a channel in which physical possession of product moves from the manufacturer to wholesalers to retailers and finally to end- users. But an alternate channel might involve not stocking wholesalers, but instead manufacturer's representatives, who generally do not participate in the physical possession or ownership flows because they do not handle physical product. In such a case, the physical possession flow might be performed by the manufacturer and retailer, but not by other intermediar- ies, on its way to the final end-user.

Similarly, financing may be spun off to a specialist and not be done by other channel members to any great degree. For example, the mission of Maruti Finance, a wholly owned subsidiary of Maruti Udyog a car maker, is to finance not only ultimate consumers of its automobiles but also the inventories held by dealers. It has worked to cement its key role as financing agent both by introducing innovations such as the 10-minute credit review. As long as Maruti Finance can handle the financing flow at lower cost than other channel members can, others (e.g., dealers) do not need to help consumers finance their automo- bile purchases.

In general, flows should be shared only among those channel members who can add value or reduce cost by bearing them. However, specialization increases interdependencies in channels, and thus creates the need for close cooperation and coordina- tion in channel operations.

It is also important to note that the performance of certain flows is correlated with that of other flows. For instance, any time inventories are held by one member of the channel system, a financing operation is also underway. Thus, when a

wholesaler or retailer takes title and assumes physical possession of a portion of a manufacturer's out-put, the intermediary is financing the manufacturer. This is consistent with the fact that the largest component of carrying cost is the cost of capital tied up when inventories are held in a dormant state that is, not moving toward final sale. Other carrying costs are obsolescence, depreciation, pilferage, breakage, storage, insurance, and taxes. If that intermediary did not have to tie up its funds in inventory holding costs, it would instead be able to invest in other profitable opportunities. Capital costs are thus the opportunity costs of holding inventory.

Channel Perform Many Vital Distribution Functions

- Provide Distribution Efficiency
- Provide Salesmanship
- Help in Price Mechanism
- Look After a Part of Physical Distribution and Financing
- Provide Market Intelligence
- Assist in Merchandising
- Provide Market Intelligence
- Act as Change Agents and Generate Demand
- Take Care of the Flows Involved in Distribution

PROVIDE DISTRIBUTION EFFICIENCY

In the first place, the channels bring together the manufacturer and the user in an economic manner and thereby provide distribution efficiency to the manufacturer.

Minimize the number of contacts needed for reaching consumers: In most cases, it will be impractical for a manufac- turing firm to sell its entire production directly to the consumers. Resource constraint is the first hurdle in this regard. Even assuming that the required resources can be found, the question arises whether it will be advantageous for the firm to sell its products directly and all by itself, totally avoiding external. Marketing channels analysis shows that in most cases, using external marketing channels/ intermediaries is more advantageous to the firm than performing the distribution function all by itself. When channels are dispensed with, the number of contacts a manufacturer will have to establish for reaching out to the consumers are far too many; Channels minimise the number of contacts.

Break the bulk and cater to tiny requirements: Channels break the bulk and meet the small-size needs of individual consumers.

Supply products in suitable assortments: Channels also combine products and components manufactured by different firms and offer them in assortments that are convenient to users. The users normally need an assortment of items. They will shop at only those outlets, which supply such assortments. But, a manufacturer cannot meet the need for such assortments, since it will not be feasible for him to take up distribution of other products required by the customers. The channels thus render the vital service of assembling the products of different manufacturers and offering them to customers in suitable assortments. In other words, the channels help in 'matching segments of supply with segments of demand'.

PROVIDE SALESMANSHIP

Marketing channels also provide salesmanship. In particular, they help in introducing and establishing new products in the market. In many cases, buyers go by the recommendations of the dealers. The dealers establish the products in the market through their persuasive selling and person-to-person commu- nication. They also provide pre-sale and after-sale service to the buyers.

HELP IN PRICE MECHANISM

In many cases, the channels also help implement the price mechanism. They conduct price negotiations with buyers on behalf of the principals and assist in arriving at the right price- the price that is acceptable to the maker as well as the user. This is vital for the consummation of the marketing process. The manufacturer would find it difficult to complete this step without the help of the channels.

LOOK AFTER A PART OF PHYSICAL DISTRIBUTION AND FINANCING

Channels also look after a part of the physical distribution functions like transportation, handling, warehousing, sub- distribution, order processing and inventory management. Channels also share the financial burden of the manufacturer by financing the goods flowing through the marketing pipeline.

Often, they pay cash and lift the products; in the process, the manufacturer gets his money long before the products reach the ultimate users. In some cases, the channels provide substantive deposits to the principals. In several cases, the channels also extend credit to the subordinate levels in the channel and to the consumers. This also relieves the principals' financial strain to an extent. More than everything else, the channels place the products close to potential consumers and thereby enhance the chance of its sale.

ASSIST IN MERCHANDISING

Merchandising is another important function performed by marketing channels. Through merchandising, they help reinforce the awareness about the product among customers. When a customer visits a retail shop, his attention can be allured by an attractive display of the product brand increasing his awareness and interest. Merchandising, especially display complements the selling efforts of the company and acts as a silent salesman at the retail outlet.

PROVIDE MARKET INTELLIGENCE

Channels provide market intelligence and feedback to the principal. In the nature of things, channels are in a good position to perform this task, since they are in constant and direct contact with the customers. They feel the pulse of the market all the time.

ACT AS CHANGE AGENTS AND GENERATE DEMAND

In certain cases, the marketing task involves diffusion of some innovation among consumers. In such cases, the channels go much beyond the conventional functions of distribution aid act as 'change agents' among consumers and generate demand for the product.

TAKE CARE OF THE FLOWS INVOLVED IN DISTRIBUTION

The distribution process can be viewed as a series of flows: the physical flow of products, the title/ ownership flow, risk flow, the negotiation flow, the financing/ payment flow, the informa- tion flow and promotion flow. Marketing channels handle and take care of all these flows.

Some of these flows are forward, some backward and the others take place as a two-way process. Normally, the flow takes place sequentially through different levels in the distribution chain. In some cases, however, the flow may bypass a particular level in the chain.

Channels Acquire Their Importance by Their Functions

The foregoing elaborations not only explain the importance of marketing channels, but also clarify the fact that the channels acquire their importance by virtue of the functions they perform.

CHANNEL FUNCTIONS CANNOT BE ELIMINATED

Sometimes, firms tend to think that channels could be easily dispensed with and that the firm would be better off doing so. The firms assume that by eliminating the channels, they can eliminate the channel costs, this is erroneous thinking. The inherent assumption in this thinking is that by eliminating the channels, they can escape the functions that the channels perform. The fact is that even where channels are eliminated, the channel functions as such are not eliminated; they are merely transferred from the channels to the manufacturer; and the costs thereof are also just transferred, not eliminated.

Sometimes, the firms assume that while channels as a whole cannot be eliminated, a particular tier in the channel can be readily eliminated and the firm would be ipso facto better off with such elimination. Here too, if the assumption is based on the logic that with the elimination of the particular tier, the functions performed by that tier can be eliminated, then the firm will soon realise that it has committed a mistake. For here too, the alternative arrangement may not eliminate the functions performed by that particular tier. What is likely to happen is a transfer of the functions from the given tier to another one in the channel, backward or forward. So, it will be wrong to assume that the elimination of the tier will *ipso facto* result in savings to the firm. It depends on the circumstances.

Channels/ middlemen are no parasites: The problem arises due to a confusion in thinking. The firms concerned might be viewing channels as mere 'middlemen', with a negative connota- tion attached to the term. And, they might consider the channels as parasites. No wonder then, they think that they would be better off by dispensing with the channel, in part or full. It needs to be emphasised that channels/ middlemen are no parasites. They are an essential and valuable part of the firm's marketing activity. Manufacturers use them as there is economic sense in doing so, and all things considered, using them improves distribution efficiency.

This is not to suggest that under no circumstances can a tier in the channel be eliminated and that there would be no advantage at all in doing so. In some cases, it certainly is sensible to eliminate one particular tier in the channel and the firm might be better off doing so. It has to be conceded that there are always alternative methods of performing a set of channel functions and a firm may be better off by following one method in preference to another. But, it depends on the circumstances of the case. The firm has to analyse and find out whether the concerned distribution functions are performed more cost-effectively by eliminating the tier and shifting the functions backward or forward to another tier in the channel, or by keeping the tier alive. As a general rule, it can be said that where the number of tiers are far too many, the elimination of a tier would be advantageous.

The test question: The test question is: Are the functions duplicated in a wasteful manner? Sometimes, duplication of channel functions does take place in a channel system; the same function being performed by more than one tier. Firms often presume that in such cases, it is beneficial to dispense with one of the tiers. This is again incorrect thinking. Duplication of functions by different tiers need not automatically imply inefficiency, or waste. In many cases, such duplication may be essential for achieving the desired service level in distribution. For example, inventories may have to be kept at different levels/ tiers of the channel so that the flow of products is smooth and customers get the products at the time and place of their choice. In such cases, duplication is essential and beneficial. 'The firm, therefore, has to find out whether

duplication is wasteful. If it serves the interests of the firm, it is not wasteful. So based on the facts of the case, the firm should find out how costs are reduced, efficiency increased and waste eliminated.

CHANNEL DECISIONS HAVE A BEARING ON OTHER MARKETING DECISIONS

The decisions on channel have a vital bearing on other decisions relating to marketing. Pricing decisions, for example, are related to the channel pattern adopted by the firm and the compensa- tion paid to the channel. Similarly, decisions on sales force, its size, type, etc., depend on the nature and size of the marketing channel adopted. The channel pattern influences the pattern of salesmen's operations. It also determines to a significant measure the size and complexity of the marketing department of the firm.

Channel decisions usually bind the firm with long-term commitments. The channel types and the number of levels/ tiers in the channel cannot be changed every now and then. For example, once a firm has developed a marketing channel of its own, with company's own stock points performing the wholesaling/ semi-wholesaling task, and dependence on external channel limited to retailing activity alone, it cannot all of a sudden switch to a sole-selling agent system or even a wholesaler-retailer system. Having invested heavily in company's own stock points/ depots, the firm cannot suddenly extricate itself from the commitments already made. Basically; once a firm adopts a particular channel model and goes along with it for some time, exiting the model will be difficult.

Channel 'Levels', Channel 'Members', and Channel 'Length'

All marketing intermediaries do not operate at the same tier; they operate at different tiers. Each distinctive tier of intermedi- aries is referred to as a 'level' in the channel; and each link is referred to as a 'channel member'. The number of 'levels' determines the 'length' of the channel; the more the levels, longer is the channel. The number of 'members' does not deter- . mine the 'length' of the channel.

Conclusion

We have discussed that channels perform many vital distribu- tion functions. They Provide Distribution Efficiency by

bringing together manufacturer and user, Provide Salesmanship, Help in Price Mechanism, Look After a Part of Physical Distribution and Financing, Provide Market Intelligence, Assist in Merchandising by creating awareness about the product among customers, Provide Market Intelligence as they are in contact with the customers, Take Care of the Flows Involved in Distribution, Act as Change Agents and Generate Demand.

The channel functions cannot be eliminated, though intermedi- ary can be eliminated. For example wholesaler can be eliminated but functions will have to be transferred to a retailer.

RETAILING AND WHOLESALING

RETAILING

Retailing can be most simplistically defined as 'selling directly to consumers'. It is the sale of goods or commodities in small quantities directly to consumers. A more formal definition of retailing is as follows: **Retailing is the set of activities that markets products (or services) to final consumers for their own personal or household use. It does this by organizing their availability on a relatively large scale and supplying them to consumers on a relatively small scale.**

The word "Retail" originates from a French-Italian word 'retailer' which means someone who cuts off or sheds a small piece from something. Retailer is a Person or Agent or Agency or Company or Organization who is instrumental in reaching the Goods or Merchandise or Services to the End User or Ultimate Consumer.

Retailing – History and Indian Perspective

Retailing in India can be traced back to the times of ancient civilisations. Historical evidence shows the existence of shops where people used to collect things that they required in exchange of other goods and also money as prevailing in those times. Retailing as an occupation came into existence when farmers started producing more food than they required. Trading was an important part of daily life in the ancient world. The existence of the current *kirana* format and other shops can be traced to 'Manusmriti' and Kautiya's 'Arthashastra'. Indian history and archaeology record the existence of markets during the Harappan civilization as well. The ancient shops gradually took the shapes of stores owned and managed by a trader and his family what is popularly called mom-n-pop stores. The new retail formats that are now seen in India have their genesis in Europe. The earliest traders are believed to be the Cretans. Their culture influenced many other great trading civilizations including India. The Phoenicians followed the Cretans as civilisation's major traders. Then came the Romans, who set up numerous small shops. In fact ancient ruins indicate the world's first department store was in Rome.

The emergence of retailing in India has more to do with the increased purchasing power of buyers, especially post- liberalization, increase in product variety, and increase in economies of scale, with the aid of modern supply and distributions solution. We must appreciate that Indian consumers are still learning to deal with Organised Retail and it shows in the fact that as much as 94% of India's retail sales still comes from unorganized sector. On one side where Indian consumers are still learning to deal with Organised Retail, the work force too is yet to learn the ropes of this wonder. And that shows in the kind of shopping experience available in the stores. But, in its more than a century old history, Organised Retail has proved that it is the ultimate 'clearing house' of 'demand-n-supply', mother of the concept of 'marketing' and more and it will not be long before India also catches on with the rest of the world. Among 30 emerging markets, India has become the number one hotspot for global retailers for the fourth time in five years. Global consulting firm A T Kearney's eighth Annual Global Retail Development Index (GRDI) ranks India first in terms of attractiveness as a retail destination, followed by Russia and China.

Retail Strategies

Competitive Environment: Behavior of Consumers, Competition, Supply Chain Members				
Strategic Planning			Operations Mgmnt	High-Profit Retailing
Mission	Goals and Objectives	SWOT Strengths Weaknesses Opportunities Threa	Retail Marketing Strategy Target Markets Locations Retail Mix Merchandise Pricing Advertising & Promotion Customer Services & Selling Store Layout & Design	Buying & Handling Merchandise Pricing Advertising and Promotion Customer Services & Selling Facilities People

t
s

Social and Legal Environment:
Socioeconomic Environment, State of Technology, Legal System, Ethical Behavior

Retail Strategic Planning and Operations Management Model

Strategic planning involves adapting the resources of the firm to the opportunities and threats of an ever- changing retail environment. Through the proper use of strategic planning, retailers achieve and maintain a balance between resources available and opportunities. Strategic planning consists of four components:

1. Development of a mission statement (or purpose) for the firm
2. Definition of specific goals and objectives for the firm
3. SWOT Analysis
4. Development of basic strategies that will enable the firm to reach its objectives and fulfil its mission.

Retail Store Location

In deciding a store location, decision needs to be taken on two broad issues: i. the current and future potential of the catchment area of the store and ii. the exact site of the store. The process could consist of the following steps: 1. Evaluate alternate geographic areas in terms of the potential characteristics of residents, offices, commercial settlements, and existing retailers,

2. Determine what type of site is desirable from the three basic locational formats: isolated, unplanned district, or planned centre,
3. Select the general location of the store and
4. Evaluate the specific alternative store sites.

In order to reach the large population spread over a vast geographical area, India has developed a complex retailing institutional structure. Retail trade is predominantly in the hands of private independent owners and the distribution structure for fast moving consumer goods consists of multiple layers such as carrying and forwarding agents, distributors, stockists, wholesalers and retailers.

The retailing system in modern India operates at three parallel levels:

The Formal Sector: Traditional small retail shops and the newer forms of retail establishments that have ongoing businesses and fixed premises registered with the appropriate Government agencies.

The Informal Sector: Enterprises without fixed premises and includes the hawkers and vendors.

The Fair Price Shops: Mostly privately owned, but, business carried under the Government's public distribution system.

Retail Formats

Once a retailer identifies its target market, it must identify the most effective way to reach this market. Two basic retail formats that can be used to reach target markets are: store-based and non-store-based retailers. Store based retailers operate from a fixed store location that requires that customers travel to the store to view and select merchandise. Non-store-based retailers reach the customer at home, at work, or at a place other than a store where they might be open for purchasing.

Retail Formats

Store-Based

↓

Freestanding Business District Shopping Centers/Malls Nontraditional

Non-Store-Based

↓ Street Peddling Direct Selling Mail Order Internet Automated Merchandising Machines

The retail format is the store package that the retailer presents to the customer. Retail formats can be defined according to different attributes like: Location, Size, Merchandise, Price, and Atmosphere and service.

Store-based Classification

General Stores: Old-fashioned, with low levels of self-service.

Variety Stores: Have mixed merchandise, wide assortment but limited depth.

Supermarkets: Self-service food store offering mostly groceries as well as some clothing and home wares and general merchandise.

Department Stores: Known for its large assortment and service. The goods and services are organised into separate departments. Comprehensive service for quality value shopping.

Hypermarkets or Superstores: Stores that unite supermarket and general merchandise sales in one store. Provide a range of shopping requirements under one umbrella.

Ownership-Based Classification

Independents: An independent retailer owns a single retail unit.

Chains: A chain retailer operates multiple store units (outlets) under a common ownership & name. **Franchising:** Involves a contractual agreement that allows the franchisee to operate a retail outlet using the name and format of the franchiser.

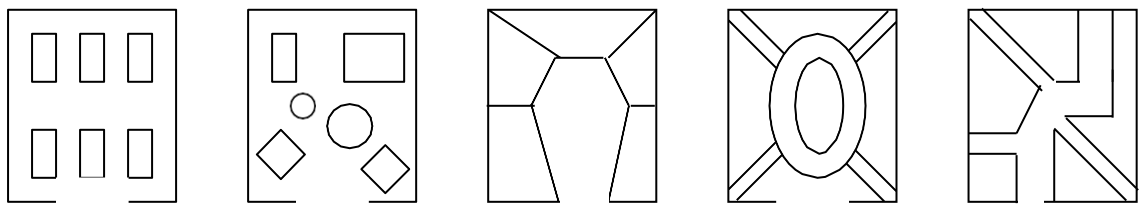
Stores Layout

Store layout is the way merchandise is laid out for inspection and accessed by consumers. It has two significant effects on the customer behaviour and buying activity. 1. It determines the appearance of the store and 2. It limits the way in which customers may negotiate their way around the store, which affects customer traffic flow or circulation.

The starting point of developing a floor plan is analysing how the available store space should be allocated to various departments. There are five basic types of **space needs** in a store: 1. Backroom, 2. Office and other functional spaces, 3. Aisles, service areas, and other non-selling areas of the main sales floor, 4. Wall merchandise space, and 5. Floor merchandise space.

A number of factors need to be kept in mind while deciding on the layout of a store. Every variable within the store sends out some kind of message to the customer. Some basic **elements of store layout** are: Planning and circulation, storefronts and entrances, merchandising, materials and finishes, lighting and music, and graphics and signage. Certain types of stores layout have evolved over time and continue to be the basis for most store layouts. Some common store lay out models are the grid, free flow, boutique, loop and spine (s-shaped).

Grid Free Flow Boutique Loop Spine (s-shaped)



Visual Merchandising Techniques

As competition has grown and stores try to squeeze more sales out of existing square footage, retailers have been increasing their emphasis on merchandise presentation. There are two basic types of merchandise presentation: on-shelf merchandising and visual merchandising. On-shelf merchandising describes the merchandise that is displayed on and in counters, racks, shelves, and fixtures throughout the store. This is the merchandise that the shopper actually touches, tries on, examines, reads, understands, and hopefully buys. Retailers can choose from a large array of fixtures and hard wares. There are essentially six methods of on-shelf merchandising: Shelving, Hanging, Pegging, Folding, Stacking and Dumping.

The second type of merchandise presentation, visual merchandising, is the artistic display of merchandise and theatrical props used as scene-setting decoration in the store. Visual displays are not typically associated with a shopable fixture, but are located in a focal point, feature area, or other area remote from the on-shelf merchandising and perhaps even out of reach of customers. Their goal is to create a feeling in the store conductive to buying merchandise. Visual merchandising uses various displays to increase consumer interest in and desire for the products offered for sale.

Props and elements in addition to merchandise are used in visual merchandising. Visuals may not include merchandise – they may be interesting displays of items somehow related to the merchandise or to a mood the retailer wishes to create. To be most effective, however, visuals should incorporate relevant merchandise. In apparel retailing, for instance, mannequins or figure forms are used to display merchandise as it might appear on a person.

There are a number of other aspects that form part of the atmosphere of the store and contribute to its image. These include signage, lighting, colours, music and scent as they can be used to control the customer.

MERCHANDISING

Stages of Merchandising

Merchandising is necessary for most types of products and services. The term merchandising is used to describe many aspects of the planning and presenting of stock. It also refers to the intermediate stages, which the products pass through from the original source to the end consumer. These stages are: *Planning, sourcing, buying, arranging, displaying* and *space management* of products or services. Merchandising is not just about laying out items on shelves; it is also concerned with the planning, sourcing, buying and arranging of these products and services. It is the coordination of these and other functions that make for a successful retail business.

Planning retail ranges involves careful consideration of the customer, competitors and the type of retail business, that is, discount/upscale, high priced/low priced. Retailers plan for the types of goods they wish to sell to their customers. This requires thinking about the image of the retail business and the requirements of the customer.

It is useful to think of merchandise fitting into four groups or categories. Merchandise characteristics can be classified into: impulse, convenience, shopping and speciality. There is, however, a more functional side of planning, which involves obtaining regular supplies of merchandise from suppliers. This involves making decisions about selection, turnover, replenishment of stock and relationships with suppliers.

Sourcing is the locating and purchasing of merchandise to sell in the store. An apparel retailer will source catwalk fashions from low-cost sources to enable them to sell at high street prices. Sourcing is all about obtaining the merchandise we wish to sell at the right price, quantity, and quality in a timely manner. Stages in the sourcing process are:

- The retailer has a need for a product
- The need is clearly defined
- The product specifications are agreed
- A suitable supplier is found

The retailer then agrees on *quantity, date of delivery, target price, packaging weight and volume*, *mode of transportation* and *payment terms*. Once all the terms and agreements are clearly established, the retailer is then able to find the best product at the most competitive price. Depending on the type of merchandise, a sourcing agreement may be given to a third party who has the resources to solve the purchasing and logistics problems. This is called a full sourcing package or FSP agreement. Such agreements include the details of delivery such as timing and frequency. The company that handles the FSP will arrange and schedule the transportation details and date of delivery.

Buying involves negotiation and a step-buy-step buying process. Every retailer has to buy stock an a managed and cost-effective manner. Most large retail firms have dedicated buying departments or systems. Small independent retailers rely on wholesalers or buying co-operatives to provide a suitable selection of merchandise. Buyers have significant influence over the following factors:

Sales volume: merchandise in the right quantity and at the right time in the right place.

Gross margins: the cost of the merchandise, the extent of the mark-up, and the price paid by the consumer.

Markdowns: buyers influence markdowns as they regulate the quantity, price, purchase period and the type of merchandise ordered.

Stock levels: buyers balance stock levels to achieve high sales with low inventory.

<u>Steps in the Buying Process</u>

Product Information → Identify Possible Suppliers → Negotiate with Preferred Suppliers → Ordering

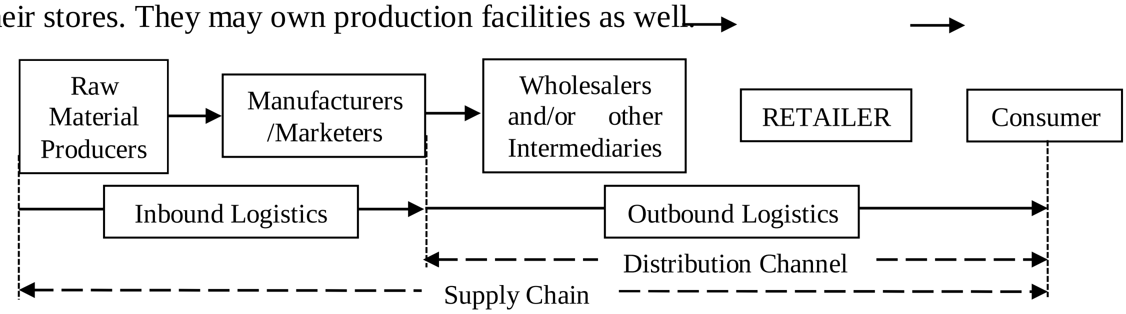
The steps in the buying process show the importance of research, and the acquisition of data about the suppliers, products and sources. The buyer will first attempt to locate the right sort of product information, with knowledge of potential suppliers and good contacts in the industry. Other sources of information inside the retail organisation are sales histories, customer comments and returns, and store market research.

Arranging and **displays** can have a major affect on sales. Customers reasonably expect displays of merchandise to be exciting and enticing. At certain times of the year, for example, Christmas and sale time, display is more critical than others. The way the merchandise is laid out in a store is also critical. For example, the placing of likely accessories next to clothing items in a women's fashion store or laying out perishable foods in a supermarket.

Space management is planning for space allocation and may require the use of computer-based planning models. Space management is concerned with placing merchandise within the store in the most profitable manner. The most significant factor in planning merchandise layout is that space varies in value. Some parts of the store are more valuable because customers visit them more frequently. Space closest to the entrances and exits is the most valuable and values decrease further into the store. Height from the ground also affects value. As a general rule, it is best to locate the highest profit generator in prime locations in order to maximise space productivity. There are several methods of planning the amount of space a store, department or product range requires. These may be by one or a mixture of the following: Historical sales, Contribution to profit, Gross margin, or Industry average.

Supply Chain and Retailing

The Retailer is a part of the Supply Chain for any product that it sells. The supply chain consists of different stages; starting with the raw materials it links raw material producers, manufacturers, wholesalers and transport firms with the retailer and the final consumer. The retailer comes at the end of the supply chain and provides the final link between the producer and consumer. Much of modern retailing, however, is linked very closely to whole supply chain, and may even be the dominant part of the supply process. Major grocery retailers play a very active role in arranging distribution of products to their stores. They may own production facilities as well.



Competition for shelf space and limitations of small retail shops to carry a large assortment of products paved way for the entry of the new organized retail stores in the Indian retail scenario. Walk-in retail stores are the latest trend in Indian cities and towns these days. In these new walk-in retail stores consumers have the liberty to walk around the stores sometimes pushing a cart or carrying a basket, browse the goods displayed on neatly arranged shelves, independently take down goods from the shelves to read the information provided on the packages, make a purchase decision and check out by paying at the cash counters. In this set up, consumers, more often than not, discover new products and brands and finally end up buying more than what they had entered the store for.

Wholesaling

This includes all the activities involved in selling goods and services to those who buy for resale purpose. They are the marketing intermediaries that buy from one source and sell it to another. The main function of a wholesaler is facilitatin g the transportation of the product and at times in the transfer of the titles. The intermediaries' performing the wholesaling function is principally divided into two types namely merchants and agents.

Meaning:

Wholesaling is defined as the activities in volved in selling to organizational buyers who intend either resell or use of their own purposes.

Classification of wholesaling:

1.CLASSIFICATION OF MERCHANT WHOLESALERS:

The merchant wholesalers are independently owned concerns that take title to the goods they distribute. Some of the merchant wholesalers operate at the national level while some of them are more into regional levels. The merchant wholesalers are classified in terms of the number and the types of service they provide to the customer. The major division of the merchant wholesalers is termed as the Full-service merchant wholesaler and Limited – service merchant wholesaler.

2. Full-service merchant wholesaler:

It provides customers with a complete array of services in addition to the mercha ndise they offer. The service may include delivery, credit facility, advice and even assistance as accountant aid. The se people are also called as full-function wholesalers. The full-service wholesalers are further classified into three types by the line o f the goods they offer.

- General Merchandise Wholesalers are those who sell large number of different product types or lines. It would be a one stop shop for the retailers to procure things from them at a much bargain able prices
- General Line Wholesalers are those who limit their offerings to one particular product line. They may hold all the products and variants in one particular product line.
- Specialist Wholesaler reduce the line further, they may hold only select products in a particular product line. The traders of spices can be classified under this category The choice of being a more general merchant wholesaler or a much-specialized wholesaler depends on the choice of the target customers, whether their customers are specialist stores or a general stores.

3.The Limited-Service Merchant Wholesaler:

It is one who offers less than full service and charges lower prices. These types of wholesalers are also known as limited function wholesalers. This model comes to prominence when some customers may not want or may not be interested to pay for some of the services the Full-service merchant wholesaler offers. They may prefer to sacrifice the services offered to get lower prices. As a result of this particular category has emerged. This Limited -service merchant wholesaler is further divided into five types b ased on the various services they try to render and the on the basis of the payment for the goods they sell.

CLASSIFICATION OF AGENT WHOLESALERS:

The agents are the next category of wholesalers, they take possession of the goods but at the same time they do not take title to them. The agents in no way provide warehouse facility or credits but provide facilities like arranging credit or delivery as a part of their service. The agents make business through commissions based on selling prices of the product. The percentage of the commission varies based on the industry as well on the perishable nature of the product. The agents can be classified as follows namely

1. Brokers:

Who are intermediaries who bring the sellers in touch with the buyers and also facili tate in the contractual negotiations and receive commissions based on the work. Brokers are considered to be neutral and are found in every field. The commissions they receive from
both the parties will be relatively less and this requires minimum investme nt. Most organizations prefer brokers because they work on commissions and do not have long -term relationships with one particular organization.

2. Commission Merchants:

Commission merchants are similar to brokers but are given certain powers by the seller s of the product. They perform majorly the pricing function and work closely with the producers of the products. The commission merchants are most common in the agricultural products. The commission merchants take possession of the goods so that the prospe ctive buyers have a chance to inspect the products; once the deal is finalized the commission merchants deduct their commission past and return the balance to the producer.

3. Manufacturer’s Agents:

Manufacturer’s agents are those who are available for t he producer who are not interested in performing the sales activity or who lack the expertise to have one. The manufacturer’s agents work in limited geographical areas and in low priority zones. If a producer of electronic goods feels having a separate sales force for the rural areas is an expensive decision they may go in for a merchant’s agent to do the job of selling their offering. The merchant’s agents will be familiar with the area they operate and this is one reason why producers opt for the merchant ’s agents. One another benefit of these people is that they need not be paid till the deal is finalized.

4. The Selling Agents:

The Selling Agents are paid a commission and are expected to be familiar with the products and the markets. Unlike the manufacturer’s agents they do not restrict themselves to one particular geographical area but rather to all places where the product has got a market. Since they concentrate on a much larger scale they are given more responsibility including the elements of promotions and pricing of the products. The organizations who utilize these people are otherwise called as external marketing department.

UNIT IV

CHANNEL DESIGN

Learning Objective

To know the steps in channel design

- In channel design- segmentation positioning

targeting

- To understand implementation of channel.

What is the best marketing channel for a particular product or service?

This question is well worth asking, given the great expense of establishing (or changing) marketing channel and the high cost of poor decision making in this area. The marketing channel challenge involves two major tasks: (1) to design the right channel and (2) to implement that design. The design step involves segmenting the market, identifying optimal position- ing responses to segments' demands, targeting the segments on which to focus the channel's efforts, and establishing (in the absence of a preexisting channel) or refining (in the presence of a preexisting channel) the channels to manage in the market- place. The implementation step requires an understanding of each channel member's sources of power and dependence, an understanding of the potential for channel conflict, and a resulting plan for creating an environment 'where the optimal channel design can be effectively executed on an ongoing basis. This outcome is called channel coordination.

Designing A Channel System

We have observed that a firm can take its product to the user in more ways than one. It can use different types of intermediar- ies; it can also structure its channel in different ways. For example, it can have a single-tier or a two-tier or a three-tier channel structure. It can reach different market segments with different channel arrangements or with the same channel arrangement. It can also use different channel arrangements for reaching a single market segment. The options are indeed many.

- How does the firm make the choice? How does it determine which one is the best?
- Should it go for own channels-company showrooms and depots-or prefer conventional intermediaries, i.e. the wholesale/ retail trade? How many levels/ tiers should there be in the chosen channel design. How many wholesale points should it have to ensure satisfactory market coverage? Where should they be located?
- How many retail points should it have? Which are the places where it should have them?
- What should be the relationship between the wholesalers and the retailers?

1. FORMULATING THE CHANNEL OBJECTIVES

Formulation of channel objectives is the first step in designing a channel system. The objectives clarify what is sought to be achieved by having the channels. All firms seek to realise certain common objectives by having the channel. In addition, they may also have some specific objectives depending on their unique circumstances.

Channel Objectives will Decide Channel Design

Channel objectives will determine the channel design the firm should adopt.

Objectives, Firms Commonly Seek from Channels

- Effective coverage of the target market.
- Efficient and cost-effective distribution.
- Ensuring that consumers incur minimum exertion in procuring the product.
- Helping the firm to carry on manufacturing uninterrupted, confident that the channels will take care of sales.
- Partnering the firm in financing and sub-distribution tasks.

Channel Objectives Differ from Firm to Firm; Consequently, their Channel Designs Differ

We see that often channel designs of firms differ from one another. Even within a given industry; different firms have different channel designs. This is so. because their channel objectives differ. Even in respect of those objectives, which are by and large common for all firms, we can see variations in emphasis from firm to firm. For example, intensity of market coverage sought from the channels and extent of convenience to be provided to the customer will vary from firm to firm. The weightages will flow from the marketing objectives of the respective firms.

Distinctive Characteristics of Industrial Products

2. IDENTIFYING CHANNEL FUNCTIONS

Identification of the functions to be performed by the channel is the next step in designing channel system Channel design depends on the functions expected of the channel and that channel functions must be identified in the specific context of the firm in order to get practical direction in designing the channel system.

3. **Linking Channel Design to Product Characteristics** Different products require different channel systems. The firm should analyse the characteristics of the product and choose the channel system that matches the product best. Consumer a

industrial goods, for example, need different channels. And within the category of consumer goods, different sub-categories such as convenience goods, shopping goods and specialty goods may need different channel systems.

Industrial and Consumer Products Need Different Channels

Industrial and consumer products usually need different channels as they differ from each other in several vital respects.

CHANNELS FOR INDUSTRIAL PRODUCTS

Industrial products need extensive pre-sale service (installation and commissioning service) and post-sale service (maintenance service).

Consumer products on the contrary, are mass products. non- technical and least most of them are of a low unit value; they are regularly consumed and replaced; and require nil or limited after-sale service. It is in view of these differences that the two can need different channel systems.

ONLY SOME INDUSTRIAL PRODUCTS ARE AMENABLE FOR SELLING THROUGH CHANNELS

First of all, among industrial products, only some are amenable for selling through channels. The firm should check whether its items are appropriate for selling through channels / distribu- tors. And, if the answer is ‘yes’, it must find out which type of distributors will be appropriate for the items under consider- ation.

Chart below presents some useful guidelines for testing the amenability of a given industrial product for marketing through channels/ distributors.

Industrial Products: Amenability for Marketing Through Channels

• Only some industrial products lend for selling through channels.	• It must be a stackable item.
• The product must have a sizeable customer base.	• The unit value of the product should not be too high.
• It must be a reasonably standard item, not a totally custom-made item.	• In any case, industrial products need specialist distributors.

Need for specialist distributors: the firm finds that a given industrial product lends itself for marketing through channels; the firm may proceed to select an appropriate channel. It must remember that:

i. industrial products as a general rule require specialist distributors. Entrusting the products with the traditional consumer product distributors does not bring in the best results.

ii. different industrial products need different types of distributors.

For example, some industrial products have to be demon- strated to the customers. Here, specialist distributors with the required demonstration facility will be more suitable. Some industrial products are hazardous from the point of view of distribution. Petroleum products, explosives and certain industrial chemicals are examples of this category these products need specialised distributors, who command specialised transportation and storage facilities. Similar is the case of products that require extensive servicing. They need specialist distributors, who command the required service facilities.

EVEN WITHIN CONSUMER PRODUCTS, CHANNEL REQUIREMENTS OF DIFFERENT PRODUCTS MAY VARY

We come across three distinct categories of products within consumer goods-viz., (i) convenience goods, (ii) shopping goods, and (iii) speciality goods. We have seen that the different categories of goods require different channel systems, since buying behaviour and buying habits differ, depending on the category Convenience goods require intensive market coverage and, therefore, need a comprehensive and high penetration channel arrangement. Shopping goods and speciality goods need lesser intensity of coverage, compared to convenience goods. Often, in these cases, the number of tiers in the channel can be less than those for convenience goods. The number of outlets too can be far lesser. In the matter of location of the outlets too, the requirements will be different in respect of convenience goods on the one hand, and for shopping and specialty goods, on the other. Obviously, there is a need for product-channel matching. .

THE PRODUCT'S PLC STAGE TOO INFLUENCES CHANNEL CHOICE

We have seen that the concept of PLC helps product manage- ment. PLC also helps channel management. Different channels fit different stages of PLC.

A product in the introduction stage will be relatively unknown to the market; its customer base small; and its sales volume low. At this stage, it may be advantageous to sell the product directly to the customer, dispensing with the channels. Such a move will enable the manufacturer to get direct market feedback on the new product and thereby improve the product as required.

Alternatively, a specilised channel could be used in this stage. A specialised distributor will be in a better position to introduce the product in the market and also provide the required technical support to the user.

When the product moves into the growth and maturity stages, the requirements of distribution will be different. In these stages, the product is almost an off-the-shelf item. Now, convenience in delivery and price competitiveness are more important factors. Therefore, conventional/ general purpose distributors would be more suitable. Producers usually appoint a number of general purpose distributors at this stage and also make more and more territories non-exclusive. Some pushing becomes necessary at this stage and conventional market channels admirably suit this requirement.

In the decline stage in the PLC, the market for the product usually gets reduced to select groups of customers and it may be advantageous to revert back to direct marketing to customers at this stage. Alternatively, the firm may serve the select groups of customers through a minimal use of middlemen.

Product Influences Type and Number of Channel Members as well

Product characteristics influence not merely the channel design to be opted for; they often influence even the type and number of intermediaries needed. For example, for textiles or shoes, franchisees, who can run showrooms, may be an effective type of intermediary. For a product like detergents, conventional wholesaler-retailer arrangement may be the appropriate one.

4. EVALUATION OF THE DISTRIBUTION ENVIRONMENT

While selecting the channel design, the firm should also take into account the distribution environment obtaining in the country/ territory. It should evaluate the vital features of the distribution environment and ensure that the proposed channel design is compatible with them. Distribution environment in the broader sense includes the trade related legal environment as well. A mention about the legal environment relating to marketing and trade matters has been made in the chapter on The Marketing Environment. The legal implications of channel design must be carefully examined before taking a final decision.

5. EVALUATION OF COMPETITOR'S CHANNEL DESIGNS

The firm should also study the competitor's channel patterns before deciding its channel design. While the firm may not necessarily follow the competitors in channel design, it should analyse the plus and minus of the channel patterns adopted by each of its major competitors. Quite a number of firms do settle down for a 'follow the leader' policy in channel design.

They find it an easy route. But such an approach may deprive them of the chance to score an edge over competition through the channel strategy.

6. MATCHING THE CHANNEL DESIGN TO COMPANY RESOURCES

Choice of channel is also governed by the resources available with the organisation.

Firms with limited resources settle for conventional channels: Firms with limited resources and small volume of business will normally find it difficult and uneconomical to opt, for own channels. For such firms, establishing branch show- rooms/ depots/ retail outlets of their own will result in a high unit cost of distribution, which they cannot afford. They are better off by depending on conventional channels. In fact, they are usually content with a small network of conventional intermediaries.

Firms with larger resources have more options: Firms with larger resources and larger marketing operations can go in for varied distribution channels. In fact, in India, in several businesses, firms which are strong in resources, usually operate two parallel channels, one reaching out to the customer through company depots and showrooms, and the other through conventional intermediaries. The textile business is a good example of this phenomenon. Firms like Reliance Industries, Bombay Dyeing, DCM and Mafatlals, have all gone in for such a two-pronged channel design. In some cases, however, even large firms prefer a distribution arrangement wherein they will not be required to pump in much of their resources. They are content with entrusting their distribution job to some distribu- tion houses, appointing them either as the sole-selling agent or as marketers. Many manufacturers of pharmaceuticals, machine tools, agricultural equipment, electric motors and household appliances have adopted this route must evaluate these alternative designs and choose the best among them.

KEEPING THE SYSTEM FLEXIBLE

The physical distribution system should also be kept flexible. Marketing is never static. Thus, in keeping with the dynamic nature of marketing, the physical distribution system should remain, flexible. At the same time, flexibility has an associated cost. Often, that is why, issue of economy vs. flexibility is raised while designing a physical distribution system. Even at the cost of economy; some flexibility must be retained. It would come to the help of the firm in the future.

Why do we need to segment, position and target in channel design?

Channel Design: Segmentation

One of the fundamental principles of marketing is the segmentation of the market. Segmentation means the splitting, of a market into groups of end-users who are (1) maximally similar within each group and (2) maximally different between groups. But maximally similar or maximally different based on what criterion? For the channel manager, segments are best defined on the basis of demands for the outputs of the marketing channel. A marketing channel is more than just a conduit for product; it is also a means of adding value to the product marketed through it. In this sense, the marketing channel can be viewed as another "production line" engaged in producing not the product itself that is sold, but the ancillary services that define how the product is sold. These value added services created by channel members and consumed by end- users along with the product purchased are called service outputs. Service outputs include (but may not be limited to) bulk-breaking, spatial convenience, waiting and delivery time, and assortment and variety.

End-users (be they final consumers or business buyers) have varying demands for these service outputs. Consider, for example, two different soft drink buyers: an office employee at work, looking for a soft drink during her afternoon coffee break, and a family buying for at-home consumption. Table below outlines the differences in service output demands between the two segments of buyers. The office employee has high demands for all service outputs except assortment and variety (for which her demand is moderate, implying willingness to brand switch within reason), whereas the family has the opposite pattern of service output demands. Clearly, a different marketing channel meets the needs of these two segments of

shoppers. The office employee cannot travel to a grocery store to buy a can of soda during her break, nor does she want to buy a six-pack or more of cans of soft drinks. She is willing to pay a slightly higher price for the convenience of getting just a single can of soda close to her office. A vending machine would be an ideal retail outlet for her. The family, on the other hand, would not find the vending machine an attractive retail purchase alternative. The family's demand for assortment and variety may not be met by a vending machine, and other service outputs are offered at too high a level, resulting in a higher per-unit price than the family wants (or needs) to pay. A local super market does a better job of meeting the family's service output demands for soft drinks. This example shows how the same product can be demanded with a widely varying set of service outputs, resulting in very different demands for the product- plus service-output bundle by different segments of end-users. An analysis of service output demands by segment is thus an important input into a manufacturer's marketing plan, and can help increase the reach and marketability of a good product to multiple market segments.

Understanding market demands also requires an understanding of the market's environmental characteristics and constraints. A market with limited infrastructural

Service Output Demand Differences (an example of segmentation in the soft drink market)

	FAMILY		OFFICE EMPLOYEE	
SERVICE OUTPUT	DESCRIPTOR	SERVICE OUTPUT DEMAND LEVEL	DESCRIPTOR	SERVICE OUTPUT DEMAND LEVEL
Bulk breaking	"I buy groceries weekly for my family, and all of us l	Low	"I'm on my coffee break and I have time for only one ca	High

	ike soft drinks."		n of soft drink."	
Spatial convenience	"I drive to the supermarkets in my area to shop."	Low	"I have only 15 minutes for my break, so I need to buy whatever is handy."	High
Waiting and delivery time	"We usually have some extr	Low	"If I don't get my soft dr	High

	a cans of soft drinks in the house, so I'll just come back the next time if I can't find the soft drinks I want on th		ink right "at 3:00 when my break starts, I'll never have a chance to go back later arid get one."	

	is trip."			
Assortment and variety	"My husband and I like Coke and Pepsi, but our kids aren't permitted to drink caffeinated soft drinks. They	High	"I can't be too particular about which soft drink I pick. It's important to me to get one, as long as it has	Moderate

	like caffeine free fruit-flavored soft drinks."		caffeine."	

development, for instance, will usually be characterized by consumers with high demands for service outputs such as: 1) spatial convenience (because the consumers cannot travel very easily to remote retail locations), 2) minimal waiting time for good (because consumers will not have sufficiently high disposable income to keep backup stocks" of goods at their homes in case of retail stock outs), and 3) bulk-breaking (again because, with low disposable incomes, consumers cannot afford to buy large lot sizes of goods, even if doing so would mean a lower price per unit). An example of the impact of these constraints on consumer purchasing is the market for Wrigley's chewing gum in the People's Republic of China: Individual packs of gum are sold through many small kiosks and stalls in local marketplaces after traveling a circuitous (and high-cost) route through the countryside. If Wrigley's is to sell to Chinese consumers, it must recognize their high service output de- mands in order to construct a marketing channel to meet those demands.

Channel Design: Positioning

When the market has been segmented into groups of end- users, each of which can be described by a set of service output demands, the channel manager should next define the optimal channel to serve each segment. We call this exercise positioning or configuring the channel (positioning to parallel the segmen- tation-targeting-positioning paradigm in marketing management). Just as positioning a product means setting its product attributes, price, and promotional mix to best fit the demands of a particular segment, so also positioning refers to the design of the distribution channel to meet the segment's demands. This exercise should be done, even if the channel ends up not selling to some of the segments in the end. The channel analyst may then discover that some segments simply do not make good targets because their demands cannot be adequately met with the channel's current resources. Alterna- tively, the positioning exercise may reveal some unexpectedly attractive segments to target. Unless the optimal channel is defined for each segment, it is impossible to make a thorough decision about what segments to target.

The optimal channel is defined first and foremost by the necessary channel flows that must be performed in order to generate the specific segment's service output demands.

Channel flows are all the activities of the channel that add value to the end user. In enumerating the list of channel flows, we go beyond the concept of the mere handling of the product to include issues of promotion, negotiation, financing, ordering and payment. For instance, our office employee looking for a soft drink on her coffee break (see Above Table) has a high demand for spatial convenience and minimal tolerance for out- of-stock product. This means that the channel How of physical possession (the physical holding of inventory) takes on great importance for such end-users. Each product or service-selling situation can have its unique set of service output demands by segment, implying that the differential importance of different sets of channel flows depends on the segment.

Further, the channel analyst must identify the optimal-channel structure to produce the necessary channel flows, which themselves, of course, result in the generation of the required service outputs that are demanded by a particular segment of end-users in the market. The design of the channel structure involves two main elements. First, the channel designer must decide who are to be the members of the channel. For example, will a consumer packaged-goods manufacturer sell its grocery products through small independent retailers with in-city locations, or through large chain stores that operate discount warehouse stores? Or will it use an outlet such as Indiangrocer.com, an on-line seller of Indian' food and household products that operates no retail stores at all? Moving up the channel from the retail level, decisions must be made whether to use independent distributors, independent sales representative companies (called "reps" or "rep firms"), independent trucking companies, financing companies, export management companies, and any of a whole host of other possible independent distribution channel members that could be incorporated into the channel design.

Beyond this decision, the channel manager must also decide the exact identity of the channel partner to use at each level of the channel. For example, if it is deemed advisable to sell a line of fine watches through retail stores, should the outlets chosen be more upscale, such as Tiffany's, or should they are family- owned local jewelers? The choice can have implications both for the efficiency with which the channel is run and the image connoted by distributing through a particular kind of retailer. In a different context, if a company seeks distribution for its products in a foreign market, the key decision may be which distributor is appointed to carry the product line into the overseas market. The right distributor may have much better relationships with local channel partners in the target market and can significantly affect the success of the foreign market entry.

The other main element of the channel structure is the decision of how many of each type of channel member will be in the channel. This is the channel intensity decision. In particular, should the channel for a consumer good include many retail outlets (intensive distribution), just a few (selective distribu- tion), or only one (exclusive distribution) in a given market area? The answer to this question depends both on efficiency and on implementation factors. More intensive distribution may make the product more easily available to all target end- users, but may create conflict among the retailers competing to sell it.

The channel structure decisions of types, identity, and intensity of channel members all should be made with the minimization of channel flow costs in mind. That is, each channel member is allocated a set of channel flows to perform, and ideally the allocation of activities results in the reliable performance of all channel flows at minimum total cost. This is a nontrivial task, particularly because it involves comparing activities across different companies who are members of the channel. Intu- itively, an activity-based costing (or ABC) sort of analysis is useful to establish the best allocation of channel flows

This exercise results in one channel profile for each segment that is identified in the market segmentation stage of the exercise.

Each of these channel profiles is called a zero-based channel, because it is designed from a zero base of operations that is, as if no preexisting channel exists in the market. The concept of a zero-based channel means (1) that the segment's service output demands are met and (2) that they are met at minimum total channel cost.

Channel Design: Targeting

At this stage of the analysis, the channel manager is equipped to decide what segments to target. Note carefully that this also means that the channel manager is now equipped to decide what segments not to target! Knowing what segments to ignore in one's channel design and management efforts is very important, because it keeps the channel focused on the key segments from which it plans to reap profitable sales.

Why not target all the segments identified in the segmentation and positioning analyses? The answer requires the channel manager to look at the internal and external environment facing the channel. Internally, managerial bounds may constrain the channel manager from implementing the zero-based channel. For example, top management of a manufacturing firm may be unwilling to allocate funds to build a series of regional ware- houses that would be necessary to provide spatial convenience in a particular market situation. Externally, both environmental bounds and competitive benchmarks may suggest some segments as higher priority than others. For example, legal practices can constrain channel design and hence targeting decisions. Many countries restrict the opening of large mass- merchandise stores in urban areas, to protect small shopkeepers whose sales would be threatened by larger retailers. Such legal restrictions can lead to a channel design that does not appropri- ately meet the target segment's service output demands, and may cause a channel manager to avoid targeting that segment entirely.

Of course, the corollary of this statement is that when superior competitive offerings do not exist to serve a particular segment's demands for service outputs, the channel manager may recognize an unexploited market opportunity and create a new channel to serve that underserved segment. Meeting previously unmet service output demands can be a powerful competitive strategy for building loyal and profitable consumer bases in a marketplace. But these strategies can best be identified with knowledge of what consumers want to buy, and impor- tantly, how they want to buy it, and the necessary response in terms of channel flow performance and channel structure.

We have now identified a subset of the market's segments that the channel plans on targeting, using the segmentation and positioning insights derived earlier.

Channel Design: Establish New Channels or Refine Existing Channels

Now, the channel manager has identified the 'optimal way to reach each targeted segment in the market, and has also identified the bounds that might prevent the channel from implementing. the zero-based channel design in the market. If no channel exists currently in the market for this segment, the channel manager should now establish the channel design that comes the closest to meeting the target market's demands for, service outputs, subject to the environmental and managerial bounds constraining the design.

If there is a preexisting channel in place in the market, however, the channel manager should now perform a gap analysis. The differences between the zero-based and actual channels on the demand and supply sides constitute gaps in the channel design. Gaps can exist on the demand side or on the supply side.

On the demand side, gaps mean that the service output demands is not being appropriately met by the channel. The service output in question may be either undersupplied or oversupplied. The problem is obvious in the case of undersup- ply: The target segment is likely to be dissatisfied because

end-users would prefer more service than they are getting. The problem is more subtle in the case of oversupply. Here, target end-users are getting all the service they desire-and then some. The problem is that service is costly to supply, and therefore, supplying too much of it leads to higher prices than the target end-users are likely to be willing to pay. Clearly, more than one service output may be a problem, in which case several gaps may need attention.

On the supply side, gaps mean that at least one. flow in the channel of distribution is carried out at too high a cost. This not only wastes channel profit margins, but can result in higher prices than the target market is willing to pay, leading to reductions in sales and market share. Supply-side gaps can result from a lack of up-to-date expertise in channel now manage- ment or simply from waste in the channel The challenge in closing a supply-side gap is to reduce cost without dangerous])' reducing the service outputs being supplied to target end-users.

When gaps are identified on the demand or supply sides, several strategies are available for closing the gaps. But once a channel is already in place, it may be very difficult and costly to close these gaps. This suggests the strategic importance of initial channel design. If the channel is initially designed in a haphazard manner, channel members may have to live with a suboptimal channel later on, even after recognizing channel gaps and making best efforts to close them.

Channel Implementation: Identifying Pow er Sources

Assuming that a good channel design is in place in the market, the channel-manager's job is still not done. The channel members now must implement the optimal channel design and indeed must continue to implement an optimal design through time. The value of doing so might seem to be self- evident, but it is important to remember that a channel is made up of multiple interdependent entities (companies, agents, individuals). But they mayor ma)' not all have the same incentives to implement the optimal channel design.

Incompatible incentives among channel members would not be a problem if they were not dependent upon each other. But by the very nature of the distribution channel structure and design, specific channel members are likely to specialize in particular activities and flows in the channel. If all channel members do not perform appropriately, the entire channel effort suffers. For example, even if everything else is in place, a poorly performing transportation system that results in late deliveries (or no deliveries) of product to retail stores prevents the channel from succeeding in selling the product. The same type of statement could be made about the performance of any channel member doing any of the flows in the channel Thus, it is apparent that inducing all of the channel members to implement the channel design appropriately is critical.

How, then, can a channel captain implement the optimal channel design, in the face of interdependence among channel partners, not all of whom have the incentive to cooperate in the performance of their designated channel flows? The answer lies in the possession and use of channel power. A channel member's power "is its ability to control the decision variables in the marketing strategy of another member in a given channel at a different level of distribution." These sources of channel power can of course be used to further one channel member's individual ends. But if channel power is used instead to influence channel members to do t_ jobs that the optimal channel design specifies that they do, the result will be a channel that more closely delivers demanded service outputs, at a lower cost.

Channel Implementation: Identifying Channel Conflicts

Channel conflict is generated when one channel member's actions prevent the channel from achieving its goals. Channel conflict is both common and dangerous to the success of distribution efforts. Given the interdependence of all channel members, anyone member's actions have an influence on the total success of the channel effort, and thus can harm total channel performance

Channel conflict can stem from differences between channel members' goals and objectives (goal conflict), from disagree- ments over the domain of action and responsibility in the channel (domain conflict), and from differences in perceptions of the marketplace (perceptual conflict). These conflicts directly cause a channel member to fail to perform the flows that the optimal channel design specifies for them, and thus inhibit total channel performance. The management problem is twofold.

First, the channel manager needs to be able to identify the sources of channel conflict, and in particular, to differentiate between poor channel design and poor performance due to channel conflict. Second, the channel manager must decide on the action to take (if any) to manage and reduce the channel conflicts that have been identified.

In general, channel conflict reduction is accomplished through the application of one or more sources of channel power. For example, a manufacturer may identify a conflict in its indepen- dent-distributor channel: The distributorship is exerting too little sales effort on behalf of the manufacturer’s product line and therefore sales of the product are suffering. Analysis might reveal that the effort level is low because the distributorship makes more profit from selling a competitor’s product than from selling this manufacturers product. There is thus a goal conflict. The manufacturer’s goal is the maximization of profit over its own product line, but the distributorship’s goal is the maximization of profit over all of the products that it sells- only some of which come from this particular manufacturer. To resolve the goal conflict, the manufacturer might use one of the following strategies: In both cases, some sort of leverage or power on the part of the manufacturer is necessary to change the distributor’s behavior and thus reduce the channel conflict.

Channel Implementation:

The Goal of Channel Coordination

Now channel has been designed with target end-user segments’ service output demands in mind, and channel power will be appropriately applied to ensure the smooth implementation of the optimal channel design. When the disparate members of the channel are brought together to advance the goals of the channel rather than their own independent (and likely conflict- ing) goals, the channel is said to be coordinated. This term is used to denote both the coordination of interests and actions among the channel members who produce the outputs of the marketing channel, sand the coordination of performance of channel flows with the production of the service’ outputs demanded by target end-users. This is the end goal of the entire channel management process. As conditions change in the

Evaluation of the Distribution Environment

Evaluating the Alternatives and Selecting the Best

The New Business Environment

Conditions are changing simultaneously in different fields, social, political, economic and technological, and they are often in conflict. It is difficult to forecast the area where changes will most affect business. For each specific business, it is important to keep in touch with the key changes in each area of the business environment and to update the forecast.

Technological Environment

This is probably the easiest to identify:

- Accumulated technical knowledge (general exponential curve)
- World-wide communications system (transport, satellites, etc.)
- Data processing (mini-computers, data banks, office systems, electronic mail (E-mail))
- New processes aimed at lower energy consumption and higher feed/ raw material utilization, new energy sources .
- High investment cost.
- New technology for basic human needs (biotechnology, synthetic food, genetic engineering)

Economic Environment

This changes in the following areas:

- Obsolescence of all past theories
- Irrelevance of past extrapolation
- World-wide population growth, but concentrated in certain areas
- High energy/ raw material costs
- Inflation coupled with lower economic growth (stagflation)
- Monetary instability and disparity between developed countries
- (DC)/ Organization of Petroleum-Exporting Countries (OPEC) and LDC.

- Shortage of capital, credit squeeze, very selective investments
- Shortage of people able to understand the new environment
- Potential shortage of food world-wide

GENERAL IMPACT OF ENVIRONMENTAL CHANGES ON BUSINESS

Coping with the changing environment is already a difficult task; the difficulty appears larger when it is realised that not only is the number of changes high, but the difference in 'quality' is even more striking. Most conditions show fundamental differences with past history and knowledge, as well as the past and even the current approach to business theories and management. Things are not only drastically different, they change quickly, much faster than they did in the industrial revolution during the 19th century. These fast changes are therefore very difficult, if not impossible, to foresee; they create business turbulence and unexpected crises at short notice; instability, discontinuity and uncertainty seem to characterise the present years and this situation will continue until the world reaches a new period of stability in all these respects.

EVALUATION

All these changes can be frightening and leave one wondering whether the ordinary business executive can cope with them; whether the 'human gap' is not too great. However, there is no choice, so one might as well adopt a responsible and positive attitude instead of a passive and negative one.

The 'serenity prayer' says:

In most businesses, a change in environment can be considered either as a threat or as a new opportunity depending on the point of view. A newly industrialised nation can be considered as a threat (cheap competition) or an opportunity (new market).

While excessive inflation is a nightmare for most governments, it is viewed as an opportunity by many businesses. Increasing crime is a frightening trend to most people; but security companies consider it as an opportunity for more business.

It is important to conduct a rational and systematic analysis of the future impact of each environmental factor on a specific business; and to avoid being trapped in a last minute crisis, under the pressure of events, when it may be too late to adjust to them. This analysis can be set out in the following manner.

I. Environmental Factor: Technological

a. Degree of change: high/ low
b. Probability of occurrence: high/ low
c. Implication: opportunity or threat

2. Environmental Factor: Economic etc.

The probability level associated with each factor is a basic ingredient of any potential 'environment scenario' and concerns the risk evaluation of each future business strategy. Thus the systematic evaluation of opportunities and threats is a key part of the overall process of strategic business planning.

The Importance of Swot Analyses Answers to the following five essential questions, asked periodically, will provide clues to gaining advantage over competitors:

- What are our company's **unique strengths or aspects** which give us competitive advantage over our close competitors'?
- What are our **relative strengths** in comparison to our nearest competitors?
- What are our **weak flanks** which we have to guard?
- What are the **weak points** of our competitors which we can attack?
- What **ideas** do the foregoing give us in terms of opportunities?

To do this, it is necessary to make an analysis of the strengths, weaknesses, opportunities and threats (SWOTs) faced by the company and the distributor. Since the market-place, the conditions and the competitors may be different as far as each distributor is concerned, it is important to start afresh in each case. This analysis must be undertaken at least once a year.

Marketing and Channel Flows

The above analysis of a company's SWOTs must be augmented by similar analyses of the other channel members. The number of members in a particular channel can vary according to the length and width of the channel strategy a company adopts.

A Checklist for Selecting the Most Appropriate Channels

PRODUCT FACTORS

Four product variables must be weighed in channel selection.

I. Physical nature: the variations that influence the decision are:

a. Perishability of the product, whether physical or due to fashion;Seasonal variation, causing inventory problems;

b. Unit value of the product;

c. Inventory investment required; and

d. Customer service requirements.

2. Technical nature: whether

a. A simple or complex product;

b. Advice is needed on product use;

c. Installation is needed or

d. Special training is needed.,

3. Length of product line: This consists of a group of products related either from a production or a marketing standpoint. Intermediaries are preferable own sales force when the line is short. Decisions must be made whether' to use a single channel for the entire line or split the line and use multiple channels.

4. Market position: An established product made and promoted by a reputable manufacturer may have a high degree of market acceptance and can be readily sold through more channels than a lesser known product.

MARKET FACTORS

1. Existing market structure: This includes traditional modes of operation, geographical factors, size and placement of the population, etc.

2. Nature of the purchase deliberation: The amount of deliberation by the buyer before purchase differs from product to product. Frequent purchases need more buyer- seller contacts and intermediaries are indicated. Formal specifications and competitive bids may be used in purchasing certain industrial products.

3. Availability of the channel: Existing channels may not be interested in new products. The promoter can either persuade them or use aggressive promotion to stimulate consumer demand on the theory that this will force the intermediaries to carry the product in order to satisfy the customers.

INSTITUTIONAL FACTORS

1. Financial ability of channel members: Manufacturers may find it necessary to aid their retailers through direct financing; willingness to extend credit can influence channel acceptance. Conversely, mass retailers sometimes finance their suppliers.

2. Promotional ability of channel members: Wholesalers cannot aggressively promote particular products, but exclusive distributors usually join the manufacturer in doing so. Manufacturers assume this function in the case

of national brands, while the promotion of private brands usually rests on the mass retailer or wholesaler who establishes the brand name.

3. Post-sales service ability: The after-sales service, with or without a warranty, may be performed by the manufacturer, the retail distributor or an independent service organization. This ability affects channel selection.

THE CHANNEL DECISION

This is made by a combination of intuition and analysis, and the exercise of judgment. The decision is complicated by the interdependencies existing between relevant factors. While it is difficult to quantify the many trade-offs associated with channel decisions, certain tools can be applied to them. Cost analysis techniques will give reasonable estimates of each channel cost. System analysis involves trade-offs in time, service and costs in order to maximize profits in the long run. Quantitative comparisons are made between alternative production runs, inventory holding levels, transport modes, customer service standards, order transmission, processing systems, etc. This must involve computer-oriented modelling techniques owing to the large number of variables to be considered.

In recent years, significant environmental changes have taken place:

1. Trend towards a short-order economy - the increase in inventory has meant that the best decision is to order frequently, forcing the primary supplier to carry the necessary inventory.
2. Rapid expansion of product lines - this generates obsolescence and stock availability problems as well as inventory imbalance.
3. Price differentials and discounts - legally speaking, these have to be cost-justified.
4. Competitive strategies - at one time they centered on product features and price; now the emphasis is on indirect competition such as outperforming competitors on logistic planning and customer service.

The members of a marketing channel are interconnected by several different factors:

1. The product line from manufacturer to end-user
2. The flow of ownership from member to member
3. The cash flow as payments are made by one member to another
4. The exchange of information between channel members
5. The advertising and sales promotion directed by channel members towards other members or end-users.

Now we will study how a dealer is selected?

Qualifications/ Attributes to be Looked for in Prospective Dealers

---

Dealer Selection

Dealer selection is the first task in the process of dealer manage- ment. It is obvious that a firm has to be very careful in selecting its dealers. It has to ensure that those selected for dealership possess certain essential qualifications. Some of these qualifica- tions are common ones, irrespective of the product lines involved; others are product specific. Financial strength, business capacity, creditworthiness and salesmanship form part of the common qualifications.

QUALIFICATIONS/ATTRIBUTES TO BE LOOKED FOR

A detailed checklist of the qualifications/ attributes to be looked into while selecting dealers is furnished in above chart. The criteria can be modified appropriately, depending on the product characteristics, the marketing environment and the objectives of the firm.

In practice, however, it is difficult for any firm to locate dealers possessing all the qualifications and attributes enumerated in the chart. Obviously, one has to compromise. Out of the available candidates, the firm has to select those who have the potential to be a good dealer. Then, it should build them into effective and strong dealers through a sustained process of development. If the product requires a specialised distributor, as in the case of industrial products, the choice must be made accordingly;

Firms which are well established in the market and those that which possess certain unique strengths in terms of product, brand, service, etc., will enjoy a wider choice when they set out to appoint dealers. Their reputation and brand equity will pull in a large number of applicants who are above average in the required attributes. In contrast, for firms yet to be established, the choice base will be small. Such firms may have to initially accept those who prepared to take up the dealership and build a good network over a period of time.

THE NET MUST BE CAST INTELLIGENTLY

Effective dealer recruitment depends in the first place on the firm's ability to attract applications from the right candidates. Advertisements will no doubt be of help in this regard. But they must be developed carefully. The companies and ad agencies must have the expertise needed for developing effective dealer recruitment ads.

'DEALER WANTED' ADS

The first test of a good 'dealer wanted' ad is no doubt its 'attention grabbing' strength among the prospects. The second test is the ad's ability to coax the stronger ones among them to respond to the proposition being made. In the present times, with more brands crowding the marketplace, the premium on dealers' shelf space is increasing exponentially; It needs a well- thought out and well-written dealer ad to bring in the right response. The communication must put across the proposition forcefully; while many companies give 'dealer wanted' ads, only a few do a good job of it. Cited below are a few effective 'dealer wanted' ads.

The Nanz ad: The Nanz ad is another example. The Nanz Lobill chain stores were to be run by franchisees. The approach of Escorts-Nanz in this regard could be understood from the ads put out by them towards locating prospective franchisees.

Evaluating the Alternatives and Selecting the Best With the completion of the foregoing steps, the number of alternatives would have narrowed down considerably; The firm must evaluate these alternative designs and choose the best among them. Actually, two distinct evaluations-an economic evaluation and a conceptual evaluation-may be necessary.

Economic evaluation; balancing cost, efficiency and risk: Cost and efficiency are the two main parameters in economic evaluation. Often, though not necessarily, the two are directly proportional. The firm has to rate the risk associated with the different alternatives. The firm's choice is a compromise among the three parameters. The first step here is the determination of the sales volume that can be obtained through each alternative design. Second, the costs of selling that volume through that alternative have to be assessed. In other words, the firm determines the unit cost of selling in each of the alternatives.

The firm chooses the one, which is attractive from the cost vs efficiency angle and is also relatively less risky.

Conceptual evaluation; flexibility and controllability: Conceptual evaluation is also equally important. It has to be used for assessing the flexibility and controllability of the alternative. It is possible that economic evaluation points to one particular alternative as superior, while conceptual evaluation gives it a low rating. For example, a marketer-oriented channel design may show merit in terms of unit cost of selling, but may show severe limitations from the standpoints of controllability/ flow of market feedback as well as requirements of long-term market development. With conceptual evaluation, the firm can also check out whether the alternative is compatible with its business objectives.

SOME VITAL ASPECTS IN FINALISING THE CHANNEL

The job is not over with the selection of the basic channel design. Within a given design, .different arrangements are possible. It means that further decisions are needed. The important aspects to be decided are:

- Channel intensity
- Number of tiers
- The appropriate variant within the design
- Choosing the Channel Intensity

While two firms may go for the same channel design, they may need different intensities. It depends on the position of the firm its objectives and strategies, its sales, profits, and market coverage, present and projected, and its resources. For example, Maruti and Mitsubishi India, being passenger car firms operating in the same market, may opt for similar channel design. But they may settle for different channel intensity; Maruti has a massive network consisting of 144 sales outlets, 175 dealer workshops and 750 authorised service stations across India. Mitsubishi has not gone in for similar intensity.

In fact, a firm would be ill-advised to adopt without question the channel intensity of another firm, even if the latter were the industry leader. What suits one may not suit the other. Blindly following another firm's channel pattern and intensity will land the firm in trouble. Recent experience of some well-known MNC FMCG firms in India will clearly amplify this point.

So, the choice depends on the context. The governing principle is that the chosen channel must have the capability to sell the product and to provide the required market coverage. It should also ensure that the user gets the products with the minimum of effort or strain on his part. And it must be cost-effective.

The channel must also be amenable to the control of the company to the extent required for operating the marketing system.

In recent years, as a general trend, the number of tiers in the distribution channels is getting shorter. Businesses that used to have a three-tier structure earlier now have a two-tier structure and those with a two-tier structure earlier are now trying to manage with a single- tier channel. And often, the axe falls on the stockists. Asian Paints, again, is an example. It chose, as a matter of conscious policy, a single-tier channel-going directly to the retail trade.

Selecting Appropriate Variant within a Given Design Usually, within a given channel design different variants can be thought of. For example, firm I: A and firm B may opt for the same channel design consisting of conventional wholesalers and retailers. Still, their approaches within the model can vary from one another. Firm A may opt for a wholesaler-weighted system, while firm B for a retailer-weighted system. For example, Nirma Chemicals distributes Nirma soap with a wholesaler-weighted system. In contrast, HLL distributes its Lifebuoy in the same market through a retailer-weighted system. Nirma off-loads the product on the wholesalers at a larger discount; the retailers buy the product from the wholesal- ers. HLL reaches out directly to a large number of retailers, using wholesalers! C&F agents to the extent necessary:

The two variants have their associated advantages and disadvan- tages. For instance. the wholesaler-oriented system obviates the need for a large sales force, thereby resulting in considerable

CHANNEL MANAGEMENT

Learning Objective

- How to manage the channel network
- To understand the trade relation mix
- To know how channel members are appraised
- To understand the need of channel member training

In this lesson let us study about how channel members are managed.

Managing The Channel Member

Developing the channel design, recruiting intermediaries and inducting them into company are not everyday tasks in channel management. It is the administration and management of the distribution network that constitutes the everyday task here. We shall examine task in detail.

Component Tasks in Managing the Intermediaries The task of managing a distribution network has several components as shown in the below chart

DETERMINING THE TRADE RELATIONS MIX

Evidently, developing the trade relations mix is the first task in distribution management. As shown in the chart A the trade relations mix or relations between a firm (principal) and its members revolve largely around the following four factors:

- Territory of operation
- Trade margin
- Functions which the channel member have to perform
- Functions which the firm has to perform

Territory of Operation

The firm must settle the issue of territory in a fair manner. Territory has significance at wholesale as well as retail levels. Different businesses have different requirements and different practices in this regard. FMCG businesses, for example, supply their products to practically all retail outlets; they do not assign any territory as such to any retailer; they assign territories only to distributors, redistribution stockists, and C&F agents. Durables marketers on the contrary, operate through a limited number of dealers in each town. Usually in these lines, territories are assigned to the dealers; even where territories are not exclusively assigned, an understanding is often worked out.

Chart – A the Network	**Component Tasks in Managing**
• Fixing the trade relations mix • Territory of operation • Trade margin • Functions which the dealers have to perform • Functions which the firm has to perform • Servicing the dealer	• Securing shelf space and merchandising support from dealers • Dealer motivation • Performance appraisal of dealers • Dealer training and development • Resolving channel conflicts

In some cases, manufacturers supply their products directly to certain specialised channels select consumers bypassing the appointed wholesale functionaries in the territory; Such buyers usually prefer, as a matter of policy, to deal with the principal rather than the wholesaler of the area. The wholesaler of the area often expects some compensation for such sales that take place in his territory: The manufacturers some times cover the wholesalers with an overriding commission for such sales. At other times, they do not provide any compensation whatsoever. The important point is that the firm must have settled in advance the policy in this regard with their wholesalers. The agreement between the firm and the wholesaler must specify whether and to what extent the wholesaler will be covered on such sales.

Trade Margin

Trade margin is the No.1 element in trade relations mix. Channel member invariably look for wholesome, juicy margin. The principals invariably try to peg it as modest as possible. The point to be noted here is that the margin must be sufficient to enable the dealer to gain a reasonable return on his investment.

Present-day dealers as a rule, expect larger margin: In the earlier days, dealers managed to operate their outlets with modest trade margins. First, their investment in infrastructure was relatively low and they were able to make a profit even with a modest margin. Second, their expectation of profit was also relatively low. In recent years, the position has been changing rapidly; First, the new generation dealers adopt a more contem- porary approach to retailing. Accordingly, their investment in the business infrastructure is much larger. They go in for attractive shops/ showrooms; they periodically renovate and redecorate the premises; they also employ skilled and better trained salesmen. All this naturally pushes up their investment in infrastructure and their overheads. Running costs too have been going up. Added to this, the expectation of the new generation dealers in the matter of profit is also considerably higher compared to the earlier day dealers.

Paradigm shift from ‘gross margin’ to ‘retained earning’: Thus, in the contemporary scene, in most cases, the manufac- turers have to willy-nilly settle for a higher outflow towards dealer margin. It also becomes necessary for them to accept a paradigm shift in this matter-from ‘gross margin’ to ‘retained earning’. They are required to hike the dealer margin to a level that would fetch the dealer a reasonable ‘retained earning’ after meeting all his normal expenses. They are also required to collaborate with their dealers and help them achieve a larger turnover and greater retailing productivity, so that at a given level of trade margin, their retained earning is higher.

In the matter of margins, the way it is structured and allocated among the different tiers/ levels in the channel is as important as the total quantum. There are several instances where firms have suffered in their marketing endeavour on account of defective structuring and improper allocation of the margin among the different levels of the channel.

Hawkins Pressure Cookers

Let us understand this with an example of Hawkins pressure cookers. They gained market dominance by recasting the margin structure.

Functions Which channel has to Perform

They have to perform the following essential functions normally expected by their principals.

Functions are

- Help establish the brand in the market
- Help achieve the sales targets
- Provide adequate shelf space
- Provide merchandising support
- Provide service to consumers
- Make prompt payments
- Maintain fair trade practices
- Provide winning store image

Functions the Principals have to Perform

Building the Brand

Dealers always want their principals to provide them a winning brand. Discriminating dealers give far more emphasis to the firm's performance on the brand front rather than the trade margin offered by the firm. They hesitate to take dealership of weak brands even if they offer very attractive margins. And, they are happy to deal strong brands even if the margins offered are low.

Functions, the Principals have to Perform

- Supply quality products
- Build the brand and keep it a winner
- Regular, adequate and prompt supply of the product
- Effective servicing
- Advertising and sales promotion support

They overwhelmingly vote for products/ brands that move from the shelf without any need for pushing. Likewise, they vote for products and brands that make their customers come back to their shops with enthusiasm. They also prefer prod- ucts/ brands that provide them volume margins rather than value margins. Dealers have to put in a lot of their time. Effort. shelf space and money on the various products that they deal in, and they certainly do not want to get stuck with a weak

brand. In particular, when a company offers a new brand the dealers want to be sure that the company would continue with the

brand and build it well.

Regular; Adequate and Prompt Supply

Regular supply of the product by the principal is another major concern of the dealer. If the firm is unable to supply the product regularly after he has pushed the brand with his customers, he not only loses face with them, but also runs the danger of losing out his other business.

Effective Servicing

We shall cover this point in the section on servicing and administering the dealer.

Advertising and Sales Promotion Support

Dealers also expect adequate advertising and sales promotion support from the principal, In particular, they expect good point of purchase promotion support. Such support. besides helping them to achieve higher sales, also serves as a good motivation.

Trade Relations Mix must Provide Satisfaction to both Dealer and Principal

The name of the game is to ensure that the trade relations mix

provides satisfaction to the dealer as well as the principal. The firm must offer a viable business proposition to the dealer. That is the baseline, It must also remember that dealers act more as a purchasing agent for the consumers than as a selling agent for the principal. And, it must hence enthuse the dealers by supplying products/ brands. which they would be happy to purchase on behalf of their customers.

SERVICING AND ADMINISTERING THE DEALERS

Dealers expect effective servicing from the firm. Prompt supply of the product is one part of effective servicing. Prompt supply of the product helps the dealers not only to achieve larger sales. But also faster turnover and lower cost on inventory carrying.

Technical support is the other part. Technical support must be forthcoming promptly from the firm wherever necessary. In any bazaar, one can see several cases of retailers switching their loyalty from one company to another purely on the basis of their servicing standard.

Effective servicing; example o f Electrolux: In the white goods business, Electrolux has scored an edge through effective servicing of dealers. They have picked up one crucial aspect in servicing-replenishment of stocks-and have scored high. They have enabled their dealers to achieve larger sales and simulta- neously reduce their inventor~ Now, they can draw their supplies from a ring of warehouses around the country and receive the stocks within 24 hours. Electrolux has actually reached a point where its dealers need not carry any inventory at all; the company delivers the products directly to the consumer, once the dealer enters the order on his computer, which is connected to company's stock points. Earlier, the dealers had to wait for two weeks or more; they had to carry heavy inventory; to avoid 'lost sales' due to 'stock outs'.

Regular visits by field force: Largely, the field sales force of the company/ its C&F agents stockists provides dealer servicing. The dealers expect regular visits by the field sales force, so that seated in their shop they can have all their problems addressed. The dealers also expect to be kept updated on all vital matters relating to the business. This is possible only if the salesman visit the dealers regularly.

Securing Shelf Space and Merchandising Support from Dealers

Securing shelf space and merchandising support from dealers is another important aspect of dealer management. By enlisting the willing cooperation of the dealers in the merchandising effort, the firm derives multiple benefits. Effective merchandis- ing accelerates the buying process as it serves as an on-the-spot reminder to the consumer to buy. A quick glance at the way in which the dealer aids/ point of purchase promotion materials supplied by a firm are used in a retail shop, can help one judge the firm's dealer management.

In the contemporary Indian context, getting shelf space and merchandising and display support from the retail outlets is of special significance as competition among brands is fast building up at the retail level. For example, in CTV's s since a number of firms compete for the limited shelf space available at the retail shops, the ones who score in this matter enjoy an overall edge in marketing.

Even big firms and major brands have to fight for shelf space: With the growing competition and the explosion in branded FMCG products, the premium on shelf space has been going up steadily: The competition *for* grabbing shelf space usually becomes more intense during stagnant market condi- tions. Even big firms and well-known brands have to earn their shelf space and display the hard way; they are not in a position to demand it as a matter *of* right *from* the retailers. For example, some time back, even a firm like HLL was not in a position to demand *from* its retailers' shelf space and display arrangement

for its internationally acclaimed brand Denim, by merely citing that it was a Lever product and an international brand. Nor could it get it by touting its bazaar power of a million retail outlets. The dealers wanted to be convinced about the con- sumer preference *for* the brand before he considered it *for* shelf space and display. Mter all, he now had the choice of a whole host of products brands with international affiliations and he could pick and choose the products/ brands to which he would allot shelf space.

Many companies are now running special communication programmes with a view to acquainting retailers with their products and brands, and convincing them of the benefit that would accrue to them if they patronised them. Companies are also now forced to meet a major part of the expenses involved in display in the shops. In fact, they are even expected to meet the expenses of general decoration of the shops. ITC, *for* example, has been earmarking a substantial portion of its promotional budget to the decoration of retail outlets. The company now sets up at its cost special counters, which add considerable glamour to the shop and serve as point of sale advertising.

Today, in most companies, merchandising accounts *for* more than 15 per cent of the total marketing spend. Many companies are also devising their own quality control checks on merchan- dising fronts. Kellogg has about 20 staffers doing the rounds of the outlets once every fortnight. And, at Pepsi, the merchan- dising teams stir out every two or three months and, even more frequently during the peak season, carrying with them scissors, cello tapes, dusters, nails, board pins, hammers, thread and, of course, the usual POP material. They clean the bottles, dust the racks, put up new posters and rearrange the bottles so that the brand fails the customer.

Ensuring Right Store Image

The competitive edge a firm derives from its retailers extends far beyond shelf space, merchandising and display: The store can be a total communication tool for the company. We shall be discussing the communication role of marketing channels in detail in the chapter on Marketing Communications. Suffice to point out here that the retail points are not mere outlets form where the products flow out. They serve as communication tools as well. It is a fact that consumers patronise certain stores and discard certain others. The store image does the trick. Today, more and more companies are realising the communicative significance of the stile image and are concentrating their attention on the ‘store image’ of their retail shops.

It was mentioned earlier that in many businesses the marketing war is fought and won at the dealer level. Better servicing of the dealers, better communication and better motivation and training bring in superior dealer loyalty. And, with this loyalty, the firm can win markets. A firm enjoying superior dealer loyalty usually gets a bigger slice of the market.

It is aptly said that a wise firm gets a good band of dealers and good dealers settle down with a wise firm. And a wise firm is one that provides right motivation to its dealers.

PERFORMANCE APPRAISAL OF CHANNEL MEMBER

Appraisal of the performance of individual channel member is yet another important element of channel management.

Performance appraisal must bring forth the strengths and weaknesses of the channel member. If the performance is below the desired level, remedial action must be taken promptly. The appraisal should specifically identify areas where improvement is called for.

The appraisal has to be based on pre-agreed standards of performance. Appraisal based solely on sales volume will be inadequate. The ranking done on this basis may not correctly reveal the contribution made by different channel member. The fact that channel member face varying environments in their sales operations should be taken into account while appraising their performance. A wider set of relevant criteria must be used in the appraisal. While the criteria may vary from company to company and product to product.

Performance appraisal is intended to serve as a means of improving the performance of channel member. In extreme cases, however, the appraisal may lead to the termination of the channel member. When termination is the only alternative, the firm should not hesitate to take that course.

Basically, all channel members are evaluated on the basis of whether they have met their assigned targets or not. Customer satisfaction surveys are also conducted to evaluate the quality oft service provided by the channel member.

WEAKNESSES COMMONLY NOTICED IN NETWORKS

- The Network is inadequate size-wize
- The network is inadequate, qualitatively
- The network is not properly spread out.
- The interior markets are not covered properly
- A part of the network is inactive
- Quite a few links in the network are unviable
- The network is excessive for the task on hand

Review of the Dealer Network as a Whole

In addition to performance appraisal of individual dealers, the firm must also carry out periodic reviews of the dealer network as a whole. Removal of weaknesses in the network is the objective of such a review.

All such weaknesses must be overcome if the channel has to function as a vital instrument of marketing.

Training and Development

Training is another important part of channel management. The primary purpose of training is to improve the perfor- mance of the channel members through a sharpening of their sales skills and product knowledge. Upon the channel members rests the responsibility of sensing, serving and satisfying the needs of the customers. The intermediary cannot fulfill this role unless they are equipped with the requisite knowledge, skills, techniques and attitudes. Any progressive firm will, therefore, make training an integral part of its channel management endeavour.

The content and methodology of training should be framed so as to suit the back- ground of the channel member and the contextual requirements. The prime purpose of the training is to impart to the channel member knowledge about customers, about products, about competition, and about merchandising and sales techniques. In addition, essentials of inventory management, credit management and sales promotion can also form part of the training content. When competing companies match each other in the marketplace in every aspect, it is the training provided to the channel member that makes them different. And that's why most companies are now concentrat- ing their energies on training. They now consider it a necessary investment.

Hyundai Motors India, for example, took all its 70 dealers to Korea a before the launch of its Accent model. Daewoo and Hyundai both conduct regular in-house training programmes for their dealers. Concorde, a Telco-Jardine Matheson JV; created for setting up the dealer network for Indica, conducts in-house training for Indica dealers. And, Maruti has tied up with National Institute of Sales for training its dealers.

Resolving Channel Conflicts

Sometimes, there may be unhealthy competition and conflicts among the different channels/ channel tiers employed by a firm. There may also be conflicts among the channel members within a given channel type/ channel tier. These conflicts must be handled with tact and fairness.

In managing marketing channels, firms will usually encounter some 'bottom-up pressure'. The retailers would exert pressure on the wholesalers/ stockists, and the latter would pass it on to the firm. Sometimes, the wholesalers/ stockists may have their own problems with the firm. Wise firms anticipate the pres- sures that can emerge from the different layers of the channels and formulate appropriate channel policies.

Tackling dealer conflicts-Wipro-lnfotech: Wise firms follow a sound policy with regard to dealer conflicts. Wipro-lnfotech Group (WIG) can be cited as an example. In the first place, it makes a conscious effort to reduce the scope for conflicts among dealers through dealer/ product class/ marketing segment alignment. It has reduced the scope for conflicts among dealers, by explicitly defining the territories of operation of each. Often, there is stiff competition among WIG dealers and they frequently under-cut each other. The under-cutting is com- pounded by the fact that different dealer categories have varying margins. For example, an A + category dealer will be able to easily under-cut a B category dealer. This de-motivates the smaller dealers. So, the company strictly enforces the sales territories. The scope for cannibalisation is also removed. And when conflicts do occur, WIG tries to resolve them in a fair and firm manner. When overlapping does occur, then it negotiates with both the dealers, evaluates as to which of them is capable of satisfying the needs of the particular customer more efficiently and entrusts the customer with him. And while

doing this, it takes care to protect the sentiments of the losing dealer.

Conclusion

In practice, the job of channel management is quite exacting. Firms usually have a large number of channel member spread over a large territory: Administering them, communicating with them and keeping them happy and well motivated, involves a great deal of effort on the part of the firm, In fact, in a sense, channel management is more difficult than employee management, While, employees of a firm are under its direct control, the channel members are not. Accordingly, administration, and motivation becomes far more difficult in the case of intermediary as compared to employees.

It should finally be mentioned that channel management, which includes intermediary selection, channel motivation and channel development, is a continuous job. The efforts cannot be slackened any point of time. Even in the best of networks, there will be some dropouts, every year; a few may become inactive. New channel members must be added in place of those who drop out. And, the inactive ones must be either activated or weeded out. Even when the dealer outfit is in a fairly trim condition, there has to be a continuous infusion of fresh blood into the system. Similarly, training and develop- ment of the channel member has also to be a continuous effort.

CHANNEL MOTIVATION

The Vision, Mission and Objectives

Channel objectives determine channel strategy. Making a major change in an established channel structure is difficult and often risky. Therefore it is desirable to set up the objectives properly in the first place. They should be dictated by the service level output which is desired by the ultimate consumer and the global vision and mission of the company in terms of long term return on investment, market share, absolute level of profits to be achieved and sales growth.

The specific objectives of any channel, apart from the global aspirations of the company, should be firmly based on the service outputs demanded by its customers. Different levels of these outputs may be required in different segments of the market and these need to be determined. The use of multiple channels catering for different segments of the market is common in marketing today.

Once the service levels are decided upon, then the market coverage has to be determined. This in turn determines the support which can be expected from the channel in the event of different coverage strategies. Here the company should also decide whether it needs to own the entire channel or parts of it and what the costs of full and part ownership are going to be in terms of possible consequences.

Three choices are possible: intensive, selective or exclusive distribution. It is worth mentioning in this context that they are all possible in case of vertical or non-vertical integration although the costs may be prohibitive in case of full ownership of a channel specializing in intensive distribution.

Intensive distribution is generally used for products which are frequently bought and which need to be easily available, like newspapers and sweets. Selective distribution is usual for products which buyers like to choose with some effort, e.g. clothing. This type of distribution can. range from expensive items which are almost exclusive, to items like cosmetics which are almost intensively distributed. Exclusive distribution implies a mutually dependent relationship between seller and re-seller and is used for large or expensive items such as farm machinery or very expensive clothes or jewellery.

It is appropriate to check and verify that the strategy adopted is in line with current circumstances when considering how to motivate a channel member. The channel structure and the type of distribution are also interdependent to some degree. A ‘long’ channel structure which possesses many intermediate wholesalers allows for greater spread and therefore more intensive distribu- tion. Conversely, a ‘short’ structure has more direct channels and tends towards exclusive distribution.

It is obvious that the more intensive the distribution, the greater the sales in the short term. However, over a long term, adverse effects such as lower margins appear, followed by unwillingness on the part of the distributors to sell the product, consequent necessity of an increase in promotional efforts by the manufac- turer and deterioration of the service levels. As a business executive once remarked ‘you can take fifty years to build a brand and you can ruin it in three years through careless distribution’.

However, intensive distribution is successfully followed in the case of innumerable products through a well-formulated marketing programme which fulfils the requirements of distributors and consumers alike. The various factors should be carefully considered before deciding on a distribution strategy, in particular the relation between the products marketed and the last selling point for them.

Motivational Tools and Control Areas

The following means of persuasion are available to channel members to influence the decision-making or behaviour of others.

1. **Rewards:** If A possesses some resource which B wishes to obtain and B believes this can be obtained through confirming to A’s wishes, this amounts to reward power. Specific rewards to channel members could include wider margins, granting of exclusive territories and various promotional allowances.
2. **Coercion:** This exists if B believes that A will punish anyone who does not conform to A’s wishes. Coercion amounts to negative sanctions or punishment including reductions in margins, withdrawals of rewards granted earlier and slowing down of shipments. This brings less results over the long term than other tools and should therefore be considered as a last resort.
3. **Expertise:** This occurs when B perceives A to possess some special knowledge which would help B. Small retailers often rely heavily on their wholesalers for expert advice. However, once transferred, expertise is considerably reduced in power. If a business wishes to retain expertise over a long term, the following options are open to it:

a. It can ration its advice to small portions and keep back sufficient vital knowledge so that the others remain dependent upon it. This could be detrimental to efficient working of the channel as every member should work up to its capacity for the channel to function successfully. A member starved of vital information cannot do so.

b. A better though somewhat expensive option is to collect accurate information regarding market trends, threats and opportunities, and other ongoing matters which individual channel members would find difficult to obtain themselves. The benefits of this option can be high in terms of channel goal achievements.

c. Another way is for channel members to invest in specialized transaction expertise which is difficult to transfer to other products or services and so hinders the members from leaving the channel.

d. The ability of a channel member to acquire information which is necessary for another channel member to function efficiently confers power on the acquirer. For example, retailers hold a privileged

position with respect to manufacturers because of their close customer contacts.

4. **Identification:** This occurs when B identifies with A or desires to do so. For example, given equal returns from two different dealerships, one may well choose that which one would like to identify with, perhaps the marc prestigious one. Here the company reputation or image confers an advantage on the business.

5. **Legitimacy:** Results from B feeling that A has the right to exercise power over them. This would be the case between workers and their supervisor, for example. In a channel relationship, such a power may be assigned to the largest firm. Or the retailers and industrial suppliers may believe that they have the power since they are in contract with the end-users and the others are not. However, the amount of power thus exerted is usually small.

In real life situations, all these powers are used simultaneously in most situations. Sometimes, the use of one power may enhance another power base; or the opposite may happen.

Environmental conditions and the effect of such a use of power on them must also be considered in this situation. The norms of the channel systems also prohibit the use of some of these powers.

The degree of success that a channel member will have in influencing the behaviour of other channel members will depend on its leadership behaviour. When the channel mem- bers have common goals, the use of information exchange and/ or recommendations will probably produce positive

results. In other situations, promises, threats, legalistic strategies and requests are used with varying success.

An international business manufacturing paints, which is based in Italy, has the policy of treating its agents like its own employees. They are required to submit progress reports every month just like the company sales force. All these reports are fed into a computer and analyzed. The company management keeps an eye on the stocks bought by key customers and the price they paid. Any falling off in an agent’s performance results in rapid identification of the problem and support provided by a senior staff member on the spot.

Focusing channels onto specific products and target markets – motivation of channel principals and sales force

Ensure that the traditional distributor attitude and priorities are recognized by you and dealt with. Distributors:

- always feel that a high price is charged by the manufacturer
- think that manufacturer's mark-up is high
- think that the manufacturer does not invest in the market Avoid the traditional manufacturer attitude. The manufacturer:
- is interested in volume sales
- is interested in profits
- wants distributors to make stock investment

How to ensure that a manufacturer's product is measured Check that the points in below Table.

For mutual benefits the relationship should produce:

- acceptable profit margins to the distributor
- acceptable volume and rate of growth to the manufacturer, at optimum profit margins

Distributor principal has:	Distributor sales executive has:
1. Quality product 2. Reliable delivery dates 3. Fair profit margins 4. Good communication, physical and written 5. Reasonable advertising and sales promotion support 6. Willingness by manufacturer to assist with distributor's general problems	1. Quality product 2. Reliable delivery dates 3. Technical information as and when required 4. Ad hoc bonuses, e.g. money, travel, trip to manufacturer's head office, etc. 5. Good communications with manufacturer's 'field' representative. 6. Fair evaluation of performance

Table: Factors affecting the majoring of a manufacturer's product

The manufacturer's 'link person' must try and assist the distributor in upgrading their entire operation. Allow the distributors to consult your financial director; let individual interested distributors have the use of the director's time for a day or two. Run seminars on relevant subjects, e.g. 'modern warehousing'. A distributor should be able to call on the manufacturer's experience when trying to solve any problem relative to their business.

Control systems

First and foremost, a system to establish an annual campaign plan must be introduced. This campaign plan should cover, as a minimum,

- the common goals to be achieved in the first year at least;

- what this would mean realistically in terms of the quarterly volumes of
- sales to the channel's customers and shipments from the manufacturer;
- the recommended price at which the product would be marketed;
- the price/ discounts/ terms of trading at which the manufacturer will supply
- the product;
- what this would mean in terms of market share;
- levels of sales and supporting staff resources to be deployed;
- a schedule of training to be provided by the manufacturer;
- promotional materials, campaigns, etc., to be undertaken by the manufacturer and the channel;
- specific actions to be taken concerning inventory/ logistics, etc.;
- key event/ action review calendar.

Secondly, regular monitoring and review sessions must be held to ensure that the performance is on course and that if needed, corrective actions are taken on time.

Motivation of the distributor

The link person or manager can do the following to motivate a distributor:

1. Attempt to categorise and understand the distributors' motives in terms of Maslow's hierarchy of needs: security, social needs, esteem, self-fulfillment.
2. Discover their wants as well as their needs; this will help your dealings with them.
3. Remember that monetary rewards serve many needs and are therefore the best rewards.
4. Bear in mind, however, that recognition, praise, promotion and successful achievement of a task can also be effective motivations and are sometimes more needed than money.
5. If people know that good work will earn a reward, this makes the reward more effective. The expectation should be clearly set out on a payment by-results basis, with an appropriate bonus or commission scheme. Achievable targets and standards should be set. Praise should be bestowed when deserved at not too frequent intervals. The rewards and efforts required should be clarified. The penalties also should be stated, if targets are underachieved or if substandard results are recorded.
6. Paraphrasing what Douglas McGregor said in another context, conditions should be such that the members of the channel system should best achieve their own expectations by working for the success of the channel system as a whole. It is necessary to identify the needs of the members so that appropriate rewards can be devised and to agree targets and standards with all the members.
7. People can be motivated by the work itself if their needs for achievement and responsibility are thereby satisfied. This can result from:

- giving ,people more responsibility where called for and more scope for variations in methods and speed of work;
- giving groups a unit of work to perform, thus reducing specialization and increasing the sense of achievement and responsibility and the expertise;
- relaxing overhead controls while setting targets and/or standards to make members accountable;
- making available the necessary information so that members can monitor their own performance;
- encouraging the channel members to join in planning and innovation.

8. Try to make sure that the group pressure is working for you by involving the members of the channel in decisions which affect them.

The link person's role can be likened to that of a master of ceremonies, who initiates the use of the available motivational tools, the link persons have to be self-motivated and display enthusiasm for their company, its products and its distributors. It is important that they appear self-confident. Their leadership, management skills and bond-building activities will then be able to play the necessary part in motivating the distributor principal and the sales force.

Managing and Motivating Your Agents and Distributors This process calls for an understanding of the relationship, mutual SWOTs, mutuality of benefits and a commitment to working together for common goals.

- A creation of the right environment - nature, scope and style of operation
- Realistic objective setting, review & control
- Joint development of campaigns

REMUNERATION OF THE SALESPERSON

Industrial selling is distinguished from other kinds of selling by 'customer penetration'. As a rule, when distributing a product for resale, the sale is made by a salesperson to the buyer or the merchant acting as their own buyer. Rarely does the sales executive have to 'sell' both the buyer and the owner of the shop, though a smart person makes sure that anyone who sells their product understands its sales points. In industrial selling, however, it may be necessary for the sales executive to persuade several people before walking out with an order. First, the user of the product has to be sufficiently interested to suggest to their immediate supervisor that this particular product be specified when a requisition is next placed; since few workers are capable of effectively relaying a sales presentation, the sales executive must also 'sell' the supervisor. After the supervisor requisitions the product, the matter may go to the works manager or the engineering department for approval, if it is sufficiently important. Again, the salesperson has to make sure that these executives understand the engineering advantages of the product. After being approved by the engineering or operating department, the requisition may travel to the financial controller, who approves the budgetary expenditure and passes it along to the purchasing department.

The buyer or the assistant mayor may not issue a purchase order at this point. After checking the price against competition, some similar product may be found which seems 'just as good' and may be cheaper. So, unless the sales executive is on the job, the requisition may travel back to its point of issue to ascertain whether the cheaper product may not be acceptable. This

process is quite usual in industrial selling. In the case of equipment involving a considerable outlay of money, it may be necessary to 'sell' several executives and the board of directors. There are usually 'no people' in every organization, who may not actually have much buying authority, but who can, if not otherwise persuaded, wreck the sale.

REMUNERATING THE SALES EFFORT

Remuneration of sales executives always provokes a great deal of lively discussion whenever the topic is raised. So it should - it is an important motivational factor as far as the salesforce are concerned. Companies use various methods to calculate the amounts paid to their salesforce, depending on their number or the products they sell or other factors. However, any method of remuneration must be of mutual benefit to both the sales executives and the company employing them; if either party feels that it is 110t getting a fair deal, then the association will eventually, if not immediately, break down. A sales executive who is dissatisfied with the remuneration, will leave the company. While a company that is unhappy with the salesperson's performance, in view of their total costs, it may discharge him. We will briefly examine the methods of remuneration in current use.

Salary Only

A salary, however high, does not provide the incentive needed for extra effort when it is necessary. This arrangement is preferred by the salesforce when the salary is high, but the cost may be too high for the management to accept. It may be a good idea when large capital plant is being sold, but in that case the selling may well be handled by a senior employee, whose incentive would perhaps be an equity holding in the company.

High Basic Salary Plus Bonus on Trading Profit

This method is a little better than the previous one from the incentive point of view. But sales executives tend to be impa- tient people, and they are not usually prepared to wait for a year or so before knowing whether they are going to get a bonus.

Therefore the advantage is slight. Also, too many intangible factors affect the bonus payments and many of them are not controlled by the salespeople. While the salesforce in the field may have done extremely well, the orders may be fouled up by a strike in the factory or an extra large payment may be made to a departing chairman, depleting profits; such happenings could cause justifiable dissatisfaction among the salesforce.

Commission Only

This can create insecurity, especially with new recruits. If they have family responsibilities, and cannot obtain orders quickly enough, it can create dishonesty, which does not do either party any good in the end. If a company with a wide range of products pays its salesforce on a commission only basis, the sales executive will only sell what they wish to sell and are good at selling. Those products may not be the ones the company wants pushed. A salesperson doing well on a commission only basis can still feel insecure. If the performance is too good, the company may decide to take on someone else, thus effectively reducing their territory and their earnings. This naturally has a dampening effect on their selling capacity. A company cannot effectively control and direct the effort of a sales force paid on a commission-only basis except by harsh measures, which may be undesirable.

Low Rate of Commission Plus A 'Liveable' Basic Salary

This method is the most widely used in industrial selling. This is quite satisfactory for a one product or one product range company, but problems appear when the company expands or increases the sales force. The sales executives are not interested in establishing new lines or in the expansion of the company's activities.

Continuous Incentive Bonus Scheme

The total remuneration should be made up of a liveable salary and a bonus, in a predetermined ratio, say 80 : 20. The company must have a master plan with its aims and expectations clearly defined. At the beginning of every financial year, the company should set out, in the form of an overall company sales target:

- the total sales target for the next twelve months;
- the target for each salesperson in that achievement;
- the share of the total sales target to be borne by each product range, particularly if a multiplicity of products are to be sold.

It is one of the functions of senior management to determine the target proportions carried by each product range and it is one of the sales executive's major functions to attain those objectives. It is vital that the salesforce sell the product range that makes the highest gross contribution to the company profit. Others may be easier to sell, so incentives should be tied to selling those lines which enhance the bottom line of the business and maximize the return on capital employed, which is the true measure of the company's success. The continuous incentive bonus scheme is designed to inform the salesperson exactly what is required of them in the year ahead and what their rewards will be if the objectives set are attained. This ensures that the goods are sold according to the overall company targets and in the right product range proportions.

Setting Sales Targets by Broduct Range

In this example, nine points are allocated to general work. This covers punctuality, grooming, accuracy of records, etc. The percentage of target achieved, up to a maximum of 100 per cent, but not beyond, will qualify for that percentage of points allocated to the product group target; i.e. 75 per cent achieve- ment of product range A target above qualifies for 75 per cent of twenty points, equal to fifteen points. In the case of general work, points received will be based on the recommendation of senior management.

At the end of the period, the points achieved per product range are added up and a total arrived at. A bonus is then paid according to a previous scale laid down, e.g. (for twelve months) it may be as given in Table

	$
95 points and above	1500
earns	750
85 - 94 points earns	375
75 - 84 points earns	nil
74 and below earns	

It should not be necessary to point out that a sales executive does not qualify for a bonus unless all the product ranges are sold, not just a few. The executive should be kept informed of progress by the regular issue of progress information. This scheme combines flexibility with a fixed basic method and level of bonus payment. It can cope with changes in territory or in targets. Product range F may be more important than product range B, even though the target is lower; the profitability may be higher or it may be a new product. Therefore, the former may carry more points than the latter.

Note that :

1. Sales should be equal to invoice sales less credits.
2. All sales targets must be achievable, for the system to work, so management must plan ahead with due care.
3. The scheme can be operated by the company over any time period, viz., twelve, six, three or even one month.
4. The scheme is not difficult to operate and makes use of paperwork, such as invoices, which should already be produced by the company.
5. Sales costs could be significant (total costs against net sales turnover). The cost depends on marketing objectives and other factors which should be considered before costing.

Finally, while remuneration is the most important motivational factor for sales executippves, job satisfaction, security, etc., also count. Remember your salesperson's role:

To maintain personal contact with customers and buyers for the purpose of obtaining sales.

Risk Management

Good management is all about anticipating events and planning for action before the events happen. This is where understanding the sorts of risks which are likely to arise is very important. The risks may be of one or more of the following types:

1. The usual product risks, political risks, economic risks, etc. that exist in any international marketing operation - these are not being explored here.
2. A chosen channel member may turn out to be a misfit. This is where careful planning and selection of the right partners is vital. A good channel member of yesterday may not be a good channel member tomorrow. A mutual understanding of the roles of the channel members and their

responsibilities to each other is a must.

3. At least one channel member is not pulling their weight. The performance expectations must be made clear right from the start. Mutual monitoring of performance is vital to the continuing success of the ‘venture’. Mutual reliance

must be recognized. All campaign planning must be undertaken jointly so that no motivation is lost due to inadequate planning.

4. Breakdown of the 'relationship' - where independent members form a significant part of the channel, the relationships are based on individuals, their interpersonal behaviour, trust, mutual understanding of a set of common objectives and other objectives based on the needs of the parties concerned. 'Mutuality' of interest must be maintained to avoid the risk of damaging the position of the two parties.

In all these cases, rapid contingency planning is crucial to safeguard the company's position.

ELEMENTS OF DEALER MOTIVATION

- The trade margin
- Special incentives
- Harmonious relations
- Effective communication

DEALER MOTIVATION

The firm should constantly motivate its dealers lists the elements of dealer motivation.

TRADE MARGIN, A MAJOR MOTIVATOR

An attractive trade margin is no doubt a key element in dealer motivation. After all, the primary objective of any dealer is to earn an attractive return on his investment. We have discussed the issue of trade margin in detail in the earlier paragraphs.

Motivational Elements Other than Trade Margin

Trade margin though important, is not everything in dealer motivation. The firm can use several other elements in enthus- ing its dealers.

DEALER INCENTIVES

Besides an attractive trade margin, the firm should provide some special incentives to the dealer so as to win him over and sustain his loyalty to the firm/ brand. Sustaining dealer loyalty is the sure route for obtaining optimal retail thrust for the product/ brand. Special incentives like quantity rebates, off- season rebates, gifts, cash incentives, etc., can be used for motivating dealers.

With increased competition, companies are now increasingly realising the role of such incentives. One measure that seems to be catching the fancy of companies is fully-paid vacations for dealers. Companies are also hosting lavish dealer meets at exotic places. For instance, ITC has been taking out whole groups of its dealers on a safari to Kenya. Godrej-GE last year flew over 40 of its best dealers to the US and Videocon sent around 650 of its best dealers to Europe. Even companies, which were giving cash or gold sovereigns as incentives earlier, now seem to have realised the potential of travel abroad as an incentive. The tours are consider- ably expensive, since the companies try to ensure that they become unforgettable outings for the dealers. The companies concerned seem to spend on an average more than Rs 40,000 per head on dealer holidays. Godrej-GE, which is one of the big spenders on dealer incentive tours, has an annual budget of around Rs 4 crore for this purpose. As the demand for such tours has been going up, some travel houses have started special divisions for corporate dealer incentive tours.

Harmonious Relations and Cooperative Endeavor Harmonious dealer relations are another important element in dealer motivation. Frequent visits to dealers' shops by the field sales force of the company/ stockists helps harmonious dealer relations. Dealer meets too facilitate this process. They help to exchange ideas and to generally bring the dealers closer to the company;

Dealers need understanding and support. They are happy to receive sales ideas from the salesmen and executives of the firm. Likewise, helpful and prompt attention to dealer complaints.

Associating the dealers in various campaigns such as service campaign, promotion-campaign, etc., will cement relations with the dealers. It will also add to the success of the campaign. =

PHYSICAL DISTRIBUTION CONCEPTS AND OBJECTIVE

Physical Distribution, Marketing Logistics, and Supply Chain Management

DISTRIBUTION/MARKETING LOGISTICS

Physical distribution is the process of delivering the product to the marketing channels and consumers. It encompasses the various activities involved in the physical flow of the product from the producer to the consumer.

Marketing logistics is somewhat larger in scope compared to physical distribution. It covers physical distribution plus a part of the task of marketing channels. While physical distribution takes care of functions such as transportation, warehousing and inventory management and facilitates the flow of the product, marketing channels actually connect the firm with its customers. Marketing logistics covers physical distribution in full measure, plus a part of the function of marketing channels. Marketing logistics bring in greater value addition in the delivery chain, beyond mere transportation or distribution.

The Physical Distribution Concept

This emphasizes the connection between costs and service levels and aims to minimize the total distribution costs at a given service level, when backed by an integrated logistics network. Its four main components are:

1. The total cost approach: this considers all the costs of the physical distribution network, visible and invisible, while trying to achieve a given service level. It is necessary to remember the interdependence of all these elements and to try to minimize the total costs instead of attempting to reduce them piecemeal.
2. Trade-offs in costs: certain costs may increase while others are being reduced, but the objective should be to reduce the **total** distribution costs.
3. Minimum sub optimization: owing to the interdependence of all the distribution functions, any change in one will affect the others. When these functions are integrated, the goal should be to minimize sub optimization through systems management.
4. The total system perspective: this takes the concept a stage further by considering the costs in the entire marketing process from the beginning to the sale to the end-user,

For example, instead of the retailer pricing the goods received, which is a time-consuming and therefore expensive process, the retailer can provide the manufacturer with up-to-date price lists, the manufacturer can price the products and charge the retailer for the service; the result being lower costs in total.

SUPPLY CHAIN MANAGEMENT (SCM)

SCM is larger in scope than both physical distribution and marketing logistics. It encompasses materials management task as well. Supply chain actually refers to the whole business chain, encompassing procurement of inputs, in-bound logistics, conversion of inputs into products, physical distribution/ marketing logistics and channel functions, which finally take the end product to the ultimate consumers Essentially, SCM can be viewed as the combination of materials management and end product distribution, which constitute the two vital compo- nents of the business process and form the key tasks at the front and back ends of the process, respectively.

It can be seen that the supply chain is in effect the firm's value chain. Value is actually spread through the firm's supply chain. A firm can optimise its total customer value by managing activities in the supply chain in an integrated manner, treating them as one continuous chain. The supply chain constitutes a value delivery network. That is why it is often said that firms compete in the marketplace using their supply chains as the weapon, not their products and brands. Superiority in supply chain is thus a major competitive advantage. A firm with the better supply chain wins in the market. We have discussed the value chain concept in detail in the two chapters on Industry Analysis, and Competitive Advantage.

Taking note of the advantage in dealing together materials management and physical distribution of end products, which constitute the two major functions at either end and which form a virtual chain permeating the business from end-to-end, many experts have preferred to combine the two subjects and deal them as SCM.

The SCM approach, no doubt, has some merits. It facilitates the integrated handling of the functions of the business, especially the procurement function and the logistics functions at the front and the back ends of the business. As a result, it comes handy in value creation! value addition.

The approach, however, has a strong demerit as well. It gives prominence to materials management and treats the customer requirements of logistics as an appendix to the business cycle. The requirements from the side of the customer/ market get diluted in such an approach. Moreover, in the nature of things, the focus as well as requirements of materials management and physical distribution of end products are somewhat different from each other. Perhaps all things considered, the two subjects should be studied independently, rather than as one unified subject.

In this text, we shall in any case avoid the SCM approach. Mer all, in a marketing text there is no scope for discussing materials management. We shall confine ourselves to distribution of end products. We shall, however, make a slight deviation from the traditional way of handling the subject. Instead of treating it merely as a physical distribution task, we shall treat it as marketing logistics.

MATERIALS MANAGEMENT

The materials management cycle consists of the inflow of goods through materials acquisition whether it is by outright purchase or partially or fully on credit basis, plus internal transport and inventory management. The relevant strategies regarding purchasing, transport and warehousing must include cost-effective methods in these functions. The materials flow Involves vendors and suppliers, and is integral to the operation of the business, Purchasing forecasts are directly based on production schedules or other internal usage plans, highly integrated materials management is possible given a disciplined internal planning process.

The logistics activity in a company acts to co-ordinate the flow of material and the related information through the system. It has to co-ordinate production planning; delivery frequencies required to match sales demands and customer order frequen- cies. All this has to be achieved through shared information. This requires an integrated information system in which:

1. Data entering one subsystem is also available to any other subsystem requiring it; for example, data concerning customer orders should be available to inventory control, production scheduling, sales forecasting, etc.
2. All inter-related subsystems should have access to data in a common data base.
3. Closely connected activities are integrated into the same procedure, order processing, credit checking and stock allocation.

A high degree of sharing of expensive capital equipment should be allowed for; for example, the central computer installation, the data base and the application packages, among others, can be shared among the various functions.

The logistics information system consists of two subsystems dealing with supplies and customers. The supply subsystem input consists of the materials requirements plan, indicating how many of what types of items are needed und when they are needed for production; this has to be checked against the standing inventory and any orders outstanding. If necessary, sources of supply for any extra materials needed will have to be decided upon and purchase orders generated. This process appears simple but a company may have a register of hundreds of suppliers and maintain an inventory with many thousands of stock-keeping units. Also a sharp look-out must be kept for possible shortages and the suppliers checked for their reliability, prices and service. At the same time, the inventory must be minimized while making sure that production is not held up due to a stockout. It is obvious that a sophisticated information system is necessary to balance all these factors simulta- neously.

In many ways, the customer subsystem is the mirror image of the supply system. An order from a customer is the start of the process. Hundreds of such orders per day have to be moni- tored against customer records for creditworthiness and special terms or needs, among other things. After which stock has to be assigned to the order, replenishment of inventory catered for if necessary, delivery and invoices as well as other comple- mentary activities arranged for, A host of other information regarding achievements of service levels, re-order levels, etc., has to be gathered at this point to assist in making demand forecasts.

These two subsystems come together in the manufacturing function and have to be integrated through production control so that the supply sub system generates what the customer subsystem demands. Many companies have installed materials requirements planning (MRP) systems. Basically these forecast the components and materials needed from the company's master production schedule (MPS) and the bill of material (BOM) for each end product. The requirements are calculated by taking existing stock levels and orders already placed into account, as well as the times when the items will be needed and the supply lead times. A successfully implemented MRP system can reduce inventory levels, speed up changes in the production process to meet changes in demand and increase the level of service in meeting demand. The basic idea is simple but the control of such multiple activities has only become possible through the use of advanced computer technology.

Other methods such as the just-in-time (JIT) system can reduce inventory levels while maintaining service levels. The idea is that the materials needed should arrive just in time for their use in manufacture. Reliable lead times are necessary for these systems to work properly. A similar development in the distribution field is the distribution requirements planning (DRP) system. This starts from the demand for the finished product and produces requirements schedules at each level of the distribu- tion chain. This is a 'pull' system in that the end demand 'pulls' the required products down the chain rather than a centrally decided production plan 'pushing' the products down the line. Since the emphasis is now on customer needs, the former makes more sense than the latter, though both have their advantages.

The latest innovation is a combination of the MRP and D RP systems into logistics requirements planning (LRP) systems, which will link the end demand through the whole chain back to the suppliers. This has a number of complex requirements which must be satisfied before such a system can be contem- plated, including a high degree of dedication on the parts of the management and the whole organization.

Importance of Physical Distribution/ Marketing Logistics

Physical distribution/ marketing logistics forms a pivotal part of the marketing task.

CONFERS PLACE AND TIME UTILITY ON PRODUCTS

It is physical distribution that confers place-utility and time- utility to a product by making it available to the user at the right

place and at the right time. Thereby, it maximises the chance to sell the product and strengthen the company's competitive position. If any product made in any place could be consumed in its entirety at the very place of production and at the very time of production, there would be no need for physical distribution of that product. But such products are very rare. In practice, almost every product gets consumed at places and times that are different from those of their manufacture. They have to be carried to places of consumption; they have to be stored; and they have to be distributed.

Order processing

Order processing is the receipt and transmission of sales order information.

A. Efficient order processing facilitates product flow.

B. There are three main tasks in order processing.

1. Order entry begins when customers or salespersons place orders by mail, telephone, or computer.
2. Order handling involves several tasks.
   a. Transmission of orders to the warehouse
   b. Verification of product availability
   c. Checking of prices, terms, and customers' credit ratings
   d. Instructions to the warehouse to fill the order
3. Order delivery
   a. The warehouse schedules pickup with an appropriate carrier.
   b. Premium transportation is used if the customer is willing to pay for rush service.balance between cost and service levels

Transport

Transport is an important part of logistics since inadequate transport provision can increase inventory costs prohibitively, as well as the investment in inventory; it can also cause customer dissatisfaction and increase the invisible costs dramatically.

Therefore the selection of the right mode of transport, which is efficient and dependable, is essential for the achievement of distribution objectives. The five modes are: rail, road, sea/ waterways, air and pipeline, plus combinations of some or all of these. The possibilities must be considered for cost, reliability and possibility of risk/ damage.

Warehousing

This can be either company-owned or leased/ rented from others. The advantages of company-owned warehousing are: greater flexibility and control, better information feedback and potentially lower unit costs. Regional distribution centres serving regional markets are a new development in the Europe of today; if they are highly automated and can cater for packaging of orders, maintenance of full inventory and combining products from different production centres, they can go a long way towards achieving improved efficiency and increased customer satisfaction. For example, some companies are considering locating regional distributor centres in Maastricht in the Netherlands, Calmar in Alsace and in Bavaria. These regions are also developing the type of infrastructure needed for the functioning of such centres.

The advantages of leasing are: location and space flexibility, and possibly lower costs for seasonal businesses. There is also wider choice available for the type of warehousing needed, e.g. special commodity warehouses for storing agricultural products or refrigerated warehouses. Warehousing firms may also offer a variety of extra services to compete with each other.

It is possible to reduce the need for warehousing by choosing a slower form of transport, e.g. storage in transit. The number and location of warehouses is decided by their purpose and the level of customer service to be provided. They should be so positioned that they will yield the desired service level after all the variables are considered. This solution is unique to each business. The transportation costs decrease as the number of warehouses increases; while the inventory and warehousing costs increase at a diminishing rate.

The locations of the warehouses affect the customer service level and the total costs; they also have a significant effect on the

competitive powers of the business. A number of models have been developed to help management make better decisions.

The significant factors are the estimates of lost sales due to the distance of the warehouses from the customers, and the costs of operation and of transport.

Inventory Management

Inventories may be held in the material management cycle to supply the production function or in the distribution function to meet customer demand. Inventory control in the latter is crucial to efficient physical distribution. Inventory represents the largest single investment for manufacturers of packaged consumer goods, amounting up to a third of their asset investment. High inventory levels are necessary in competitive conditions where the market segments are diverse in nature and customers are used to obtaining goods quickly.

The objective of inventory control is to minimize total inventory costs subject to demand and service level constraints. The main costs are due to holding inventory, ordering and the risks of stockouts. The system has to figure out how much to re-order, when to re-order and how to control stock outs at the minimum cost.

There are a number of inventory control systems available, depending on the type of business. Distribution requirements planning (DRP) systems deal with connecting the production process with the other inventory levels further down the channel. They operate on the assumption that they are manag- ing inventories intended to resupply other inventories.

An accurate forecast of future demand is obviously essential for any inventory control system, Lack of such a forecast or inaccuracies can wreck havoc throughout the physical distribu- tion channels. Unpredicted increases also cause stockouts and loss of orders in the future, Every firm and every channel member has to balance the costs of holding higher inventory levels against the costs of stockouts.

roduction Control and Materials Requirement Planning

These, together with purchasing and raw materials handling, are generally grouped under the materials management function.

Sometimes the objectives set by the management for these functions clash and cause a drop in the level of the customer service and/ or a rise in physical distribution costs as a whole. Production is the focal point of all this activity, because production levels determine the needs for raw materials, parts, etc., and also the amount and types of finished products, which in turn influence the delivery times and modes for the distribu- tion function.

Materials management is the 'single manager' organization concept embracing the planning, organizing, motivating and controlling of all activities and personnel principally concerned with the flow of materials in an organization. If the physical distribution concept is adopted by a business, it is usual to combine all activities concerned with raw materials under a single manager, who is sometimes also responsible for production scheduling. These activities are similar to those concerned in physical distribution of finished products, the difference being in the materials handled and their recipients.

JUST-IN-TIME (JIT) LOGISTICS SYSTEMS,

This is a logistics system by which materials arrive at the point of use just in time, thus saving on inventories "and warehous- ing. Their implementation affects the purchasing, transport, warehousing, production, quality control and data processing functions, and requires an amount of discipline which many businesses find difficult to create and sustain.

In order to be successful, it has to be operated by all channel members in a given channel. It calls for all materials to be part of the work-in-progress, without pausing to collect storing expenses. Each part of the manufacturing process has to get the right elements in the correct amounts just in time. JIT is found to work best in repetitive manufacturing situations where the suppliers are close by, the forecasts are accurate and there exist significant levels of inventory to start with. Significant cost reductions can be made if JIT is successfully applied.

PLANNING A LOGISTICS STRATEGY

Strategy for the logistics process requires the evaluation of possible physical distribution systems which meet the customer service standards required at the lowest possible cost. A system thus properly planned will increase the "response of the various elements in the process, the sensitivity to the distribution environment, knowledge of the possibilities of cost reduction and service optimization in the function, and the awareness of the effect of corporate strategy on the process.

The planning begins with deciding on the customer service strategies and goals, and goes on to the functions and invest- ment involved in physical distribution, to decide on systems and procedures for the functions and then developing these strategies in human resource terms and implementing them. After this process is complete, the criteria for the selection of channel members have to be established. The performance of the strategy has to be monitored periodically and action for improvement taken if needed.

MANAGEMENT

Learning Objective

- To understand the main task in Transportation Management
- To understand Transportation requirement and optimization of mix of transport mode.
- How to control Transportation cost

Transportation

Transportation confers 'time utility' and 'place utility' to the product; it determines the company's customer service; it also has a crucial bearing on the other elements of physical distribu- tion and marketing, like warehousing, inventory control and channel management. Finally, transportation is also a very important cost element in most businesses.

Main Tasks in Transportation Management

- Main Tasks in Transportation Management
- Assessment of the transportation requirement
- Choosing the 'mix' of transport modes
- Deciding the routing
- Development of operational plans
- Implementation/ review
- Control of transportation costs

Basically transportation management involves decisions on:

- How much to move?
- When to move?
- Where to move?
- By what mode, or combination of modes to move? The considerations in making these decisions are:

a. the lead time for stock replenishment
b. sales expected in the territory in the intervening time
c. The normal cycles of inventory build up at the warehouse/ dealer points.

If a firm can estimate these factors fairly accurately, it can make the basic decisions on transportation. In a fundamental sense, transportation has to be based on the sales forecast. Decisions on when to move, how much to move and where to move will essentially depend on the sales forecast.

ASSESSMENT OF THE TRANSPORTATION REQUIREMENT

In the first place, a transport manager makes an assessment of the transportation requirements based on the sales forecast, sales plan and schedules. He also watches the actual sales performance vis-a-vas the forecast and updates the transporta- tion.

MIX OF TRANSPORT MODES

Depending on the product, the market and the cost factors, firms select the transport mode, or the combination/'mix' o

Routing has two dimensions: First, systematic assignment of territories to each production/ supply point; Second, the actual sequence in which a delivery vehicle should move and service the retail points. When a firm has more than one production location or supply point, it should clearly demarcate the marketing territory to be serviced by each location. Similarly, for each warehouse/ stockpoint too, it should demarcate the territory. Transportation effectiveness depends very much on systematic assigning of territories to each source. When there is a strong need for drawing supplies from a source other than the designated one, it can be done, but only on the basis of strong justification.

Secondly, equal care should be taken in deciding the actual sequence a delivery vehicle should take in supplying stocks to the various retail points that come under its service territory. Intelligent routing, covering both the above aspects, is an integral part of effective transportation. Optimisation of transport lead, reduction of transport time and optimization of costs are the objectives in effective routing.

DEVELOPING OPERATIONAL PLANS

The transport manager must work out detailed operational plans from the overall transportation plan. Detailed plans/ schedules must be developed for each product and each supply point/ warehouse, month-by-month and week-by-week. The plans must indicate the made/ combinations of modes. They must also be properly dovetailed with the warehouse plans.

Once the plan in all its details is ready, the task becomes one of creating the required transportation capacity and securing the required linkage between transportation schedules and wan house space procurement.

IMPLEMENTATION OF PLANS

The transportation job does not end with the preparation of plans, the determination of optimal modal mix, development of operational plans and putting in place the required service contracts. In fact, it begins there. The smooth movement of the product and efficient execution of the whole plan, with minimum deviation, is the real task. Many practical problems may crop up in the process. Sometimes, transport capabilities

CONTROLLING TRANSPORTATION COSTS

As mentioned earlier, transport cost is a major element of distribution costs in most businesses, and it has been increasing constantly in recent years. As such, it is essential that the transportation costs are controlled tightly. Also, this has to be done without sacrificing the minimum guaranteed distribution service level to the channel and consumers. Saving in transporta- tion can be realised by: (a) optimizing the mix of the transport modes, (b) reducing the transport lead and the lead-time through effective routing and other means, and (c) eliminating multiple and wasteful transfer, and handling of products. The transport controller has to have an overall appreciation of the whole range of physical distribution activities and the costs thereof. He cannot remain confined to the narrow role of freight rate negotiator, or a transport liaison man. He has to view transport as a total back-up capability, supporting the marketing function and a source of competitive advantage for the firm in the marketplace.

Warehousing

Warehousing is the major component of physical distribution. Warehousing management has two distinct and equally important parts: (i) the physical job of creating and running the network of storage points, and (ii) the managerial task of controlling inventory levels without sacrificing service levels.

Though interrelated, they require separate and detailed discus- sion. We shall, therefore, devote two independent sections to the subject. In the first, we shall deal with the warehousing aspects and in the second, with the inventory management aspects.

DESIGNING A WAREHOUSING SYSTEM

In most cases, products flow from the factory to the consumer through a long winding chain, consisting of multiple tiers of warehouses and multiple tiers of marketing intermediaries. In designing a warehousing system, the following basic questions relating to this flow become significant.

- How many warehouses should we have?
- Where should we locate them?
- What should be the size or capacity of each of them?

THE COST-SERVICE TUSSLE

When we look closely at these questions, two interesting, but conflicting, points emerge. Salesmen and channels always plead for greater convenience in delivery and consequently more warehouses. But, maintaining a large network of warehouses is a costly proposition. Thus, there is an inherent tussle between cost and service in warehousing decisions.

WAREHOUSING TO BE TACKLED AS PART OF THE PHYSICAL DISTRIBUTION SYSTEM

While designing a warehousing system, the fact that warehous- ing is a part of the overall distribution job should be borne in mind. The warehousing design should fit smoothly into the overall distribution design, which includes physical distribution elements like transportation plus channel arrangements, which will be discussed in the succeeding chapter.

WAREHOUSING, A PARTLY FIXED AND PARTLY ADJUSTABLE ENTITY

In most cases, it may be apt to view demand in a given territory as consisting of a constant component and a transient compo- nent, which is to be added to or subtracted from (mostly added to) the constant component. Past sale corresponds to the constant component. Changes occurring in demand in the current period correspond to the transient component. The transient component is related to change in market demand per se, or company demand (a company may lose or gain relative market share). Thus, in the nature of things, warehousing will have a constant component plus a variable component. And, there is some scope for adjustment in warehousing of prod- ucts, depending on market behaviour/ company's performance.

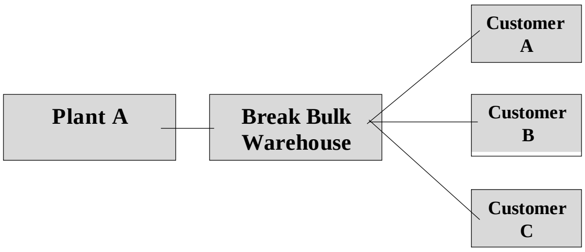
WAREHOUSING JOB CAN BE TAKEN CARE OF IN DIFFERENT WAYS

As regards the actual organising of the warehousing system, different alternatives can be considered by the firm.

- Hire warehousing service from public warehousing agencies
- Own the godowns and manage warehousing through company staff
- Entrust warehousing to C&F agents/ stockists/ distributors
- A combination of the above

Each alternative has its associated merits and drawbacks. Decisions have to be basically situation specific. FMCG (Fast Moving Consumer Goods) firms usually transfer a large part of the warehousing task to their C&F agents.

WAREHOUSE BENEFIT BREAK BULK OPERATION



Determining the Number Location and Size of Warehouses

Determining the locations and capacities of the warehouses is the crux of the task. On this depends the firm's customer service level, its competitive advantage in distribution and its inventory cost structure. While one might point out that it is the inventory turnaround that primarily determines inventory costs, the fact remains that the costs are also influenced by the locations and spread of the inventories -at how many places and in what sizes are stocks kept. Moreover, inventory turn- around itself is partly the outcome of the manner in which the inventory is spread.

Determining the number: The optimum number will depend upon the nature of the product, the size and geographical spread of the market serviced by each warehouse. the current and potential sales in the territory, the extent of seasonality of demand if applicable, the level of peak demand, the trade patterns, the number of distributors/ retail outlets to be serviced by each warehouse, the acceptable order-execution time, the possible speed of replenishment of stocks and the cost involved in operating warehouses. Future requirements and pattern of competition are also relevant factors in deciding the number and sizes of the warehouses.

Choosing the size: The decision on the size of the warehouses must be taken in alignment with the decision on their total number. After a firm assesses the sales potential in each warehouse territory, the question to be decided is: What is the optimum inventory holding needed for realising the sales projected for the territory?

Warehouse size and costs are inversely interrelated. So, as a general rule, small-sized warehouses are uneconomic compared to larger ones. At the same time, if the sales projected are small, warehouse size has to be small. Customer convenience and channel service will call for a large number of small-sized warehouses spread extensively all over the marketing territory.

There will also be the additional consideration of future requirement. As a general rule it can be said that by reckoning the volume of sales and the desired market share in the area

IMPLICATION OF SUPPLY CHAIN MANAGEMENT IN PHYSICAL DISTRIBUTION

What is Supply Chain Management?

A supply chain is the set of entities that collectively manufac- tures a product and sells it to an endpoint (the ultimate customer). In this sense, supply chains are like value added chains. However, they include only players that add value in production and distribution. The concept of a supply chain is narrower than that of a value-added chain, but it is broader than the idea of marketing channels. These go from factory to buyer. A supply chain goes back to a more distant starting point-the suppliers of the factory that makes whatever is being sold-and the suppliers of the suppliers. Indeed, the beginning point of a supply chain is somewhat arbitrary, although it

usually is considered to include only the immediate suppliers of the factory that produces finished goods. A supply chain is also distinctive in that it ends with the ultimate buyer, the customer of someone's customer. The end of the supply chain is the last invoice.

In practice, much of what is called SCM does not go all the way forward to the last invoice, nor backward to the suppliers of suppliers of manufacturers.

A good working definition of SCM is that it is an organizing concept that starts with customer service and argues that this results from the cumulative efforts of the entire channel.

Customer service cannot be interpreted as the sole responsibility of any single channel member. The guiding principle is to unify product flows and information flows up and down the production and distribution chain. Doing this requires

An organizing concept, a statement of principles, a focus on end customers, channel management, and logistics—critics charge, with some fairness, that SCM needs a "more precise definition. Yet, SCM is not really a package of techniques, it is akin to a paradigm; that is, a set of common values, beliefs, and tools that unites a group of people engaged in related tasks.

Any paradigm has subfields, and SCM is no exception. A number of concepts and techniques can be folded into SCM, and we will treat these as we encounter them. Let us begin with the roots of SCM in the grocery industry.

EFFICIENT CONSUMER RESPONSE

Efficient consumer response (ECR) is a landmark in marketing channels. As a movement it has wrought radical change in the U.S. grocery industry, and that change is spreading to other sectors and other countries. Its success is surprising, given how different it is from the usual operating methods of most channels. Indeed, ECR is so successful that some critics are now declaring it outdated and looking for a new movement to replace it.

The source of ECR is fear. In 1992, the U.S. grocery store industry was feeling threatened by the rapid growth of non grocery outlets, such as drugstores.23 these “alternative format” (alternative to a supermarket) stores were aggressively adding food to their assortments, and the consumer was responding positively. A principal threat was seen to be Wal-Mart, which was moving from mass-merchandising to a hypermarket concept (merchandise and groceries). This is why, in 1992, two grocery trade associations commissioned a study of grocery methods. The report strongly criticized existing grocery channels and proposed a radical and complex series of changes to these channels. This program of change was named according to its objective: to achieve efficient (as opposed to wasteful) consumer (the final buyer) response (supplying only what is desired).

As initially proposed, the idea is to focus on four areas where the industry as a whole had and still has great potential for improvement. How great? The United States grocery industry converged on an estimate of $30 billion annually, or 5 percent of retail sales. Interestingly, a similar figure (£21 billion, 5.7 percent of retail sales) is being suggested for European grocers.24 The four areas are

1. A continuous replenishment program (CRP). The goal is to end the bullwhip effect. The method is to use purchase data captured via scanners from the final buyer to inform all upstream supply chain members of demand, right back to the suppliers of suppliers. This requires massive standardization of codes and methods, and implementation of ED!
2. Efficient pricing and promotions. A scourge of the industry is poorly calibrated promotions that wreak havoc with pricing and buyer behavior. At the consumer level, excessively generous promotions (such as one free for one purchased) create demand spikes and degrade brand equity. Non-targeted promotions encourage price comparisons and brand switching purely for temporary price cuts. At the wholesale level, manufacturer promotions lead to huge demand spikes. These push factory production up too high, then down too low. This, in turn, pushes inventory up too high (resulting in spoiled food) or down too low (running out of stock).
3. Changes in product introduction. Thousands of new- product introductions, most of which fail, are endemic to grocery retailing. ECR calls for combining market research commissioned by channel members in order to forecast

new-product success better on a store-by-store basis, or based on reasonable store groupings (store clusters).

4. Changes in merchandising. This is the same idea (combine research) for the purpose of finding better ways to merchandise brands and their associated categories (e.g., snack foods, pet food, soups) store by store, or cluster by cluster.

Over time, these ideas have been developed and expanded. ECR has become an umbrella term that now encompasses a variety of means by which pure grocers combat alternative format stores. Some major operational features of ECR follow.

Category Management and Efficient Promotions: Histori- cally, grocers think of what they sell in terms of how they buy: one brand of one type of item (e.g., Frito-Lay Taco Chips).

Category management is the principle that a higher level of aggregation is called for. A consumer's shopping list is com- posed of product categories ("remember to buy two bags of salty snacks"). Therefore, a grocer should think in terms of a product category, and manage it as a whole, rather than manag- ing each product-brand and letting the collection of items amount to a category. Further, in the spirit of ECR, retailers and suppliers should work together to understand each category's dynamics as perceived by the consumer.

The rationale is that any item competes with any other item for shelf space. Consumers think in categories, and some as a whole merit more space than do others. Depending on the store, the diaper category, for example, may merit (on a contri- bution per-space basis) more space than it is getting, whereas the laundry detergent category might merit less. This conclusion may not emerge from analyzing items one by one. And what should be in a category? The principle is to look for groupings that seem natural to a consumer. Thinking in category terms is made easier by advances in activity-based costing (ABC). The cost of slow-moving items is often surprisingly high, and ABC helps point out these items.

The category management focus is related to the idea of an efficient assortment: Having what the customer wants and skipping the rest. For groceries, skipping the rest is of great importance. It is widely believed that brand managers have proliferated SKUs to lock up shelf space and brand share, with the result that consumers are overwhelmed with unsought variety. For example, P&G claims that in the laundry category 40 percent of SKUs could be eliminated, yet 95 percent of consumer needs would still be met. Some manufacturers believe that having fewer SKUs actually increases overall sales.26 this paradoxical observation might be explained by the idea that buyers aren't motivated to sift through multiple options in

low-involvement product categories. Bewildered by more variety than they want, consumers depart with fewer purchases. A simplified display enables faster information processing, thereby increasing consumer confidence and motivation to purchase.

Category management sparks thinking about efficient promo- tions. These can be defined as limited-time offers that are win-win for all parties. This means that they

This third objective masks the real concern of many manufac- turers: that their promotions do not offer value to their brand-loyal shoppers, nor do they build brand loyalty within the segment of consumers who rely solely on promotions to decide what to buy.

Efficient promotions use data about consumer behavior to discover what is selling, at what price, and to whom. Retailers, wholesalers, and manufacturers work together (often by commissioning a market research firm) to make sense of reams of transaction data or market research data. The purpose is to discover win-win promotional opportunities for a store or a cluster of stores. For example, in Italy, manufacturer Kraft Jacobs Suchard and retailer Groopo GS have jointly analyzed loyalty card data to target consumers in a single attitude-based segment labeled "seeking healthy relaxation." As the label implies, it is no easy matter to identify these people. Similarly, in Spain, manufacturer Elida Faberge and retailer Auchan have jointly analyzed panel data to identify a mutually interesting growth opportunity: susceptible consumers who are secondary customers of Faberge and who are secondary shoppers at Auchan.

Continuous Replenishment: Continuous replenishment planning (CRP) is the practice of replacing stock based on speedy knowledge of consumer "withdrawals" (Le. sales). More precisely, in SCM the term means partnering between distribu- tion channel members in order to replace the traditional practices (push systems, stocking to forecast) with a pull system. In this pull system, a retailer's stock is replenished based largely on actual sales data from the end of the supplier chain (the consumer).

The goal is to automate the process related to warehouse fulfillment and shipping, using consumer demand (captured by scanners) to trigger just-in-time restocking. By automating, ECR practitioners seek to cut errors and processing costs, which are substantial. For example, British grocer Sainsbury's estimates that one-quarter of the chain's supply chain management budget is spent confirming the location and movement of inventory.

Continuous replenishment is an arduous task. In CRP, a supplier (perhaps a distributor, perhaps the manufacturer directly) takes complete responsibility for monitoring and refilling the retailer's inventory. In the grocery industry, CRP is often accomplished by charging the manufacturer with manag- ing the downstream channel member's inventory. In most of these cases, powerful retailers have obliged manufacturers to make the significant expenditures necessary to perform continu- ous replenishment. Intriguing, albeit preliminary evidence suggests the biggest winners of this exercise are consumers (lower prices, fewer stock outs) and retailers (higher profits).

The profit benefits for manufacturers are somewhat difficult to document. Although many report sales increases, they also find that significant logistical complexities and costs have been moved back to their level. As oil industry analyst notes, just-in- time (JIT) often becomes just inventory shift (JIS). Perhaps the biggest benefit of CRP for manufacturers is that they remain suppliers to large retailers. CRP keeps them in the game. It may or may not yield increased profits.

Obstacles to ECR: The list of obstacles to ECR is formi- dable.32 At a physical level, ECR requires agreement on codes and on a huge number of ED I choices. In general, it requires standardization of methods. For example, the delicate exercise of cross-docking is difficult to pull off if channel members cannot agree on a number of issues. ECR implementation is a long and expensive affair.

One of the greatest barriers to ECR is the necessity of trusting other channel members. Trust and good working relationships are necessary for the information exchange, joint planning, and joint actions that underpin efforts to make the entire grocery channel respond to consumers while cutting waste. And trust is essential for continuous replenishment. The idea of making another party responsible for one's own stock, and doing so without an abundant safety stock, is a very difficult one for many industries to accept.

Trust is based on equity. The fundament of ECR is not that channel members share risk and information to produce gains for the channel as a whole, but that they then share the gains equitably. Opportunism (reneging on a promise to compensate all players fairly) is fatal to ECR.

And yet, ECR exists. Although not the norm in grocery retailing in the United States, it has made great progress. If imitation is the most sincere form of flattery, sincere compli- ments of ECR abound. Trade publications of many industries overflow with discussions of how to create ECR in their sectors. For many, ECR has become synonymous with supply chain management, which is attracting considerable attention in Europe.

Demanding customers seem to create excellent supply chain operations-albeit painfully. The auto giants and1he major retail chains not only know what they want, they are determined to get it: delivery to a tightly specified time slot, in exactly specified quantities, at near-faultless quality; and "faultless" is extended to cover not only the products themselves but also the associ- ated planning, delivery, and invoicing systems. In these industries, that is now the entry ticket to the game, not a differentiator. And the word is spreading.

That ECR began in the grocery industry is miraculous. When the initiative was unveiled at a trade conference in 1993, few in the audience were confident that the traditionally adversarial relations in these marketing channels could be set aside. The cooperation and transparency that ECR requires had to be brought into being. The power of example is critical, and here the example used is the now-legendary arrangement between Wal-Mart and P&G (Chapter 11 on strategic alliances). Ironically, Wal-Mart's entry into the food business drove the grocery industry to devise ECR in the first place.

ECR also requires considerable change in the internal operations of a channel member. Jobs are lost and roles are redefined when EDI rationalizes supply chains. People representing many different functions in the organization (sales, marketing, purchasing, production, shipping, warehousing, accounting) must work together in project teams to create tremendous organizational change. And teamwork becomes permanent. Salespeople and purchasing agents, for example, are replaced by multifunctional teams on the buyer's side and the seller's side. And each side is expected to understand the other's business. These are wrenching changes.

Rapid Response

Rapid response, or what logisticians prefer to call quick response (QR), is another approach to supply chain management.34 It appears similar to, and is often compared with, ECR, but is really quite different. QR originated in the early 1980s in the fashion industry, in which it has seen its greatest development. Many of the original developments are attributed to Benetton, the knitwear retailer. Many of the later ones are due to Giordano, a retailer that perfected QR from the late 1980s to the early 1990s. Since 1993, Giordano's methods have diffused considerably in the industry and are now practiced by retailers such as Gap and The Limited.

In some ways, QR is like ECR. The fundamental pull system idea-let the consumer tell the entire channel what to make and what to ship, then do it quickly-is the same. And the emphasis on inter firm cooperation, data analysis, data transmission, inventory management, and waste reduction is the same. The fundamental difference is in the volatile, unpredictable nature of what is being sold. For FMCG (fast-moving consumer goods) categories, such as toothpaste, consumers know well in advance what they want and what they don't want. ECR enables them to tell the retailer and the suppliers readily.

In fashion, consumers don't know what they want until the moment they are ready to buy it. They don't know what will be fashionable and whether the next fashion will appeal to them. In fashion retailing, consumers see and try an item, then form an opinion. And they change their minds readily. Benchmarks are difficult to find, in part because of lack of standardization (e.g., of sizes) in the industry. Routinely, retailers put out a line of clothing, then. discover consumer reaction. If the sizes tend to run bigger or smaller than normal, the retailer will have the wrong size assortment. If one fabric or color or variation pleases more than another, retailers will find themselves with too much of one item and not enough of another. And fashion is perishable Consumers won't wait months for restock of a desirable item, and items that sell poorly must be marked down quickly in order to get rid of them at all.

Historically, store buyers forecasted fashion demand well in advance and committed to orders, sometimes six seasons before the items would be sold. This is a push system (make to forecast). Over time, consumer fashion tastes have become so difficult to forecast that many fashion retailers have adopted the opposite strategy: Try something in a small wav and see if it works. If it sells, stock more and quickly. But stock how?

Manufacturers need lead time. By the time fashion is discovered, it's too late to order up more.

Here is the impetus for quick response. The essence of QR is in manufacturing. QR involves keeping manufacturing flexible as to what to make and how much to make. In contrast, ECR is more focused on how much to make and when to put it into a ware house. There is no need to keep manufacturing flexible to produce variations of toothpaste, and there is little harm in stockpiling it for a while. Demand can be steadied (e.g., by restraining promotions). heading off production surges. But it is critical to keep clothing fabrication flexible to produce more of the latest hot dress or jacket, in this season's hit colors and fabrics, in the sizes that have proven popular. Production volume needs to be scaled up or down dramatically, and setups from one item to another should be quick. The items produced should be out the factory's door and to the customer rapidly.

Thus, whereas ECR focuses on shipments and promotions, QR focuses more on manufacturing. QR firms are heavy users of flexible manufacturing techniques. Computer-aided design and computer-aided manufacturing (CAD-CAM) occupy center stage in quick response programs. And a good deal of empha- sis goes into keeping the components flexible. Benetton, for example, is famous for waiting until the last minute to dye its wools, after receiving early information from pas (point-of-sale) cash registers about what colors are selling.

Much of ECR is about pricing and promotion. This does not figure at all in QR. The objective is always the same: Catch the fashion and charge highly for it. When mistakes are made, which should be a frequent event, catch the mistake soon and mark it down quickly-but modestly. Then mark down again what is left-quickly. In this way, drastic markdowns are reduced:

These become necessary to move out merchandise that has been around well after people realized they didn't want it.

In short, QR is not about merchandising and inventory. It is about manufacturing and timing. Another difference is that ECR always seeks to minimize transportation costs. This is fitting in FMCG: Toothpaste and foodstuffs are low-margin items' that don't pass out of style while in transit. Fashion goods are the reverse. Hence, many channel members in the fashion industry willingly airfreight the hot sellers-as soon as they know what those are and to save time, suppliers locate near designers and final points of assembly for the most fashion sensitive categories.

Net, ECR is about demand that consumers know they will have. QR is about demand that consumers don't sense themselves until they're at the point of purchase. Both are pull stems that respond to a consumer. But ECR focuses on being efficient (holding down physical costs), whereas QR focuses on being quick; that is, fast to produce what the market has just decided it wants.

Quick response is an objective. In general, the key is to have access to POS data, then to use the information to cue an array of shippers to pick up and deliver within a network of flexible factories. These factories can be individuals working at home. The transportation network shunts raw materials, work in process, and finished goods around through various steps design, pretreatment of fabrics, cutting, sewing, labeling, quality control, fulfillment of orders, shipment of packages. Firms have multiple suppliers, some of which act as backup systems, and others of which check on work in process.

These intricate arrangements drive off of POS data. Those with access to the data are in position to trigger frantic waves of manufacturing once a "winner" has been noticed. The speed required to respond to fashion puts a premium on EDI (for fast transfers), CAD-CAM (for changing what is being manufactured), excellent P_S systems, standing arrangements with members of the supply chain, and standardized identifica- tion. One of the most difficult challenges to QR has been implementing a standard system of universal product code (UPC) and scanning.3.5 In contrast, the grocery industry had already made great progress on this problem in the 1970s, making ECR easier in the 1990s.

Given the intricacy of the production process, QR puts a very great strain on the myriad fashion channel members, particularly the subcontractors in manufacturing. Trusting relationships and open information transmission are difficult to keep up among so many players. The uncertainty of the demand environment also puts a strain on the system, making it hard to issue guarantees.

Hence, some vertical integration is commonly used to achieve QR in fashion. It occurs in two functions: design of the merchandise and retailing. Design is wholly owned because it is the key to manufacturing. Retailing is wholly owned in order to have stores to serve as test sites, observatories, and transmitters of fast, thorough information. Benetton, for example, is largely franchised but keeps some stores under company ownership.

And with their stores, integrated providers such as Gap can quickly alter prices, raising them to stave off stock outs on surprise winners (while rushing more into production), or

lower prices early, before it is obvious to consumers which items are losers. This is quick response indeed.

How quick it has to be depends on how fashionable the goods are. The less demand is influenced by fashion trends, the more the supply chain looks conventional. For moderately priced staple clothing, for example, a hyper responsive supply chain is neither necessary nor profitable. A good system of regional warehouses will suffice to fill in surprise inventory gaps, and long lead times for production and transportation are employed to cut costs without penalty.

Putting it All Together: What is the Right Supply Chain?

To this point, we have discussed building blocks of supply chain management and have seen them put together in different ways to serve different environments. Which model is better: the QR philosophy (keep manufacturing design flexible, don't focus on minimizing transportation costs) or the ECR philosophy (fix design, control costs tightly)? Both are pull systems, but differ in how and when they react.

PHYSICAL EFFICIENCY VERSUS MARKET RESPONSIVENESS

A good starting point is the nature of demand for a brand. A functional brand is of a product that is a staple which people buy in many outlets and which serves basic stable needs. Thus, the brands have stable, predictable demand and long life cycles. This invites competition, which creates low margins. In contrast, an innovative brand of a product is new and different. This enables it to earn higher margins. But the sales cycle of the product-brand is short and unpredictable, in part, because such brands are quickly imitated, and their advantage dissipated.

Fundamentally, an innovative product faces unpredictable demand, has a short product life cycle, and is hard to forecast. It has high margins but also higher markdowns and stock outs (due to changing tastes and forecast errors). And, because these products are differentiated, they often exist in many variations. Functional products have the reverse profile. Figure 16.4 summarizes the contrasts between these two endpoints of a spectrum.

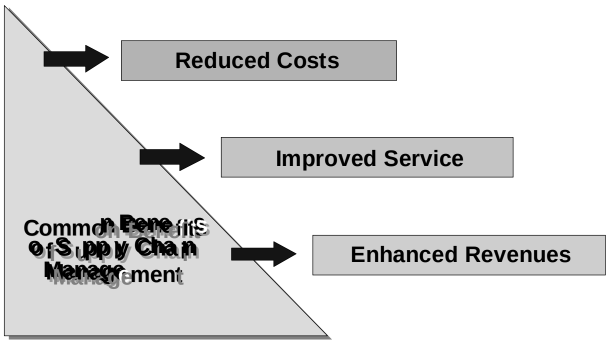
The key to supplying functional goods is to hold down three types of costs:

1. manufacturing,
2. holding inventory, and
3. transportation.

These observable physical costs all involve handling a good and accountants to track them. Efficient manufacturing and logistics are crucial. They matter first because low margins make cost consciousness important and second because predictable demand simplifies decision making. ECR fits in this spirit, as do many manufacturing methods based on tight planning and management of supplies. Here, the most important informa- tion flow occurs inside the chain from retailers back to suppliers of manufacturers.

Supply chains for these products need to be physically efficient. At the factory, this means running at high capacity; in the warehouse, fast-turning inventory. Products are designed once and for all to make them easy to manufacture and to maximize their performance. Cost and quality are the criteria used to select suppliers.

Benefits of
Supply Chain Management



Innovative goods demand the opposite. The greatest risk with these products is to miss the market by having the wrong item at the wrong time at the wrong price. The key to innovative goods is speed: Demand can’t be estimated, only noted as it begins to surge. Hence, the point of sale is a critical information flow. For innovative goods, the opportunity cost of a stockout is very high, given the high margins. And by the time the stockout is rectified, the item may have lost favor, leaving the supplier with drastically devalued stocks.

Supply chains for innovative products need to be market responsive. To do this, product design must be modular to postpone final assembly as long as possible. Performance and cost are less critical here and can be sacrificed somewhat to achieve modularity. Suppliers are selected for quality and flexibility, not lowest cost. The manufacturing system keeps buffer stocks of supplies, just in case. An obsession exists with reducing the lead time needed to fill an order, even though this raises transportation and fulfillment costs.

Market responsiveness and physically efficiency are two end- points on a continuum, along which a supply chain philosophy can be fitted.

An intriguing element here is that where a brand falls on the spectrum from highly functional to highly responsive depends on the brand's marketing strategy. Thus, the same product category can have more innovative or more functional brands, each calling for a different supply chain. For example, in cars, some brands are very conservative and stable, often appealing to a buyer who resists change (Cadillac Seville, Ford Fairmount).

Others have an ephemeral, faddish appeal (the BMW Z3 roadster, the Mazda Miata). The more functional brand needs a more physically efficient supply chain and doesn't need to be so market responsive. The more innovative one needs somewhat more market responsiveness and can afford somewhat less physical efficiency in its supply chain.

TWO KINDS OF SUPPLY CHAINS

Supply Chain Management: Why Only Now?

On paper, supply chain management is an eminently sensible idea, so sensible that one wonders why it is having its heyday only now. Even now, SCM is more a slogan than a reality at many companies, and the methods needed to make pull systems work are still very difficult to implement. Pull systems in channels are so different from push ones that it is a very challenging task to make the changeover. Internal and external barriers to implementation exist everywhere. What does a company need to build a supply chain management mentality into its marketing channels? Experience from data suggests that these elements are critical: