



# UNIT

## 7

### Contents

#### Chapter I

1. You must Possess Managerial Skills
2. You have to be an Entrepreneurial Manager
3. Distinction between Manager and Entrepreneur
4. Your Business has Special Features

**The aim of this chapter is to:**

- help you understand the reasons why you need to possess managerial skills

#### **Objectives:**

On completion of this chapter you will be able to

- identify the reasons for opting to be an owner-manager
- distinguish between an owner-manager and an administrator
- identify the strategic advantages of being a small scale entrepreneur



## You Must Possess Managerial Skills

The earlier Units have helped you in learning how to start your business. In this chapter, we will explain to you why merely starting a business is not enough. It is important to remember that creating an enterprise is not the end of entrepreneurial process. In fact, the challenge lies in earning profits out of your business venture. This requires efficient management of your resources, production of goods and services and marketing of products for generating profits.

You must be aware that you are, as the owner of a business, responsible for the management of your enterprise. This is because,

1. during the initial stages of business, you may not be in a position to engage or employ competent professional managers, and
2. as the ultimate risk-bearer you would certainly like to familiarise yourself with what it takes to manage a business. Let us recall the first chapter of Unit 1 where while listing the functions of an entrepreneur we have mentioned that the entrepreneur takes ultimate responsibility of managing the enterprise. This means you have to acquire certain managerial skills if you want to achieve success in your business.

However, with the growth of your business you will be in a position to hire the services of competent people. Then perhaps you will need to delegate the responsibility of management to professionals. Experience tells us that your enterprise at the beginning will be characterised by a stage where you yourself attend to various managerial tasks. This is very necessary for the survival of your business.

### SAQ 1.1

i) List two important reasons why an entrepreneur should possess managerial skills

a) _____ _____
b) _____ _____ _____

ii) Do you think the owner of a business is expected to discharge managerial responsibilities throughout the life of the enterprise? (YES / NO)

Give reasons for your answer

_____ _____ _____
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## You have to be an Entrepreneurial Manager

When you begin to manage your enterprise you will realise that your functioning style will be totally different from that of a professional manager or administrator. Professional managers are hired personnel and therefore, they do not have any stakes in the growth of your enterprise. Their orientation to management will be only to maximise the returns on the utilised resources. But, as an entrepreneur you must explore every opportunity irrespective of the resources under control. While you perceive an opportunity and evaluate it for its profit potential you will also explore the ways and means to mobilise resources. This is a subtle success factor which is required for the growth of your enterprise. Let us examine it in detail.

We have mentioned earlier that entrepreneurship is a process which comprises:

1. identification of opportunities
2. mobilisation of resources
3. committing actions and resources for long-term personal gains.

To be a successful entrepreneur you have to record substantial gains continuously over a long period of time. Your operations have to be different from those who initiate and operate business only for earning livelihood. In order to do this you need to have growth orientation in addition to survival instinct. Growth orientation is a very necessary condition to being highly successful.

What is this growth orientation we are talking about? It is nothing but the desired future state of your enterprise having growth and change as its major components. However, a mere desire to achieve growth may not be sufficient. You must have the ability to manage it. Study the diagram on the right.

Even if you are an employee of a company, possessing both the desire and ability to succeed you will play the role of an entrepreneur. Larger companies and corporations would like to employ people like you if you possess the desire and ability to succeed. They will call you an entrepreneur or an entrepreneurial manager and a division or department will be put under your control. You will manage this division or department as an owner-manager.

### Desire for Growth and Change

Ability to Manage		No	Yes
	No	Bureaucratic Functionary	Frustrated Potential entrepreneur
	Yes	Satisfied Manager	Entrepreneur

In the diagram we have shown desire on the horizontal side and ability on the vertical side. The signs 'yes' and 'no' will tell you whether you have this, that is desire or ability, or not. If you have both desire and ability you are an entrepreneur. If you have neither, you are just an office-employee. If you have the ability to succeed and not the desire, then you are a mere manager. If you have the desire to achieve growth and do not possess the ability to manage it, you will only get frustrated or the enterprise may become sick.



Even if you are an employee of a company, possessing both the desire and ability to succeed you will play the role of an entrepreneur. Larger companies and corporations would like to employ people like you if you possess the desire and ability to succeed. They will call you an entrepreneur or an entrepreneurial manager and a division or department will be put under your control. You will manage this division or department as an owner-manager.

Growth orientation is manifested if you have a higher level of :

- energy
- risk-taking aptitude
- social adroitness (mixing in society with a view to taking maximum advantage of your acquaintances)
- autonomy
- desire for change and a lower level of conformity (confining to yourself and not begin open to suggestions, guidance and help)
- interpersonal affect (trying to score point over others)
  - \* harm avoidance
- succourance (sticking rigid on to your beliefs)
- aptitude for long-term planning.

If you are growth oriented, you only need introduction to basic managerial requirements to become a successful entrepreneur. This and the subsequent two Units, aim at familiarising you with the management process and functions.

## Distinction Between Manager and Entrepreneur

We again emphasise that your orientation to business management as an entrepreneur should be different from that of a professional manager or an administrator. The subtle distinction in the behavioural pattern of an entrepreneur vis-a-vis a manager are listed on the right.

<b>Orientation</b>	<b>Administrative/ Managerial</b>	<b>Entrepreneurial</b>
Strategic or long-term	Use of existing resources	Perceiving opportunities
Commitment to opportunity	Evolutionary, long-term and controlled	Revolutionary
Commitment and control of resources	Ownership of resources	Pursuing use of rented resources also
Management style	Formal hierarchical structures	Informal networks
Compensation	Resource-based	Value-based

As mentioned earlier, your long term goal in the business is to explore every opportunity that comes your way. In doing so, you will take unusual leaps and jumps and emerge with revolutionary ideas and not just gradual outcomes. Unlike an administrator, your aim is not to own the resources which help you in exploiting these opportunities for profit. You are fully aware of the fact that resources are only a means to earning profit and hence you will never



hesitate to use hired resources. As regards organisational structure, you will not rely on formal hierarchical layers. You will give a high priority to establishing personal and informal contacts with every person involved in your business. You will consider the returns on your business as rewards to your values and not to the resources you have used in producing the goods and services.

You must remember that the following two specific roles you are going to perform as an entrepreneur will make you indispensable to your business:

1. In order to produce a commodity you are required to have inputs such as raw materials, machinery and labour. Normally, you will purchase these inputs in the market. There are certain other inputs which are equally important for producing commodities, but they are not available for sale/purchase in the market. For example, risk taking, innovation, pursuing opportunity and motivating your employees to perform better are not available in the market. Unless you supply these inputs, production will not take place. If you want to supply these inputs, since they are not available in the market, you have to possess them within yourself. Otherwise, you end up in sickness and closure of your business. Further, the cost of the inputs purchased in the market is known to you but not the cost of the inputs which you yourself possess. The difference between the cost of inputs which you have purchased in the market and the income from the sale of the commodities you have produced must be the cost of your involvement in the business. Higher this difference higher will be the cost of or in other words reward, for your involvement.
2. It is not sufficient to have one or two inputs when you require three or more. You have to provide all the inputs that are necessary for producing the commodities and in required quantities. Otherwise, production discontinues. People working for you will not be bothered even if production is discontinued on account of input deficiencies. It becomes your concern, as the owner of a business, to see that all the required inputs are available in required quantities whether they could be purchased in the market or not. For example, if you require a certain raw material, risk-taking and innovation to produce a commodity, possessing only the raw material and risk-taking will not be sufficient to produce the commodity, you also require innovation. And there is no short-cut for this.

While acquiring managerial skills, we urge you not to loose sight of these indispensable qualities. Ultimately, these are the ones which will make you entrepreneurial and place you at a rank above that of professional managers. These are the qualities which make small business management subtly different from the management taught in business schools.

## SAQ 1.2

i) Fill in the blanks

While managerial orientation is to maximize resource use, the entrepreneur would prioritise

\_\_\_\_\_

ii) What are the two necessary conditions for becoming a successful entrepreneur?

a) \_\_\_\_\_

b) \_\_\_\_\_



iii) As an owner-manager what are your two major responsibilities?

a) _____
_____
b) _____
_____

## **Your Business has Special Features**

Before introducing you to the process of management, we wish you recognise the features of small business. It helps you manage your business successfully.

1. You will require far lower investment in the operation of your business since it is small. This is true not only for investment in equipment, machinery, building and furniture, but also in day-to-day expenditure on raw material, labour and utilities like electricity and water. If you compute the money invested per worker, it works out to be substantially low. This is beneficial, for it makes your business labour intensive. It gives you the flexibility of using your labour for different production jobs. If and when you want to change the line of production, it becomes easier for you to switch off the existing one. This is because, you do not have heavy investments in immovable assets. You just have to tune your workers to new production skills. You will be able to respond and adapt much faster than the larger corporations to the social, economic, political and technological changes.

Besides, initial investment being very little, the funds required can be raised from personal sources, family, friends and relatives. Evidence shows that entrepreneurs operating on funds raised from internal sources perform better in risk-taking, innovating and flexibility. They are far more committed to achieving their goals since it is their money which is at stake. Larger companies operate on funds raised from the public through equity shares and loans from financial agencies. If they fail to achieve success, the loss is borne by too many stake holders whom the leaders of these corporate bodies may not have even seen

2. Your business normally operates with a small number of employees, dealers, suppliers and customers. This helps you in having better interactions with the people who are directly responsible for your profit. As an owner-manager you will be able to give a personal touch to the relations you have with them. Because, only in a small business all employees, dealers, suppliers and customers have a chance to meet and interact with the head of the business, at one point or the other. In all possibilities they would consider themselves as part of your empire (business), which is crucial for success of your business. Your customers give more importance to your concern for their satisfaction and suggestions. Similarly, your employees lay great value on your affection and concern for them. This insures internal motivation of your firm and helps in doing away with opportunistic behaviour and an overall better performance. Working with a small number of people also helps you in quicker decision-making. Such an achievement is possible only in a small divisions of a large business.



3. The possibility of frequent interactions with customers makes the small business more suitable for service industries. It is being observed that businesses are moving towards supply of services. And small businesses are indeed suited for this. As the societies move towards comforts from necessities, it is found that possessing experience helps in day-to-day problems rather than possession of mere physical goods. For example, tooth paste is a necessity but, customers are more comfortable with a soft-squeeze tube. Further, technological progress is making the life of physical goods shorter and shorter unless appropriate after-sales service is available. For example, audio players gave way to video players. For marketing the audio players the better option now is to provide prompt after-sales service. A time will come when the customers will compare goods supplied by two companies in terms of the after-sales service these companies provide. Companies which could form a niche here only survive.
4. In an increasingly competitive world specialisations are more important than routine commodities or services. Larger companies by virtue of huge machines and heavy operations would not be able to cater to the special needs of various segments of the society. For example, different groups of people require different types of hair oils. A large company which produces huge quantities of one particular type of hair oil may not be able to satisfy all the groups of people. In addition, large companies themselves require certain special components which can not be provided by large-scale operators. This is because the demand for special components such as tailor-made bolts and nuts will not be so large as to be worthwhile for manufacturing by a large company. It is here that they as well as the society look towards you. As a small operator, you will be able to supply tailor-made services or goods to large companies or direct consumers. Quite possibly, you may become an ancillary unit to a large firm or a large firm may subcontract certain work to you.
5. In terms of production, exports and employment, statistics show that small businesses have recorded a substantial share in the Indian economy over the past two decades. In view of this and also to bring about regional balance and decentralisation of economic power, governments protect and promote small scale enterprises. Several incentives and subsidies, tax relief, concessions and priorities are given to the owner-managers of small scale enterprises. Details of these schemes are presented in Unit 2. While chalking out management strategies, you must take these into account.
6. Although your overhead costs would be quite low on account of small scale operations, your per unit cost of production will be higher. This is because you cannot purchase raw material and components in bulk and hence, the cost of these will be far higher than that of larger units. But, you will also make substantial profits on account of the fact that you are satisfying very specialised needs of your customers, which is just not possible for larger companies. All that you have to remember is that your business requires substantial amount of money for day-to-day operations. If timely finances are not available, you will run the risk of losing customers. Efficient assessment and management of working capital only can help you in such a situation.
7. You have to use personal attention or high quality or specialisation as an instrument to promote sales, or you may have to explore those markets where price is more important than quality. This is because on the marketing front you have certain limitations. Your



products may not have the brand image in the market if they are competing with those of large companies. You cannot even provide credit to the customers, as you yourself require finances for running the business. You may not be able to branch-out your organisation to broaden your market. You may not be able to use advertisement media for promoting sales, since the media is a very costly option. What you need to remember is your business does not need these strategies during the initial stages. While designing marketing strategies for your business you have to keep this in view.

8. Your potential for motivating employees to perform better and making them feel a part of your enterprise will help you in retaining them for long. This is important because you may not be able to hire competent people as you cannot afford better salaries or better growth. If you recruit unskilled labour, you have to arrange for their training. After accomplishing development of skills, the employees may not like to remain in your services. They may either move away to a company where they have better prospects or establish a firm which could become your competitor. Your recruitment plans and human resource development strategies should keep these aspects in view.
9. Information on technological changes is normally costly. But, there are several information agencies and industry associations which will help you keep up-to-date. As a small business-owner you have this advantage. However, you have to constantly keep in touch with them. You may also subscribe to one or two important journals. Otherwise, since you cannot invest in libraries and research and development you are vulnerable to finding your products becoming obsolete. While the society is moving ahead, you may find yourself in out-dated processes.

### SAQ 1.3

- i) What is going to be the competitive advantage of your enterprise? (select the right choice)

- a) Personal touch \_\_\_\_\_

b) Low price \_\_\_\_\_

c) Less number of employees \_\_\_\_\_

d) Flexibility to switch over \_\_\_\_\_

- ii) List the limitations of your (small) firm in terms of following functions:

- a) Production: \_\_\_\_\_

\_\_\_\_\_

b) Personnel: \_\_\_\_\_

\_\_\_\_\_





c) Marketing: \_\_\_\_\_  
\_\_\_\_\_  
d) Finance: \_\_\_\_\_  
\_\_\_\_\_

List three inherent advantages of a small business

a) \_\_\_\_\_  
\_\_\_\_\_  
b) \_\_\_\_\_  
\_\_\_\_\_  
c) \_\_\_\_\_  
\_\_\_\_\_



# UNIT

## 7

### Contents

#### Chapter II

1. Managerial Tasks
2. Managerial Skills
3. Managerial Functions
4. Organisational Structure

#### The aim of this chapter is to:

- help you develop a plan for the success of your business

#### Objectives:

On completion of this chapter you will be able to:

- list the issues on which your plan should provide focus and direction
- identify what needs to be done in order to remain competitive
- decide on the growth strategies



In course of operating your business, you will be required to handle four managerial tasks and discharge four managerial functions. While doing so, your approach to the issues should be opportunity oriented and not mere resource optimisation. This is primarily because, as discussed earlier, you are an owner-manager and not a mere manager.

## **Managerial Tasks**

The first and foremost task is to define the objectives of your business and thereafter plan the actions in order to achieve these objectives. There could be several such plans. You may plan long-term objectives stretching over 3 to 5 years or even more. You may also plan short-term objectives relevant for just 1 or 2 days. You may plan medium-term objectives for a few months or even a year or so. For example, expanding your market to national or international boundaries could be a long-term objective; achieving break-even level of capacity utilisation could be a medium-term objective; obtaining loans and sanctions could be a short-term objective.

You may plan objectives for a specific area of your business. For example, objectives related to raw material purchase may be separately planned. In essence, you are required to plan in advance, everything that you want to achieve in your business. Planning provides the basis for action and you can compare the results of what you have achieved with what you had targeted.

The second task is to organise people, time, money, machinery, materials, processes, etc. so that you can achieve your targeted objectives as efficiently as possible. This enables you to turn the plan into reality.

After having established an organisational structure as a result of the task mentioned above, your success will depend on how you are able to control your operations. You have to establish performance standards, procedures, targets and budgets. This will help you in measuring the performance of your business. You will be able to monitor workers' performance, job progress, financial conditions, etc. You will come to know when you fall short of your planned performance and why. Then, you can take corrective measures and resolve the problems that arise.

The final and most important task is that of leading, supervising, co-ordinating and motivating. In other words, getting other people to perform which will lead to your plans being achieved and objectives being met. This may be termed as directing or executing.

## **Managerial Skills**

There are four types of skills which you need to possess in order to handle the tasks described in the previous page.

1. communication
2. decision-making
3. problem-solving
4. measuring or quantifying



When your business is small everybody tends to get to know what is going on in the work place and the kind of work that is handled by all the people. Communication therefore, takes place in an informal manner. As the business grows and becomes more complex, you need to put in more effort to make sure that all the people involved in various activities of your business stay in touch with one another. This is true, not only with the employees but also with the customers, the suppliers, professional advisers, government officials, etc. You do not need to be formal but you do have to plan and give a serious thought to make sure that people communicate. But, you have to take decisions regarding which information ought to be communicated and which should not be.

Making decisions is important. Unless you make up your mind you will not get anything done. Once you have made a decision, you also need to think about its consequences. Making a wrong decision is not necessarily harmful. In fact, it can provide a useful learning experience. The important thing is to understand how and why you made that decision and to use the knowledge to help you make better decisions in the future.

Your expectations may not always come true. The unexpected occurs. These situations can be viewed either as 'problems' or as 'opportunities'. They need to be tackled or managed. Ignoring them could be disastrous. Worrying about them would not help either. So, you have to be a problem resolver. You have to transform these problems into opportunities.

Information about the performance of your business as well as the environment around your business is available in the form of factual data or numbers. This needs to be collected, processed, analysed and interpreted for using it for the growth of your business. You should be able to understand not only what these information's mean but also use them to monitor the performance of your business and make necessary adjustments if required.

We do believe that you possess all these skills to some degree. How to realise it and how to develop these skills to a level required for success in your business are dealt with in the remaining chapters of this Unit.

## **Managerial Functions**

One of your primary functions as owner-manager is to procure raw materials, components, machinery and equipment and utilities such as electricity and water. You are required to plan how much of these are needed and when, how to acquire them and where to store them, which technology to be adopted for resource mix and transforming the inputs into outputs (finished goods) etc. You have to implement these plans in such a way that you keep up with the flow of production with minimum possible wastage of either inputs or finished goods. This is what is known as managing production.

Employing the right kind of labour and professionals, improving their skills and ensuring adequate and appropriate performance form an equally important function. Contribution of your employees to the production of goods and services could be far higher than that of physical inputs such as raw material and machinery. Let us see how is this possible. There are two special features of human resources:



One, without their involvement, physical inputs cannot transform themselves into outputs. Two, physical inputs can not improve their performance, but human resources do and by doing so they will improve the value of the physical inputs in the outputs. While the contribution of the first role mentioned above could be quantified in terms of wages, the contribution of the second role cannot be easily quantified. This depends on the motivation of the human resources concerned, which could be successfully improved by you. The more you motivate your employees the more will be the value of your output. This is what is known as managing the personnel.

Once you have produced a product, you have to sell it to consumers or buyers. This is a function which pays you back for the labour and money you have invested in your business, probably in excess so that you can make profits. What, where, when, whom and how to market are the crucial decisions which you have to take. You must learn to market rather than sell your products. Because, while selling, you sell your needs but while marketing, you sell your customers' needs. You alone as a small businessman cannot influence the needs and styles of the consumers. So, you have to understand the needs of your customers and satisfy them in an innovative manner. This is what we call 'managing the marketing'.

You require finances for all the above mentioned functions. You have three ways of procuring funds for these activities:

- i) raise funds internally,
- ii) borrow funds from external sources,
- iii) use the income generated by selling the products.

Which source needs to be explored, when and to what extent is a question on which you have to take decisions from time-to-time. When you start the business and when you want to expand or diversify, you would definitely need substantial finances for investing in fixed assets. Even for day-to-day operations you would require money. You have to assess how much money you would require on hand and how to acquire it. Further, you must also maintain details such as how much money you have spent and on what, how is it procured, how much profit could be earned, how much more will be earned and what are the prospects of expanding the operations. Planning and acting on these issues is known as financial management.

There are several tools and techniques of managing these functions effectively. You will learn the principles of production and personnel management in Unit 8 in detail and in Unit 9 the principles of marketing and financial management.

## SAQ 2.1

- i) List the four managerial tasks

a)	_____
b)	_____
c)	_____
d)	_____



ii) Fill in the blanks.

Success of your business depends on your communicating effectively with

\_\_\_\_\_, \_\_\_\_\_, \_\_\_\_\_, \_\_\_\_\_  
and \_\_\_\_\_.

iii) If you make decision you are not fit to be an owner-manager.  
(TRUE / FALSE) Please explain:

\_\_\_\_\_

v) Measuring or quantifying information will help you in (choose the correct answer):

- a) Motivation \_\_\_\_\_  
b) Communication \_\_\_\_\_  
c) Performance evaluation \_\_\_\_\_  
d) Delegation \_\_\_\_\_

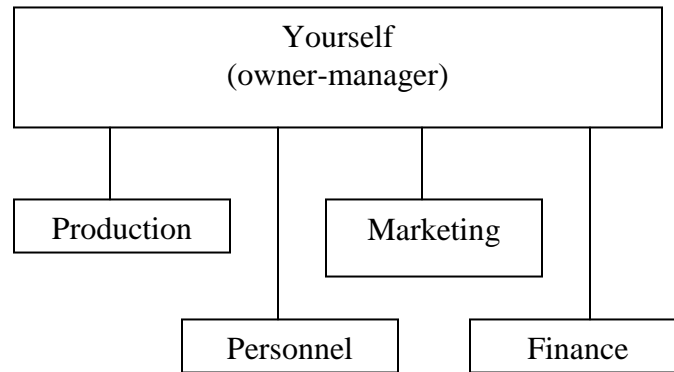
vi) List the four functional areas of management.

- a) \_\_\_\_\_  
b) \_\_\_\_\_  
c) \_\_\_\_\_  
d) \_\_\_\_\_

## Organizational Structure

Every business, whether large or small, invariably needs an organisational structure. However, size of operations dictates this structure.

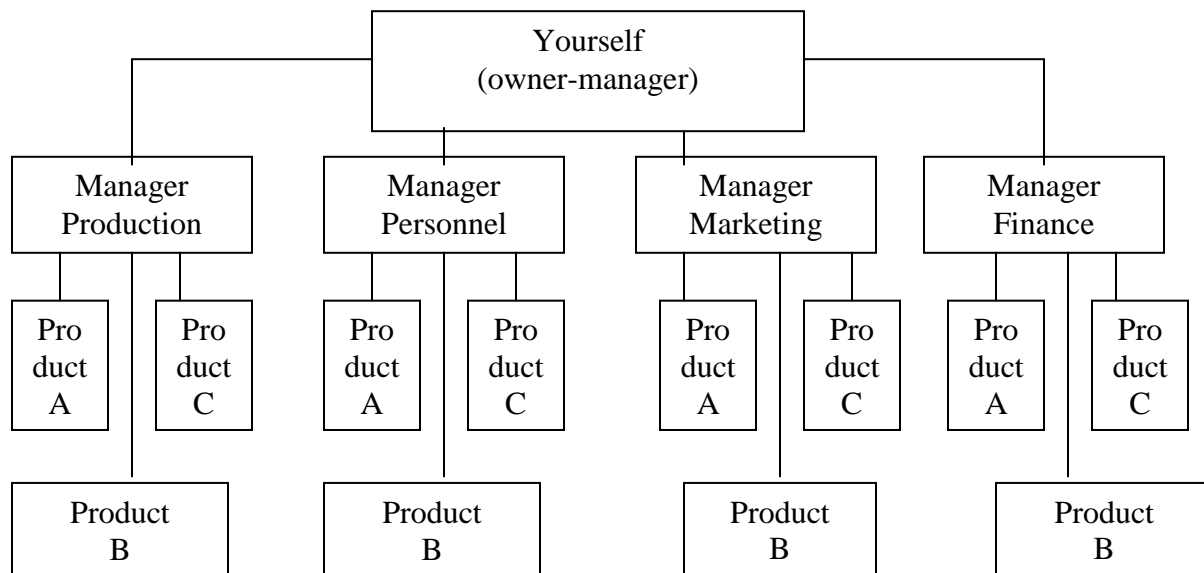
As a small entrepreneur you have to respond to all the requirements of your business. Since you cannot afford to hire competent professionals, when you start your business all these functional responsibilities will be rested in you. You will have to by inputs, hire people, commit the inputs to produce goods, market the products, arrange for financing your activities and do the accounting. The organisation structure will be, perhaps, like the chart on the right.



You may not like to call this as a structure. But, as your business grows you will be required to devote more time to higher level problems and less time on day-to-day details. Then you need to have a definite structure. Initially, you may be producing one or two products. But, as your business grows you may produce more products.

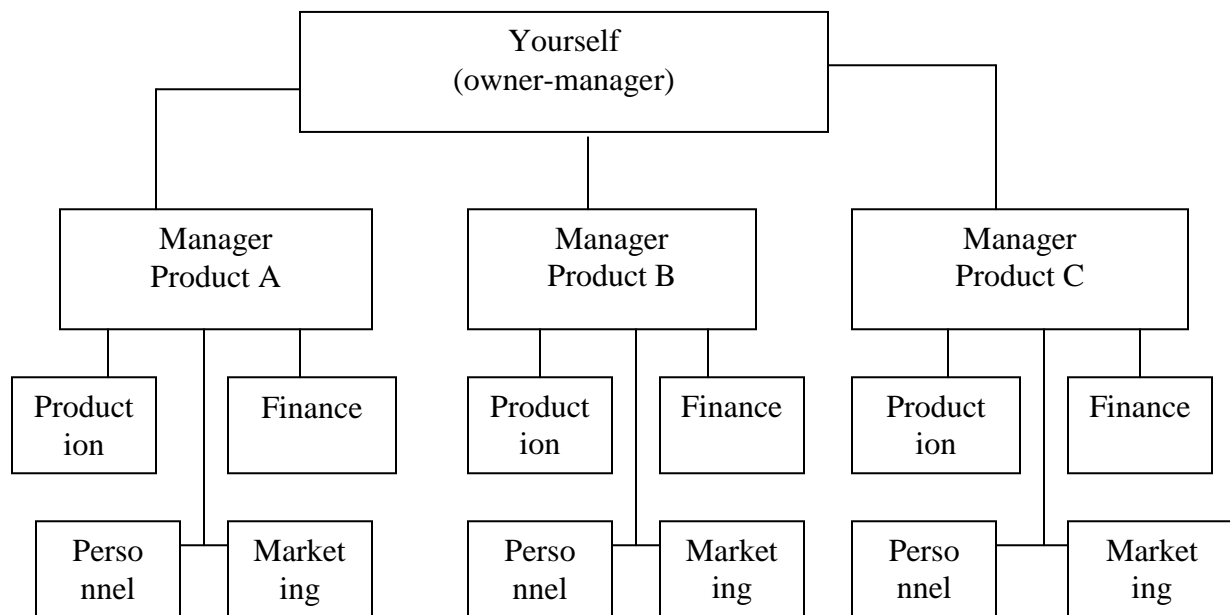
Then you may require one of the three following organisational structures:

**1.** If the market in which you are operating is stable and predictable and you want to ensure better performance of human resources, an organisational structure, where each management function will be handled by a manager who will directly report to you, is more suitable. Each functional manager will in turn handle the requirements of the concerned function in all the products your business deals in. The structure may be something like the following:



But, it is important to remember that the transition from your entrepreneurial structure to this functional one is gradual. Success in this transition depends on your ability to delegate responsibilities to your subordinates. It is true that you will continue to have an attachment to your business. But, as the business grows you will not have time to handle the increased load personally. And so, you will have no option but to delegate.

The same is true even in a structure where the responsibility of each product will be handled by a manager who will be directly reporting to you. Here the manager in turn looks after all the functional requirements of producing a product. Look at this:



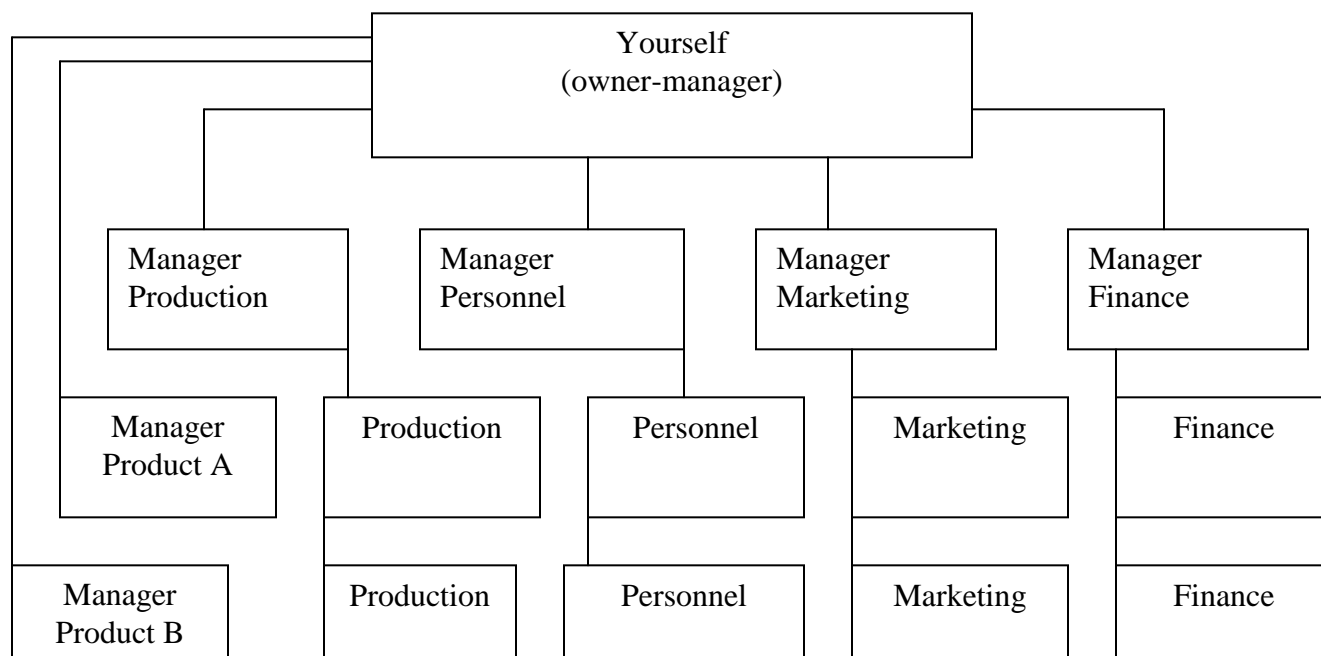
This product based structure is appropriate where the competitive situation is volatile and decisions have to be made quickly at a decentralised level. Particularly, when your business starts producing more than two products, such a structure is more functional.

When you can afford and especially when the designs and composition of your products are required to change continuously to suit the market demands, you may need a slightly complex structure. In this type of organisation, a manager is assigned the responsibility of co-ordinating a particular product with each functional area. Both the product managers as well as functional managers will be reporting to you directly.





Diagrammatically the structure may be presented this way:



Organisational structure may also specify the other shift involved in the business.

## SAQ 2.2

i) Design an organisational structure for your business.

ii) Specify why have you chosen this.

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iii) Match the following:

a) Stable and predictable market	Complex organisational structure	(       )
b) Volatile and unpredictable market	Functional organisational structure	(       )
c) Flexible product design	Product organisational structure	(       )



# UNIT

## 7

### Contents

#### Chapter III

1. Be sensitive to the Environment
2. How to be Aware of Change
3. How to Manage Change

**The aim of this chapter is to:**

- help you understand why and how to manage external factors.

#### Objectives:

On completion of this chapter you will be able to

- identify the changes in your environment and the implications they have on your business
- innovate such changes and the sources of information on these changes
- decide on the actions to be taken regarding the changes in the environment.



## **Be Sensitive to the Environment**

Developing your business is as entrepreneurial as establishing your business. You must strongly believe that the development of your business will bring you long-term personal gains. In the previous chapter we have attempted to make you understand the scope of managing your business. But, you must also remember that your business is situated in an environment where several external factors influence your performance. Changes in external factors may either reduce the demand for your product, or provide you with new profitable opportunities. Merely managing the functions of your business is not enough, you must know how to manage these external factors as well. Or else, you may loose out either on the possibility of exploiting new opportunities or in producing products which are not in consistence with the demand of the society at large. In this chapter we will help you understand what external management is all about.

While planning for development, you will have to make certain assumptions about the environment in which you are living. For example, since the ultimate aim of producing goods is to market them for profit, you will have to estimate the demand for your products. After having assumed a certain demand, you will next schedule for the production. If your products are more in demand during the winter season, you will obviously produce more of them during winter. If they are more in demand in a neighbouring city you will have to market them more in that region. But, your assumptions may not hold good forever. Reality changes with time. There are several factors in the environment which influence the prospects of your business. You have to constantly study the environment in order to identify these changes. Once the changes are identified, you have to accordingly alter your assumptions. Otherwise, your plans will fail and development will halt. At the same time certain changes in the external environment may create new opportunities too for you and you must have the capacity to exploit them gainfully

The environment around your business comprises of four broad areas:

1. Social
2. Economic
3. Political
4. Technical.

Let us look at some of the critical elements of change in these areas of environment and examine what possible implications they may have on your business.

### **Social**

Changes in social attitudes will have major implications on your business. For example, it is likely that the following changes are taking place in your region:

1. People are moving towards purchase of video cameras in place of still cameras. If your business deals in developing negatives of still photographs, it is worthwhile pursuing recording, processing and editing video films.



2. The percentage of working women is increasing steadily. With fewer women at home, door-to-door selling may not be of great use. Since working women now have less time for household work, the demand for ready made foods may go up. Since working women also have less in children for having more children, there is a decline in the birth rate and therefore demand for products meant for children may also fall. On the other hand, with women supporting the family income by way of working, the demand for child care-homes such as creates and toys may go up. Demand for convenient garments may also increase since working women prefer comfortable garments for the work place.
3. The percentage of population above 60 years of age is increasing steadily. Demand for leisure-time entertainment such as programmes on satellite channels as well as demands for, old age homes and garments may steadily rise.

To keep pace with such changes you may need to either diversify your business into a new activity or may even have to change the product line. Of course, before exploring these options, you have to check whether these changes are really affecting your line of business. Because you should react, only when your profitability is affected. You have two options before you. You may either react as and when the changes in consumer requirements are detected or you may anticipate the changes in advance and be pro-active

## **Economic**

Changes in the economic position of your country or region, your competitive position in the market, and the position of the suppliers of raw material and machinery and the buyers of your products will have direct and indirect impact on your business.

For example, a lower rate of economic growth is a reflection of a much higher energy cost, less productive labour, a shift towards larger government service sectors and a shift of business investment from traditional industries to service and high- technology sectors. Similarly, higher rates of interest would make investment in physical and long-term assets uneconomical. Perennial increase in rates of interest encourages shortened investment horizons.

If your line of operation is in an industry where employment is declining such as rubber, textile and automobiles, or even if you are a supplier to these industries, you have to make a shift to a comparatively modern sector such as electronics. This is because a declining rate of employment is a sign of sickness.

If setting up a business in the line of your products is easy, you will have too many people producing the same products which means you will have many competitors. A situation may arise where the supply may exceed the demand. This would bring down the price of your product and eventually your profits. If the entry into your business is not so easy you will enjoy higher profits. For example, if you are manufacturing an electronic product the design of which is known only to you, nobody can enter that business. In a situation where a few other businessmen are also producing a product similar to the one you are manufacturing, there could be a possibility that you enter into an agreement with them and jointly fix up the price or share the market. You have to explore such possibilities.



The type of product you are producing is bound to have a life span, beyond which it will not have any demand. For example, if you are manufacturing radios, it may not have any demand, at least in the cities, say may be 10 or 20 years from now. People may like to acquire pocket televisions. Therefore you must always be ready for such changes in customer requirements. Similarly, the market in which you are selling your product may not continue to demand your product for long. Your market also has a life time beyond which it does not need your product. For example, if you are selling water coolers and all households in the region have procured one water cooler each over a period of time, then you will have no further customer to purchase your product. You will either have to change your line of production or move on to another region.

The changes in economic environment such as the ones we have discussed above will not only affect your business, in one way or the other, but affect the business of your suppliers and the behaviour of your buyers as well. You must keep a watch on these changing influences and respond accordingly. If your suppliers decide to quit their business then, you have to either locate alternative sources or change the line of production or do the needful to keep the business of your suppliers alive. If the average family income of your consumers goes up, try to trace on what they spend their excess (disposable) income and endeavour to enter that very line of production.

## **Political**

The continued growth of government intervention in the economy, the power of trade unions, and the rise in public interest significantly influence the performance, operations and markets of your business.

Government intervention over the past few decades has led to regulating the business environment. It has provided protection to small businesses against the larger companies and corporations. However, since the last few years there has been a substantial deregulation of the economy and liberalisation of policies. While some of these may provide opportunities to you, the remaining may cause a concern. For example, relaxing the ceiling limit on investment in plant and machinery for a small business would help provide a scope for expansion of your business and upgradation of technology. But, the import liberalisation may depress the price of your product, if it is an import substitute. In such a case, you may have to shift to the production of a product which is not a substitute to the cheap imports.

Political ideology of the ruling parties have an impact on the business environment. Several lobbies attempt to influence political decisions. These decisions favour some businesses and disfavour others. Often, the directly affected groups are the larger companies. If you are a supplier of products or services to these companies, your business potential is clearly influenced by these decisions. For example, the Government of India, over the past few decades, has been supplying cheap imported oils to the vanaspati industry in order to make the production of vanaspati a viable proposition. This would depress the price of indigenous edible oils such as groundnut oil and mustard oil since they are substitutes to vanaspati. But, if you are entrepreneurial, you would produce oils such as cotton-seed oil and mahua oil and supply these to the vanaspati industry for use in its manufacturing.



## Technological

Combined with critical elements of change such as those listed in the above three sections, technological changes will upset stable markets and competitive relationships. It has also been seen that new technology sometimes makes winners out of losers. When adapted, it may help you in reducing the cost and consequently the price of your product. It may also help you in creating a new business.

Technological change is particularly important to smaller businesses. Many small businesses have achieved success through technological innovations. You must constantly try to obtain information on the changes in technology and examine whether they could be exploited for improving your competitive position.

### SAQ 3.1

i) Give two reasons why you should manage the external environment.

- a) \_\_\_\_\_  
b) \_\_\_\_\_

ii) Identify one recent change in each area of your external environment and project its implications for your business.

	Change	Implication
a) Social		
b) Economic		
c) Political		
d) Technological		

## How to Be Aware of Change

You are required to constantly stimulate your thinking and your curiosity regarding the critical changes which are occurring in the market area. In order to do so, you have to focus on the following issues:

1. What are the changes in the attitudes of people?
2. What are the trends in population?
3. What is the composition of the population?
4. What are the trends in the rate of growth of the economy in your region?
5. What are the trends in interest rate, unemployment and inflation in the economy of your region?



6. What are the entry barriers in your line of business?
7. What is the life cycle of your product?
8. What is the life cycle of your market?
9. What are the recent changes in the government policy?
10. What are the recent technological changes that are relevant to your business?
11. How are these changes affecting your business, your suppliers' business and your buyers' behaviour?

These are a few of such issues on which you should obtain information. Large companies often possess public affairs departments that specialise in thinking about and analysing these issues. Since you cannot afford this investment, you have to explore alternative avenues. Several departments, committees and ministries of the Government of India and the state governments periodically publish a number of books which will provide you with factual data. In addition, industry associations, trade associations, research organisations and premier organisations like the Reserve Bank of India also publish periodical information on various issues. Many of these publications are available with the libraries and government offices in your area. Your employees, customers, suppliers, competitors and bankers are also a good source of information. They can not only provide you with the latest information but also suggest its implications for you.

### SAQ 3.2

Search, identify and write the sources of information on the eleven issues listed above.

i)	_____
ii)	_____
iii)	_____
iv)	_____
v)	_____
vi)	_____
vii)	_____
viii)	_____
ix)	_____
x)	_____
xi)	_____



## How to Manage Change

Once information is obtained, you should make a list of the critical changes. Each of these changes should be analysed separately in the following order:

1. Check whether the change has any impact on the profitability of your firm. If it does not have any impact, then just do not worry about the change. But, if it has an impact, then go on to the next stage.
2. Check whether you should take any action to prevent the change. This depends on whether you can succeed in preventing the change. If you think you cannot succeed in preventing the change, go on to stage (4) or else, go on to stage (3).
3. Check whether you have properly understood what it takes to prevent the change and whether you can afford it. If you think you can afford it and you are fully aware of how to go about it, then just do it. Otherwise, go to stage (4).
4. Accept the change and adapt to the new situation. Explore new strategies. Either change the line of production or move over to another market area.

Successful small businesses tend to follow orderly and systematic patterns with respect to managing external environment, even though these patterns are seldom consciously recognised by them. Unlike larger companies you cannot always involve yourself in preventing changes. Therefore, at least during the initial stages of your enterprise, you have to manage change in such a way that it contributes to your profitability. However, if you take a positive decision to be involved in the process of change, participation in industry associations is a worthwhile option

### SAQ 3.3

Select an issue of change and analyse it. Write down on the separate sheet the issue and the process of your analysis. What have you decided to do with this change element?

Change Element: _____ _____
<b>Analysis :</b> _____
stage 1 _____ _____
Stage 2 _____ _____





Stage 3 \_\_\_\_\_  
\_\_\_\_\_

Stage 4 \_\_\_\_\_  
\_\_\_\_\_

Your \_\_\_\_\_

Decision: \_\_\_\_\_



# UNIT

## 7

### Contents

#### Chapter IV

1. Planning is Essential for Success
2. The Plan Provides Focus and Direction to Your Business
3. The Plan Indicates How to Remain Competitive
4. The Plan Insures Your Growth
5. It Pays to Remember

**The aim of this chapter is to:**

- help you develop a plan for the success of your business.

**Objectives:**

On completion of this chapter you will be able to

- list the issues on which your plan should provide focus and direction
- identify what needs to be done in order to remain competitive
- decide on the growth strategies.



## Planning is Essential for Success

Planning in simple words means deciding on actions well in advance. As the number of activities increase, you will find it increasingly difficult to control your business, unless you make and implement appropriate action plans. Especially, when you employ ten or more workers you are making investments at a level where you cannot afford to fail in your venture. Therefore, you must plan your future and check periodically whether the plan is accomplished. Once you start planning, you will attempt to make your business as sound as the professionally managed larger businesses. However, the process of planning in your business has to be somewhat different from that of large businesses. This chapter will explain to you all that you need to keep in mind while planning for success in your business.

Experience tells us that successful entrepreneurs constantly evaluate the impact of alternative decisions on achieving their goals. They also study and analyse all possible outcome or pros and cons of a given decision. After analysing the advantages and disadvantages of various managerial options, they develop strategies suitable for probable alternative future scenarios. These are then documented in the form of a plan which helps the owner-managers in warding off the affect of the changes in the environment we had referred to, in the previous chapter.

As mentioned in chapter-2, planning cannot be done as a one-time exercise. It must be a continuous activity. There could be several plans catering to various functions of your business but you must prepare an overall plan for success. Such a plan, when implemented should serve the following three purposes:

- i) Provide focus and direction to your business
- ii) Help you retain your competitiveness in an ever changing environment
- iii) Help you grow and develop

### The Plan Provides Focus and Direction to Your Business

If you provide for clear definitions on the following, then your plan gives focus and direction to your actions:

1. **The mission of your business:** A powerful mission statement helps in your business decisions. Such a statement describes accurately the true identity and goal of your business. You must be able to clearly specify what product you will produce and what gains you will make from it. If your mission is properly understood by the people connected to your business such as your workers and suppliers, they will be able to contribute effectively to your success.
2. **Your vision of the future of your business:** You must clearly specify what promises your business has for you, your employees, your suppliers and for the society at large. You must also be able to indicate how your business is going to become an important activity in the society for years to come; and what would be the growth potential of your



business over a period of time. Such a statement on the future of your business would energise the people working for you and provide inherent incentives to them.

3. **The core skills of your business:** Identifying the skills and specialities of your business which provide you the competitive edge over other businessmen, prevents your business from dangerous deviations. Your vision of the future is dependent on these skills. By defining the core skills of your business, you and your people will be able to gauge whether to make any changes in the line of production and whether to make any changes in the market. You will also be able to nourish your business and further your competitiveness.
4. **The environment of your business:** Listing down the external factors and changes which may affect your business will help you in obtaining relevant information and thus narrowing your focus only to a few important change elements. Once these factors are clearly defined and made known, even your employees, suppliers and customers will be able to keep you informed of their perceptions of the trends in relevant changes, so that you can take timely actions.
5. **Your suppliers, customers and competitors:** Knowledge of the nature of your suppliers' business is important because the success, failure or changes in their business plans have implications for the availability of major resources for your business. You have to quickly respond to the shortages in raw materials, components, equipment or machinery, if you want to keep up with the production schedule. You must identify new suppliers and ensure regular supplies of the resources. You must also know who your customers are, the nature of their behaviour as well as their position in the society. Changes in the environment may affect their behaviour as well as their position, which in turn would affect their demand for your product. In other words, knowing who your customers are, will help you and your employees in identifying and keeping track of those factors which might influence their demand for your product. You must also identify who your competitors are and their strengths and weaknesses. This helps you in formulating strategies in order to improve your competitiveness. You will know explicitly what and who you have to compete against

### SAQ 4.1

How will the following provide direction to your business? Write in one or two sentences.

Mission:	_____
Vision:	_____
Core Skills:	_____
Environment:	_____
Suppliers:	_____
Customers:	_____



Competitors: _____ _____
-----------------------------

## **The Plan Indicates How to Remain Competitive**

You must specify in your plan, the strategies that help you to retain the competitiveness of your business. Described below and on the following pages are a few tips which will be of immense use in designing strategies for competitiveness.

1. There are three types of competitors you will have to deal with in your business. The first type of competitors are those with whom you can work out an agreement so that you can share the markets appropriately among yourselves. If you market your products in one market or one segment of the market, they can market their products in other markets or other segments of the market as the case may be. In such a case, same products or substitute products produced by you and your competitors could be sold at almost the same price. You must constantly search for and identify businessmen with whom you can work out such agreements.

The second type of competitors are those who for some reasons do not agree with this kind of proposition. These are the ones with whom you have to wage battles. You have to compete with them from a position of strength. You must choose the place and time for the battle in such a way that you have a clear edge over your competitors.

You can exercise several options such as making use of your interpersonal skills to attain brand loyalty of your customers, or improve upon the quality of your product, or reduce the price of your product, or cater to a market segment to which your competitors cannot reach out. You must examine and evaluate carefully all these options and adopt the one where your competitors cannot win. The strategy you adopt will give you your market niche. As and when your competitor(s) enter your market niche, you will lose your competitive edge. You must be flexible enough to identify and then switch over to a new market niche. Or else, you stand to lose in the competition. You must always select such market which gives you maximum flexibility.

The third type of competitors are those with whom you cannot compete. These are normally the larger companies. You must either avoid a direct confrontation with them or if possible agree to be a sub-contractor to them. As a sub-contractor you will supply the products to them which would be marketed under their brand name. Their marketing network would market your products under their brand name.

Making agreements with the first and the third type of competitors require effective negotiation skills, while competing with the second type of competitors requires intelligence and presence of mind.

2. A sure way to remain competitive is to go in for a partnership with every key person concerned. Ultimately, customer satisfaction determines your competitiveness. While taking any action, you must always consider its impact on the customers. What your



customers want may differ from what they need. It is important for you to satisfy their wants rather than their needs. You must observe and consider customer demand and understand their concerns and problems. It would prove to your advantage if you could establish a network of customer-manager nexus and provide them with services your competitors do not. This would make them feel that they are a part of your business and a sense of belonging which ensures loyalty to your product. Customer satisfaction ensures a high rate of unsolicited repeat business.

Making mutually beneficial contracts with your employees is a form of partnership. You should provide your employees with a clear set of incentives which would encourage extra commitment on their part. You could thus share with them the responsibility of work in unison for the growth of your business.

Suppliers are an integral part of your business. They contribute actively to the competitive edge of your business. You should communicate your plans and requirements to them and honour valid suggestions for innovations.

Financial agencies, commercial banks, industry associations, government agencies and of course your family are the support network for your business. Work in close confidence with them. It will contribute to the growth of your business. You should be able to clearly define what your support network is, and allot some time for managing it efficiently.

3. You must positively respond to the increasing demand for product quality and services. By adding value through quality improvement, you would be in a better position to charge premium prices. Needs and especially wants of your customers should define the quality levels of the product. Every person concerned with your business should be aware of the definition of quality and the ways to implement it. Businesses which have quality as their competitive advantage will be in a better position to maximise the profits.

You must understand the definition of quality in terms of a documented quality system such as BIS mark or ISO 9000, and be committed to achieve it. The product which you manufacture should have a distinctive range of features. This is only possible, if your business responds to the customers' wants consistently and continuously. You can also attempt at changing the beliefs and attitudes of your customers by integrating them into the process of change. This would help them to easily adapt.

Quality improvement should necessarily entail a price rise, higher than the product of the competitor. This would reflect the benefits provided to the customer. If you have taken into consideration the quality consciousness of your customers, the increase in prices will not affect their demand for your product.

4. You must establish functional systems, both formal and informal, to provide quality information in order to enable effective decision making. Your business must be able to identify and acquire critical information and communicate the same to all people concerned with the business.



Computerised systems of information on suppliers, customers, markets and opportunities would provide a clear competitive advantage to your business. Such systems should be constantly upgraded and improved upon.

With the help of customer perception surveys, the performance of your business could be evaluated. It is important to monitor and document your performance and communicate it to all concerned.

Based on the assessment of your business performance you need to take immediate action to bridge the shortcomings. Taking action should be an integral part of your business culture and appropriate incentives should be given for taking positive actions. You must remember that taking actions should be a constant process and should not be done on an ad-hoc basis.

## SAQ 4.2

i) Classify the three types of competitors to your business.

a)	_____
b)	_____
c)	_____

ii) List the alternative strategies which can help you to remain competitive.

a)	_____
b)	_____
c)	_____
d)	_____

iii) List the group of people with whom you should have partnership relations.

a)	_____
b)	_____
c)	_____
d)	_____



iv) Identify the important steps involved in quality improvement

a)	_____
b)	_____
c)	_____
d)	_____

v) What steps should you follow to assess your performance and what should be your actions once you have assessed your performance?

--

## **The Plan Ensures Your Growth**

Instead of just responding to changes in environment, you should actively pursue in initiating change. Despite the possibility of committing mistakes while implementing change, you should constantly try to stay in tune with the changing world. In an increasingly competitive world, people working for you will continually strive to determine their prospects and growth in your business. If your business does not hold any promises for them, they may leave you. It is important to note that mere survival is just not sufficient. You must grow and develop and eventually establish an empire. You definitely would like people to remember you as an achiever for years to come. Your planning for success apart from helping you become competitive, should aim at increasing your profits continuously over a length of time. So now we shall examine a vitally important issue. How do you develop your business?

You have before you three alternatives in order to develop your business:

- i) expansion
- ii) diversification and
- iii) merger.

In case you continue with your line of production, you can expand your capacity to produce more. This can be done if the demand for your product is on the increase. If your customers are satisfied with the quality and service you offer, their demand for your product will increase. Alternatively, you may explore new markets where there is a demand for your product. You could even successfully manage and improve the corporate identity of your business by creating trust and goodwill. Your image which supports your business objectives will help in generating opportunities for expansion.





In course of your business transactions, you may be able to identify new opportunities which are consistent with your core skills. You should immediately explore them. If you delay doing so, your competitors will take over. Therefore you should act fast.

Incorporating customers in the process of identifying your core skills would help in developing these core skills into new opportunities. You can even attempt at converting individual idiosyncrasies into new opportunities. Once you have identified a new viable opportunity, you must diversify your business into producing the new product. This is being "innovative". Innovation assures handsome profits because you will keep enjoying high profits till a competing business unit enters your line of manufacture. As and when you sense a stiff competition emerging in your business arena, you must try to innovate by producing either another new product or a new resources or by adopting a new technology which brings down the cost of your production. This process is continuous. If you falter at any stage, then you cease to be an entrepreneur. Remember, pursuing new opportunities is your major function. You cannot compromise on that.

When there is no scope for expansion or diversification, you should either consider acquisition of a competing business unit or amalgamation of your business unit into the competing one. This is called a merger of two units. Which alternative to pursue is dependent on the strategic and financial position of the two units. In either of these situations, you stand to gain. The strengths of one business will compensate for the weaknesses of the other. Contrary to popular belief, merger is not a losing option. In fact, it safeguards you from risks and helps you succeed.

### SAQ 4.3

When should you adopt the following strategies of growth?

Expansion: \_\_\_\_\_  
Diversification: \_\_\_\_\_  
Merger: \_\_\_\_\_

## It Pays to Remember

1. Planning is a very useful and productive technique. You will realise it, only when you start implementing it. It will provide direction to your actions. It also helps in evaluating your performance periodically. Even if your plan is a long term one, it will help you to check and verify your actions at shorter intervals.
2. As an owner-manager, you should draft plans for the future well-being of your business after careful considerations and analysis. You will be able to draft a realistic plan only when you take into account facts and figures collected through standard and reliable information sources. However, do not get obsessive with numbers. The main aim of planning should be to specify what you are going to do or what your actions would be in order to achieve the set-goals.



3. Agility and flexibility with which you can respond to change are the two most functional tools on which depends the growth of your business. Even though you are required to be very positive and decisive in policy matters, rigidly clinging to a strategy once adopted is often harmful for growth. You have to adapt to the changing situations and hence, should not hesitate to try out alternative strategies. You do not always have to work perfectly and qualitatively. Your aim should be to win over your competitors and consequently earn reasonable amount of profits in the long run. If that calls for a compromise on perfection, you should not attach or give too much importance to any preconceived notion or dogma.
4. Whenever you implement a plan, you will realise that it helps you in developing your business while preventing all possible crises. As a small businessman, you will encounter several crises throughout your business life. What these crises are and how planning helps in managing them will be explained to you in the following chapters.



# UNIT

## 7

### Contents

#### Chapter V

1. How and Why does Starting Crisis Occure
2. How to Avoid the Starting Crisis

**The aim of this chapter is to:**

- caution you against the starting crisis of your business

#### **Objectives:**

On completion of this chapter you will be able to

- diagnose your business for possible starting crisis
- take action to prevent starting crisis



This and the subsequent three chapters attempt to make you aware of some precautions you should take to avoid getting into difficulties and problems in your enterprise earlier. Thousands of small scale industrial units come up every year and a considerable number become sick and die within the first two to three years. It has been found that every business, sometime in its life, faces certain specific problems. We, through our experience, have identified seven major ones and we call them 'Seven Crises'. Not that every business faces all the seven crises, but at least some of them do sometime or the other. Do not lose heart. We are going to tell you how to ward-off at least those crises which we feel are relevant to you as a beginner. These are starting, cash, delegation, leadership and financial crises.

## How and Why Starting Crisis Occurs

You are going to set up your enterprise and at the start-up stage itself, you have to be aware of and careful about a number of aspects which are likely to affect you in your business. Otherwise you may face the 'starting crisis'.

It occurs when:

1. You do not have an adequate and all round experience or understanding of the managerial aspects of the business line you have chosen.
2. There is no proper arrangement for keeping accounts, and hence you cannot have financial information for making decisions.
3. Your estimates of the money required for the business turn out to be below the required level.
4. Your ignorance of taxation, particularly sales tax.

Let us look at each of these in detail:

1. It is a known fact that when you set up your enterprise as a small scale entrepreneur you cannot afford to employ managers or personnel for the different functional areas. Which means that you are owner, personnel manager, marketing manager, production manager, finance manager, etc. -all in one.

If you make a mistake in any one of these management areas, it would mean monetary loss. So it is essential that you know everything about your industry. This can be made possible if you are either qualified for this through education, work experience or make up for the lack of these two by gathering knowledge on your own.

Let us look at the case of the salesman who had a long experience of looking after the sales of an industrial firm. One fine day he felt that the firm was successful because of him and his marketing skills. So why work for a salary? Why not start an industry of his own and make a lot of money! So he set up his own enterprise and took a person with manufacturing experience to join him as a partner. So far so good. But he did not understand anything about finance and costs. He neglected them and ended up selling his product at a price below the cost of production.



This is also true of engineers and technicians starting their own ventures. They know how to manufacture a product, but when it comes to marketing, they generally fail. And lacking knowledge of finance and its management, they eventually fold up.

There is another example of two sons of a businessman. Both had degrees in business administration from a very good business school. They decided to set up their own industry. They came across a person who had developed a new product. This new product seemed to have a market too. So they set off. But it took quite long to develop the new product and start production. By this time, they needed more money and asked their father for it. This went on for two years and they kept on asking for more money. Their father finally got fed up by these demands and refused to oblige. By then, due to the delay in delivery they lost the demand for their product. Finally the unit was sold off to an uneducated but experienced person who started producing what he knew well and made a success of it.

The examples on the right show that you have to know all aspects of an enterprise you intend to set up. What we mean is that a lack of all-round management experience is cause of failure of a business.

You should have experience in or understanding of the specific line of business which you take up. There are cases of people who venture into a business as others are doing well in it. This is called the 'me too' syndrome. But if you do not have understanding of the business or relevant experience, the outcome is failure. So do not plunge into a business seeing the success of others.

2. When a new entrepreneur sets up an enterprise, he/she feels that he/she cannot afford an accountant. He/she also thinks that he/she knows everything about the business and need not spend (waste) money on an accountant. But the fact is that most of the entrepreneurs lack understanding of accounts and do not know what financial information they must have to manage their business well. They always keep themselves busy with production or marketing of their products.

We asked a high ranking officer of a bank as to what his best advice to a new entrepreneur would be. He said 'invest some amount to engage a good accountant as soon as you start your venture'.

Look at this owner of a construction business. The business was one or two years old and he thought that he was making good profit. However, at a latter date he was told by the accountant that his business was running in loss. He just could not believe this. He immediately engaged a finance expert to do audit of his business. The expert studied the accounts and confirmed that he was really making losses. The owner was under wrong impression that he was making good profits.

What had gone wrong here ?

The owner had not included depreciation of two items of his equipment (because no money had actually gone out). He had not taken into consideration the salary of his wife who was helping him in the business (she had left her job to do so). He had not remembered the overtime paid to the workers. Interest on the capital brought in by the owner was also not added.



And this is not an isolated case. If you talk to a banker who advances funds to industry, the first thing he would tell you is that owners of most of these businesses do not have a clear idea about the actual costs incurred by them for their business. As a result they run short of working funds.

What you can learn from this is that only with proper accounts you would have a clear idea about the actual cost of manufacturing the product you have selected. And you would also know how you arrived at the figures of your profit/loss.

3. Be always careful about making a correct estimate about the investment you would require for your project. Otherwise, one fine day you are going to discover that you are short of money halfway through and have either to give up or borrow money at a high rate of interest. Correct investment estimation will help you avoid other problems like no-money-left to buy raw material or to pay wages.

This reminds us of the case of an enterprise manufacturing electronic items, described on the right.

Two partners set up a unit to manufacture electronic items. Both had a good background in designing such items while working for a large company. Each of them invested his entire life savings in the enterprise, and also borrowed money from relatives and friends. Their idea was to take sub-contracts for some items so as to ensure steady income and also to develop and manufacture certain new products. But the money they raised was not enough to manufacture even the routine products. One partner had to devote for quite a few months all his time in raising money. The result was that they could not start production of new products at all, and started blaming each other for it and quarreled. Finally the unit was sold to a large unit at a loss. Of course, this shows not merely underestimation of funds required but also poor management.

One of the common mistakes made by new entrepreneurs is underestimation of working capital requirements. It is desirable that you consult your bankers about the amount of working capital required. This way you could know not only the requirement but also the amount which you will have to put in as working capital margin.

We would go further and say that if your margin is to be 'X' amount, you should provide for 'X+', i.e., little more than required amount to be on a safe side.

4. Lack of knowledge about taxation as applicable to small scale industry could make your enterprise sick in two-three years.

Generally small entrepreneurs worry about income-tax which is to be paid on profits, but they forget that there are taxes like sales tax, excise tax etc. which one has to pay even if there are no profits. Even if you are making a loss but selling your goods you have to include sales tax when you charge your customer, and then pay up the amount thus charged to the Sales Tax Department.

So, be sure you familiarise yourself with various types of taxes payable by your enterprise before you start your industry.



We shall narrate here the case of a technocrat who lost his unit just because of his ignorance about sales tax liabilities.

A technician set up his electronic motor-winding unit. He had previous work experience in an engineering unit and knew all about the technical aspects involved. But he did not know anything about sales tax liabilities and the Sales Tax Department. After he started his unit he bought the raw material from suppliers without proper bills. After some years of working like this the Sales Tax Department became aware of the fact and he was made to pay sales tax right from the day he had started production and sales, up to the date he was contacted. And this was not all, he had to pay interest on that amount and a penalty. The poor man's unit was auctioned off to recover the dues and all his property was attached. A very heavy price paid for ignorance!

### SAQ 5.1

Present your knowledge in two sentences each, on the factors that could lead your business to 'starting crisis'.

1.	_____
2.	_____
3.	_____
4.	_____

## How to Avoid the Starting Crisis

Do not lose heart -you can avoid all these mistakes. You can take precautions, take advice from experts, bankers etc. and most important of all, prepare yourself by learning as much as you can about your business.

Here are some tips:

### 1. Listen to all available advice

You and every new entrepreneur for that matter, are very enthusiastic when you set about putting up your unit. You make plans and projections. But in most cases these are too optimistic.

We have found that generally entrepreneurs overestimate their sales turnover and underestimate expenditure. When you are in the process of setting up your enterprise, please think through questions such as 'who will buy my products and why? Why the customer who has been buying



the products from other suppliers till now should leave them and buy mine?' You may think that the quality of your product is better than theirs or as good. But who has to judge that? Not you, but the customer. Also remember that a cheaper price is not always the criterion for a customer to buy a product.

- i. Sleep over your scheme. Once you have prepared a report of your project, do not be in a hurry to submit it for a loan or to start the process of setting up. We understand that in your enthusiasm you would be in a rush to start of. But you should let some time pass and give some more thought to your plans and projections. May be your second look and the changes that you make would be more realistic especially about the capital needed for your project.

The time is yours before you start your project. Once you begin the process of setting up, you will not have time or opportunity to change your decisions.

- ii. When planning for the investment required for the project, you should be a little conservative. Go through every item minutely. In brief, be frugal when you estimate your income and lavish when you estimate the expenditure. Play safe.
- iii. Get your project/project report scrutinized by bankers and consultants and those who are directly or indirectly interested in your project. Their advice on the weak points in your project and how to take care of them could benefit you.

Bank officers say that a typical small scale entrepreneur never came to meet them until his unit got into problems. And he would never discuss his project-plan with the bankers before taking various decisions.

## **2. Organise up-to-date business information**

Before you start your enterprise you should set up a system to get good financial information on production cost, income from sales, profit/loss and cash flow in a reliable manner. This system should be such that you get the information periodically. It would help you know the outcome of the business decisions that you want to take or have already taken. Without such a system you would not know the outcome of your decisions. Consider the expenditure involved not as cost but an investment. And of course, engage a good accountant too.

## **3. Encourage participation of investors**

Whenever you start looking for additional capital for your new or even existing enterprise, make sure that you identify the right type of investors from whom you can obtain as much finance as you possibly can. One reason for this is that these investors, who could be the state financial institutions or developmental banks, would examine each and every aspect of your scheme thoroughly and objectively. Besides, these investors do not panic easily. If you are in some temporary financial trouble and cannot keep up with your repayments, they do not withdraw their support. While if you borrow from private investors and are in financial trouble they would immediately ask for their money back and harass you. And this way they may also indirectly ruin you.

Do not be secretive. Share your financial problems with the financial institutions/bankers. Take their guidance and advice and financial help. If you keep them informed of your real situation, lack of finance would not hinder the growth of your unit.





#### **4. Meet your tax consultant or officer often**

When you start your enterprise do not rely too much on your accountant or managers in matters of tax liability, let them do the routine work like writing accounts or filing sales tax returns etc. But acquire knowledge yourself and monitor their work. And before you start your enterprise, check what tax laws are applicable to your line of business, and what benefits or refunds are available to you from the government. Make it a point to often discuss this and other related matters with your tax officer.

Do not forget that income tax is payable by you when you make profits but sales tax is payable by you on sales that you make. It is irrespective of the fact that you might have made a loss. So, you should not underestimate its importance. Besides, there are other taxes like excise and octroi etc. applicable to your enterprise. So get to know all about them.

#### **5. Estimate the investment figures realistically**

We have already talked about making realistic estimate of investment in your project; also what happens if you underestimate it. It is easy to make estimates of investments in land and building; they can be checked easily. But estimate of investment in plant and machinery is often made with less care than necessary.

When you select machines for your project, it is a long term decision. You are going to use the machines for years. You cannot easily change your machinery once you have selected it. Yet we have seen entrepreneurs who take the decision without due consideration. They look at the machinery used by similar units or their competitors and purchase the same. 'If it is O.K. for them, it is O.K. for us'. This is short-sightedness.

Let us give you a typical instance of how an entrepreneur took the decision about the machinery for his project and got into trouble.

Mr. Jaiswal put up a ball-bearing project. He decided to buy eight turning lathes for turning rings of the ball bearings. He took this decision because an earlier project for manufacture of bearings also had eight turning lathes. He did not think of any other aspect. For example, he did not consider whether buying the rings from outside would be cheaper than making them. After he started production, he found that the cost of the turning rings was almost double than the price quoted by a neighbouring unit for the same rings. Where did he go wrong?

The earlier project had these lathes because it was located in an area without any ancillary unit nearby making the rings. So the owner had to make them himself. Besides, it manufactured different bearings with higher accuracy.

The result was that he stopped production of the rings and all the eight lathes remained idle.

So here is an example of selecting wrong machinery. He did not give thought to anything else, but went by the example of another unit.



This is an example of electing wrong machinery. Mr. Jaiswal did not give a thought to anything else, but went by the example of another unit.

This can also happen when you select a machine without considering its production capacity aspect.

Suppose your market demand is 10 tonnes per day you purchase a machine with 50 tonne capacity. What happens if there is a waste of the capacity till you are able to generate that much demand (market)! And when you get the 50 tonne machine you obviously have to pay more. As a new entrepreneur you cannot afford this. So do not rush; think and then decide.

The fact is that the decision to purchase machinery requires careful thinking. We suggest here some questions, which you should be able to answer for analysing your selection of the machinery. It is a kind of a checklist:

- Does the machine have specifications of performance that I need?
- Does the machine need skilled labour? If yes, can I get required skilled workers in the area where my unit is going to be established?
- Are the specifications of the machine compatible with those of other equipments in my proposed unit?
- Does the process (built into the machine ) generate effluent? If yes, how can I treat the effluent and at what cost?
- Is the technology of the machine appropriate to my needs and my environment?
- How effective is the after sales service? How much does it cost?
- Is the machine energy efficient?
- Is the machine within my budget?
- Can I avoid buying it altogether?

## SAQ 5.2

What do you propose to avoid 'starting crisis'?

1. _____
_____
2. _____
_____
3. _____
_____
4. _____
_____



# UNIT

## 7

### Contents

#### Chapter VI

1. How and Why Cash Crisis Occurs
2. How to Avoid the Cash Crisis
3. Two Categories of Cash

#### The aim of this chapter is to:

- caution you against the 'finance crisis' crisis of your business

#### Objectives:

On completion of this chapter you will be able to

- diagnose your business for possible cash crisis
- take action to prevent cash crisis in your business
- select appropriate source(s) of finance for funding growth



Many small entrepreneurs are so engrossed in production, marketing, profits and growth that they do not realise that their entire business depends on availability of cash. Only if they have adequate amount of cash then they can achieve their targets. That means they run into cash crisis.

The important points is that they become aware of it only after they get into it. We do not want you to get into this problem.

## How and Why Cash Crisis Occurs

The reasons for the cash crisis are:

**1.** Excessive attention to profits and sales growth rather than cash-on-hand; over-investment in raw material stock, rising outstanding amount. When an entrepreneur sets up his/her business, what does he/she generally concentrate on? Increasing the market and making profits. But then he/she forgets one important aspect-keeping adequate cash on hand (which includes cash in bank also) for requirements of raw material, wages, utilities and any contingencies which are required for profit/sales growth. That lands him/her in trouble.

Sometimes entrepreneurs buy up a lot of raw material and block most of their money in that.

They may also extend credit to customers and if the recovery is delayed it causes cash shortage.

**2.** Excessive investment in fixed assets by tying up funds. When an entrepreneur, on getting loan for land, building, plant and machinery, goes all out and without thinking, spends so much money on these assets that later on he is starved of cash.

**3.** Unplanned expansion in time and stages. It also happens when an entrepreneur, once he/she starts doing well, goes in for expansion without considering whether the time is right or whether he/she has adequate cash reserves/resources for it.

When your business grows, you require more money for raw materials. The number of your debtors, those whom you have given your goods on credit, also increases. The result is shortage of cash in hand.

Let us take the example of an electrical goods manufacturing company:

The three partners of that company worked day and night to establish production of three new products. Finally they succeeded in it, but the income from the sales was much less than expected. Three of the customers on whom they depended for orders, could not order the products due to various reasons.

After sometime they could succeed in getting good orders for two of their products. But by that time they were short of cash. They did not even have enough money to pay wages to their workers, purchase raw material or meet any other production cost. In fact they had mortgaged all their fixed assets by this time. To buy more raw material they even mortgaged on remaining piece of property. In spite of this, they felt shortage of cash.



Then the partners rushed to their original investors for more funds. But, the investors too did not have surplus funds. By this time they were worried whether they would get back the money they had already advanced.

Then they tried their bankers. As they had enough orders on hand, they were confident that they would be given finance. The bankers however hand their doubts. The company was 'red' - loss making. One customer, whom they contacted also gave adverse opinion bout the company's products. So they also did not loan them any money.

This, as you can see, it a classic case of underestimation of working capital required. Had they concentrated on only on product at a time an the market for it., there would not have been such problems.

Giving too long a credit to customers also causes cash crisis - or shortage.

One textile mill in Ahmedabad was experiencing working capital shortage in spite of good sales. They engaged experts to identify the reasons for it. Experts studying the working of the mill observed that a large amount of the mill's funds was blocked in debtors. As a result there was a chronic shortage of cash on hand. The credit period in the textile industry in 45 days. The mill management allowed a period of 120 days. The directors of the mill did not take notice of this phenomenon. They were concentrating on production. And hence the problem.

Here is one more case where a manufacturing unit experienced cash shortage because it had blocked a lot of money in raw material.

A small scale unit manufacturing electrical laminations and stamping located in Ahmedabad, always experienced working capital shortage. The proprietor consulted some experts. The experts discovered that he had invested a considerable amount of money in stocking raw material. The unit manufactured thirty varieties of stamping and 8 varieties of laminations. For this it required three different varieties of special electrical steel. As some of these were in short supply, the proprietor kept a large stock without thinking of his real requirements. What he should have done was to calculate the requirement of each variety depending upon the production quantity of the various items. But he had not done this. His forte being marketing, he concentrated on that.

So, keep all this in mind when you start your own industry.

## SAQ 6.1

Present your knowledge in two sentences each, on the factors that could lead to 'cash crisis'.



1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_

## How To Avoid The Cash Crisis

Here are some tips for a avoiding cash crisis:

1. Understand the relation between profit and cash on hand.
2. Constantly watch for ways of economising on cash.
3. Consult a good accountant, bankers, financial experts.
4. Constantly assess cash position, prepare cash flow statements in advance every three months.
5. Monitor raw material stocks, semi-finished goods, inventory of finished goods and outstanding recoveries.

We think the above five are self-explanatory and we need not go into details. But remember, the first and foremost way to void this crisis is that you should keep a watch on the amount of cash on hand which includes money in your bank account. You should also prepare a cash budget, say for a period of six months. You should review and revise the budget every three month. The estimated figures of income should be checked with figures of actual income. This way you can avoid errors.

Actually what you should do is to prepare a complete cash-flow statement for a period of three months or six months. This statement can, at any given moment, tell you about your cash position, whether your out going amount is more than the incoming one or the other way round . If you have less cash in hand than required, you have to think of ways of obtaining it. But it is necessary, rather essential, that you are aware of it beforehand.

Ready-made forms for preparing cash budgets are available in the market. They are useful to analyse the past as well as a projected budget item.

More importantly, when you have this (analysis) in your hand you can think of ways to see to it that you have cash on hand. For example, you can purchase your raw material at a discount during slack season and be more vigilant about giving credit. Instead of purchasing land,



building and machinery you can rent or lease the same or out source some of your production and thus save on expenditure which can be avoided.

Moreover, this can help you decide which product to concentrate on, if you are going to manufacture more than one product, depending on the profitability and market demand. And if there are any contingencies and you require immediate cash, you will be prepared for them.

A good accountant can help you learn cash management and set up a good cash management system. You might feel that the only way to avoid shortage of cash would be to acquire additional cash. But if you have a good accounting system which provides you with relevant information you can really operate so as to make best possible use of the available cash.

Remember, as in case of starting crisis, cash crisis can also be caused by underestimation of capital required for the project as well as faulty cash management.

## **Two Categories of Cash**

It would be easier to understand cash, if we divide it into two categories - 'long-term capital' and 'short-term capital'. The money which you invest in fixed assets like land, building, plant and machinery etc. is called 'long term capital'. While the cash that you invest in raw material, work in progress, finished goods, working expenses and debtors is 'short-term capital'.

Remember that unless you keep a close eye on the five above items of short-term capital, you will end up with cash shortage. And if you do keep such a close eye, you would rarely face cash crisis. Let us now discuss these items one by one.

### **1. Raw material**

You should purchase only minimum requirement of raw material. But if the material is available under quota system or is usually in short supply or seasonal, then it may be necessary to stock the material. In such cases the best thing you can do is to go to your banker in the beginning itself. You can discuss the situation with him and ask for necessary working funds. But, otherwise, never stock more than the quantity required.

### **2. Work in Progress/Process**

Work in progress means the production time taken in converting your raw material into finished goods. Some types of products take more time in process and some others less. You should keep your inventory based on this factor, that is the taken for conversion.

You should also try and avoid a mistake commonly made by small entrepreneurs. Sometimes an entrepreneur gets an order for manufacture of a special item which he/she normally does not produce. Then he/she stops the regular production work and uses the machinery for making the special product. Avoid this. You must first complete the manufacture of your regular item/s in hand. Then only you may consider taking up the special product. Otherwise, you are likely to face the cash crisis.



Take for instance, there are five machines installed in your factory to manufacture one or more product/s. Now, if you decide to manufacture another product on the same machines, the machines can be used for the purpose, but you might have to change the settings and the tooling of the machines to suit the manufacture of that particular product. What does this mean ? Waste of time as well as piling up of the raw material of the regular product and of course a possible shortage of that finished product. Which in turn would mean less sales and you might not be able to recover the loss from the sale of the special product.

So it is wiser not to disturb your regular production work for the sake of short-term gain from manufacture of the special product.

### **3. Finished Goods**

This is another aspect you have to be careful of. See to it that the stock of finished goods does not accumulate. Decision for this can be taken depending upon the size of your regular orders and market. If it so happens that your flow of orders is reduced, go and check the market - your customers - and find out the reason for it and if possible, rectify. Always talk to your customer about his needs and his expectations from your product and try to satisfy them.

### **4. Working Expenses**

You might recollect from Unit 2 that working expenses also form a part of your working capital. These include wages to be paid to workers, cost of utilities, repairs and maintenance, etc. and adequate provision has to be made and kept aside for these too. Otherwise, you will end up with shortage of cash.

### **5. Credit Collection**

You know from the example of the textile mill given to you earlier, what happens if you give too long a credit to your customers. Besides this, you have to make sure about timely collection. While we are at it, be always sure to check your customers for their credit worthiness. If a customer places an unusually large order, check for the reasons for such an order. It does happen that a customer is on the verge of winding up his business and he acquires a large stock of goods from his supplier, which can be you. And you end up losing your money as once he has wound up, you cannot collect.

So, ensure that you keep control on these five areas and you will not face cash shortage - crisis. And importantly, be up to date about information on financial matters. Our advice would be to get weekly information from your accountant on key financial matters.

**SAQ 6.2**





A) Distinguish between short-term and long-term capital.


B) What do you propose to avoid cash crisis ?

1. _____
_____
2. _____
_____
3. _____
_____
4. _____
_____
5. _____
_____



# UNIT

## 7

### Contents

#### Chapter VII

1. How and Why Delegation Crisis Occurs
2. How to Avoid Delegation Crisis

**The aim of this chapter is to:**

- caution you against the delegation crisis of your business

#### **Objectives:**

On completion of this chapter you will be able to

- diagnose your business for possible delegation crisis
- take action to prevent delegation crisis in your business



We would like you to know and put into practice one important adage - 'delegate'. Always delegate your work and responsibilities when you find that you, on your own, cannot cope with them. Do not be afraid to delegate - that is, to share work as well as decision making authority, powers etc. when you need another set/s of hands.

Is it not better to delegate and increase your work efficiency, rather than create a situation of chaos or mismanagement?

## **How and Why Delegation Crisis Occurs**

At some point in the life of your enterprise, you reach a level of operations when it becomes difficult for you to do everything single-handedly. You have grown. At the same time you cannot hire managers for each functional department yet. What you should do then is to look for someone to whom you can delegate some of the responsibilities. This would leave you free to look after the essential and more important matters.

This need generally arises when the number of your workers goes beyond twenty. The number of workers can be lower or even higher depending upon the nature of your business. For example, if the production process of your business is simple or if you have only one product and the market consists of a few big customers, then perhaps you can possibly control the whole thing yourself even if the number of workers you employ is much higher. But if the production process is complex or your market is widespread then you may need another person to help even if the number of your workers is less than twenty.

You will ask 'why would I have a crisis just because part of my responsibilities need to be delegated to someone else?'

There are three main causes of this crisis:

1. Inability to delegate responsibilities and share decision making burden
2. Psychological problem (only I can do better, lack of capability to guide and groom others, a lack of trust in subordinates).
3. Business grows, responsibility grows, time does not - business suffers, success end up in failure.

The problem is that some entrepreneurs just cannot delegate. They either resist or postpone delegating under some excuse or the other. Their attitude and mindset prevent them from delegating responsibilities or even tasks - work. They feel that they have to do everything themselves, take all decisions - they do not want to lose control. They do not trust others. As a result their business suffers when they fail to attend to the growing workload all by themselves.

Initially, when you set up your own independent enterprise you not only take all the decisions yourself but also do all the managerial and other work related to the enterprise. You also put in, in most cases, all your savings as your part of investment in the project. So, your enterprise is your own baby - you bring it up, you nurture it, you put your blood and soul into it. How could you entrust it to anybody else? That is understandable. But at some point in the life of your



enterprise, you will have to accept that a change or changes are needed, you cannot look after everything yourself. You have to delegate some important tasks to someone else.

If you cannot, it is to your disadvantage. It might even mean the ruin of the business you have set up with so much effort and love. You would become so harried that you would not be able to function effectively. You would even begin to snap at your customers, your workers and even your family members because of work pressure, tension etc.

You must always remember that once your business is on the way to growth, you cannot stop and if you take any wrong decision about new orders or growth in production, what happens? You lose good customers and of course money.

We shall narrate a case which is a good example of entrepreneur's inability to delegate.

### **Case : Inability to Delegate**

Ramesh, a technician, worked for a number of years in a precision instruments company. While working there, he acquired experience in almost all functional areas of that business. Then, he set up his own manufacturing unit for the same products. After five years, his earnings reached a considerable high level. He also employed thirty workers. Ramesh had good entrepreneurial competencies. He was also ambitious. On the advice of his bankers, he floated a public issue to enable him to expand. His bankers advised him that he was too talented to remain a small scale entrepreneur, he should become an industrialist.

Ramesh raised Rs. 3 cores through the public issue and added a lot of new machinery etc. in his unit. But with this expansion he had to make more efforts to sell his products. Before he went in for expansion he had a few large loyal customers and it was easy to deal with them. Now that his production had increased he had to sell the products to wholesale dealers and many retailers all over the country.

It was obvious that a sales manager had to be appointed. But Ramesh was reluctant. He did employ a sales manager. In fact there were five sales managers, one after the other in two years. But he either sacked them or they resigned, as he did not allow to work without interference.

Ramesh had, thus, to look after both production and other matters as well as sales. He could not cope. And for the first time in the history of his company, he suffered losses



## SAQ 7.1

Present your knowledge in two sentences each, on the reasons that might cause delegation crisis.

1. _____ _____
2. _____ _____
3. _____ _____

## How to Avoid Delegation Crisis

If you want to avoid this crisis there is a very simple way out. You can limit your business to such a level, that you can handle everything yourself. But is it a solution? Not if you want your business to grow, as it must, over the years.

We will suggest the following solutions:

1. Find or associate a capable second person to supplement 'you'.
2. Test him, watch him and start sharing responsibilities.
3. Consult with management experts or colleagues to identify your own weaknesses and select a second person who is strong in the management areas in which you are weak.
4. Be prepared to pay high salaries, give status, authority or share of profits to retain the valuable second person.

## Appoint a Competent and Effective Person

The main difficulty in implementing this could be that you may not be mentally prepared to loosen the reins and hand over some responsibilities of your business to that person.

We again repeat that the person whom you appoint or select, should be strong in the areas in which you are not very good. And please do not be afraid to admit your weak points.

If you cannot identify such a person, there are executive search organisations as well as consultant who can help. These organisations or consultant would talk to you, appraise you (your strengths and weaknesses), your company and its needs and arrive at the type of person who would be suitable for the purpose. They can even locate such a person for you and help your overcome your reluctance to delegate and accept new person.



There are many advantages in having such a person:

- He can share your burden
- He can help in smooth functioning of your unit
- Being strong in the areas in which you may be weak you can have the benefit of "all-round knowledge and experience".

But do not expect miracles. There can be a few problems:

- It might take a long time to find the right person
- Both you and the new person might have difficulty in working harmoniously
- If the new man is really very competent, he might expect a large salary or a share in the company

But remember that it is much better to have an 80% share in a thriving company than to have 100% ownership of a sick or loss-making one.

Let us have a look at 'Tushar Interiors' a furniture making company of Ahmedabad and what happened to them when they were not prepared to pay their export well.

Tushar Interiors was set up in the late sixties when most people in Ahmedabad were still not very conscious about decorating their houses with expensive furniture. But still the enterprise did well and made good profits. The owner, and later on his son Tushar, could very well manage the company.

But a time came when both the production and sale increased along with the population and its awareness about decorating its homes. The number of workers also increased. It became difficult for the father and son to manage the show. Luckily they could find a young man in Ahmedabad itself. Within a few years this man, Animesh, could really take over a lot of the management work of the business.

Then Animesh asked for a salary much higher than the one he was getting. The owner and Tushar requested him to continue and promised that he would be later made a partner in the enterprise. He agreed. After a year he again demanded a raise or a partnership. Again, they gave him a bonus and more empty promises. After the sixth year Animesh got fed up and left his job.

Not only that, he set up his own furniture manufacturing company. To-day he is established and making good profits. So is Tushar Interiors. But neither company is doing as well as Tushar was doing before the new company was set up.

One word of caution. Before you really accept the new person on a permanent basis, 'wait-and-watch' for a while. In short, there should be a kind of trial period before you make your final decision about taking him/her up on a long term basis with adequate financial rewards. you should get to know how well you work together and whether he/she really is the right person for your needs.



Often, it also happens that the person whom take on may also have money to invest in the business. In such cases, you have a double advantage - money and manpower. But again - a word of advice - Do not accept a person who has money to invest but does not have management skills. The requirement is mainly for a competent second-in-command and not merely money.

Do not over-delegate. You should occasionally check the person's performance of various tasks assigned to him.

Sometimes it so happens that you put full faith in the person and leave everything to him and that person misuses his powers. So monitor his work.

Take the example of 'How Ravi was Financially Ruinded'. He over-delegated and suffered.

Ravi was marketing manager for a large multinational engineering company in Bombay and well settled. But still he was restless. He was too independent minded and did not like working under somebody. One day he took the decision to resign and set up his own small scale unit. He resigned, came to Ahmedabad and started his own unit manufacturing the products which the multinational he was working in produced.

But he was new to Ahmedabad and Gujarat and weak in financial aspects of business. So, he took help from a cousin who was also a chartered accountant. This man, Rahul, was more than willing and agreed to work with Ravi. Ravi put full faith in Rahul and delegated all work related to accounts, sales tax etc. to him. And never checked anything.

A few years later Rahul died in a road accident. After his death Ravi, while going through Rahul's and the firms papers, received a shock.

He found that sales tax returns for a number of years were not filed and he had to pay a large amount in outstanding to the department. There were a number of entries falsely made where the firm had not received any money. But the money had been diverted by Rahul. Actually, unknown to Ravi, he had also set up his own venture manufacturing the same items.

As a result, due to his own negligence and over-delegation, Ravi was financially ruined.

In short, delegation is a must if you want to grow. But over-delegation or delegation without monitoring can be as dangerous as not delegating at all.

## SAQ 7.2

What do you purpose to avoid delegation crisis?

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_



# UNIT

## 7

### Contents

#### Chapter VIII

1. How and Why Leadership Crisis Occurs
2. How to Avoid the Leadership Crisis

**The aim of this chapter is to:**

- caution you against the leadership crisis of your business

#### **Objectives:**

On completion of this chapter you will be able to

- diagnose your business for possible leadership crisis
- take action to prevent leadership crisis





Leadership crisis is similar to the delegation crisis, we have earlier talked about. But this is not merely a matter of delegation, much more is involved here. You should be able not merely to delegate but also lead your personnel and your enterprise.

When your enterprise reaches a level when a team of managers is required to shoulder responsibilities of varied functional areas and workforce is increased to 150 or more, this crisis is likely to occur.

You would ask us to what is the necessity for us to know about this now? We will be just starting our small scale enterprise! And we would reach this level only after some years!

But our aim is to make you aware of all eventualities and prepare for them. The knowledge will stand you in good stead when you are a successful growth-oriented entrepreneur.

So, we shall tell you what happens, why and how it happens and you get enmeshed into the leadership crisis.

## **How and Why Leadership Crisis Occurs**

Leadership crisis occurs when:

1. You or your partners are not able to manage all responsibilities and have to delegate to the managers not merely your tasks but also quite a few of your responsibilities.
2. You fail to develop a management team. You have been till now successful as an owner/manager. You are used to looking after all the areas of your enterprise, viz., marketing, production, accounts, finance etc. and you have been managing fine till now. But is it possible now - with such a grown workface - to look after everything yourself? Or to take each and every decision yourself? No! You have to appoint professionals to manage these various functional areas and delegate powers and responsibilities and groom them to replace yourself in managerial tasks.
3. You fail to change your management style. You have to learn to change the way you manage your unit or company. Your small unit has undergone a transformation. Now you have to become a leader instead of a 'do-it-yourself person'.

To be more specific, you have to make the following changes:

1. Delegate more powers to other people.
2. Instead of doing all tasks yourself develop yourself to be an effective leader.
3. Keep control over your enterprise through efficient paperwork and information system.

We will again talk about delegation now - but here the delegation is very different. When you are facing or are likely to face the leadership crisis, you have to delegate most of your powers and responsibilities to your competent managers. You should delegate the responsibilities of almost all of your functional areas.



## Being an Effective Leader

Being an effective leader means that you have to become a guide and leader to others. You do not have to deal directly with most of your personnel. As an owner manager you are used to directly interacting with, say for example, your supervisors, salesman etc. All this has to stop now. You deal directly only with your team of managers. In short, you have to keep away from the functioning details of your company.

Besides, to ensure a smooth running and growth of your company, a two-way communication between the management and personnel has to be established. This way the policies of the company can be made known to everyone; and at the same time there is an upward flow of information from the personnel.

Keep one important thing in mind. The goals and objectives of the company should be made clear to all managers. They should also be clearly explained their roles and responsibilities. You now become only the planner and thinker of your company.

### Managing through effective written communication

As we earlier mentioned, you have to be in direct touch with or manage only your team of managers. This communication with them should be in the written form. Day to day interaction would be a waste of time. Apart from this in oral communication there is a possibility of distortion of the message.

We understand that as a small scale entrepreneur you are an action -person and would hate 'paper work', but it becomes necessary and important now.

We would give you one example of the leadership crisis, where the outcome was disastrous.

#### Case: Inability to change management style

Mr. Pillai was the works manager of a medium scale unit manufacturing textile machinery components. He, however, was not satisfied with the fat pay package and good working conditions. He, was bitten by the bug of entrepreneurship and independence. He left his cushy job and set up his own venture making the same products. He was not merely good at production but kept good relations with his workers too. Market was also not a problem. But he was ambitious too and gradually expanded his production as well as his market- from local it became national.

This meant a grown workforce, managers for all functional departments and controlling all of them. And there he failed. Instead of leaving all day to day working of his new medium scale unit, he tried to see to everything himself and interfered in everything.

He stretched himself too much physically and mentally. This taxed his health. One day he got a massive heart attack. He was saved but his doctors advised him a long bed rest. They also asked him to take it easy for the rest of his life. As he had no son to take over, he had to sell his business.



## SAQ 8.1

Present your knowledge in two sentences each on the factors that could lead your business to 'leadership crisis'

1. _____ _____
2. _____ _____
3. _____ _____

## How to Avoid the Leadership Crisis

Let us have a look at how to face or avoid this crisis:

1. Train, discipline and re-educate yourself in new management skills and style for growth.
2. Old knowledge and management as a small scale entrepreneur and personal physical check on everything would not work.
3. Act more like a leader than owner/manager/supervisor
4. Constantly evaluate how you spend your time
5. Concentrate on business strategies, planning for future, competition, government policies etc.
6. Develop a team of executives, give them authority.

Of course there are no quick solutions to the problem of leadership crisis. The experience has been that only 10% to 20% of the entrepreneurs can make the necessary change in their management style. There is one class of entrepreneurs who, however hard they may try, are unable to change. They do understand the need for the change but they do not unfortunately have a mind flexible enough.

There is a large number of others, owners of small scale units, who do have a potential to change once they face this crisis. You should belong to the group, who if he tries hard, can change. How?

- i) **Obtain training in management:** Till yesterday there was a traditional approach to management. Training meant that you acquired experience and learnt on the job. To-day's approach is to learn it in a management school. And one has to admit that the traditional old approach is lacking in several respects, especially with the changed industrial scene.

A large number of entrepreneurs have begun to undergo training in management at seminars being organised by universities chambers of commerce and industry and other training institutions.



Attend short term training programmes and seminars conducted by management schools or management associations. You can attend programmes in the area of your interest - whenever you can. These programmes not merely give you some training inputs on how to behave, the effect of the behaviour on others, look into yourself (self-assessment) but also some change from the routine. Interaction with other like minded participants also would help.

**ii) Develop the qualities of Leadership:** As has been said, 'leadership is to business what oxygen is to life'.

If you want to change in order to become a better leader, you have to take stock of how you behave with people around you and how you deal with them. This itself will bring changes in your behaviour.

Have you ever thought of how one wastes time in unnecessary meetings, conferences and having a so-called open door policy? A number of entrepreneurs engage in such activities and other similar behaviour. And they consequently neglect what they really should be doing.

Always remember not to form such habits. And if at all you have, try to get rid of them. No one is going to point this out to you. You have to realise yourself. We accept that this is not easy, but try - try hard.

You will ask: how can I become a good leader?

All we can say is to have a tough style of leadership when you deal with people who like to be told at every step what they have to do and who are not themselves motivated enough to do. While with people who know what they have to do and how to do, you have to become a kind of facilitator. Which means, being there to help only when needed. So it depends on the people you lead and also the situation.

Here is a check-list which can help you.

1. A good leader inspires a vision amongst those who work with him/her. He/she makes them share the overall aims of his/her enterprise.
2. He/she strains every nerve to inspire confidence in his/her people and makes them effective through mutual trust.
3. He/she makes effort to ensure a high quality of work life in his/her enterprise.
4. He/she listens to the employees and communicates with them effectively.
5. He/she leads by setting example. Personally, he/she is a fountainhead of energy, enthusiasm and commitment. People love to work with him/her and for him/her.

Do you think that reading practical books on effective leadership will help? Gaining a few tips and hints on leader behaviour, you can change your ways of thinking and behaving? No.

Take our advice and consider the suggestions we are going to give you. And please take some action on these suggestions.

**iii) Conduct a feedback survey:** Conduct a feedback survey among your employees to find out what they really think of you. This can be done through professional experts who can have personal meetings with your employees or through letters. The expert can also advise you on how to utilise the feedback.



- iv) **Make a periodic audit of time-management:** It would really be an eye-opener if you keep a record of how you spend time. Try it for a month or so.

One entrepreneur found that he spent more than 60% of his time in looking after sales and marketing. The reason being that marketing was his strong point and he loved to do that. What happened was the other aspects of his industry were neglected.

Another established entrepreneur frequently has visitors who came to him for advice about their projects. He liked helping the newcomers and being active in his industries association. As a result he could not really interact with his employees and know their grievances etc. or build rapport with them. And they in turn did not give their loyalty and support to him.

Of course, there are no hard and fast rules as to how much time you spend for each activity. You have to plan that as per the needs of your enterprise.

But ensure that your time is spent productively.

- v) **Develop a team of managers:** We have already mentioned that a team of competent, suitable managers should be developed with responsibilities for various functional areas. You should do this very carefully by selecting one manager at a time. And keep a close watch on each new person till you are sure that he/she always has the profit angle in mind.

You should also keep a time-limit for selecting the team. Then delegate the powers and responsibilities and get along with your role.

And make sure to keep a record of how you spend your time.

You also have to make sure that the company's goals as well as their own roles and responsibilities are clear to all managers.

You should run your entire company by managing your four or five senior key managers. Your managers in turn will manage the operations of your business. That gives you enough time to concentrate on planning for expansion, diversification and eventually for growth and success.

You will realise that after a certain stage of the growth of your enterprise and after you have successfully delegated responsibilities and power to your managers, you are not required to look into day to day minor details. However, to be relieved from the routine functioning of your enterprise and yet assured of continuous growth you need to instil in the management team trust and confidence in your leadership. Remember that mere ownership does not entail leadership of the enterprise.



# UNIT

## 7

### Contents

#### Chapter IX

1. How and Why Finance Crisis Occurs
2. Sources of Finance
3. How to Avoid Finance Crisis

**The aim of this chapter is to:**

- caution you against the 'finance crisis' of your enterprise

#### Objectives:

On completion of this chapter you will be able to

- diagnose your business for possible finance crisis
- take action to prevent finance crisis
- select appropriate source(s) of finance for funding growth



A time will come when your enterprise is not only established but is growing. You would need additional funds or money to take care of your expansion/growth needs.

Initially when you set up your enterprise you either invest your money or take loans to augment it. But the requirement now will be for a considerable sum of money. The reserves that you might have or the profits that you might have made, might be there. But would those be adequate for the purpose? Not possible, especially after a sizeable chunk of the profits has gone towards income tax.

So you have to consider various sources for the required funds. Major sources are the following :

- Promoters (that is you) by way of increasing equity or loan
- Public through equity/shares/bonds, debentures or unsecured loans
- Financial institutions by subscription to equity or term-loan under their available schemes
- Commercial banks through term-loan
- Suppliers by way of short term or long term credit
- Financing and leasing companies
- Venture Capital funding agencies

Money can be raised from any of these sources depending on their suitability for you. Then why and how does this finance crisis occur?

## **How and Why Financial Crisis Occurs**

Finance Crisis occurs because of:

1. Failure to choose right source of funding for expansion (too much dependence on borrowed funds)
2. Failure to go public
3. Over-ambitious and unrealistic expansion plans using up surplus funds
4. Psychological problems of losing control - 100% ownership to 80% or less ownership.

Failure to realise the various sources of finance and their advantages and disadvantages lead to finance crisis

## **Sources of Finance**

### **Finance from Promoters**

Funds or the required money can be raised by you yourself or your partners, if you can manage it. This can be done in two ways:

1. through equity
2. through loans



## 1. Equity

The big advantage for you is that the money is easily available without getting into the hassles or procedures for obtaining money from outside sources. Here, the money can be acquired without and cost.

Another advantage is that the increase in amount of your equity would automatically bring down the debt equity ratio. This fact would help you in getting additional funds when you need from your investors like financial institutions or banks.

You might as well know the disadvantages here.

As we mentioned, in a proprietary/partnership firm no permissions from regulatory authorities are required. But in case yours is a private limited or public limited company then such permission is required. This would cause delay and costs will have to be incurred.

It is also true that you as a small scale entrepreneur would not have money adequate for the purpose, so it is desirable that you do not utilise this limited source, your money, for expansion, but keep it for contingencies.

## 2. Loans

Here too the main advantage is that money can be brought in without going through procedures. And as it is given to the enterprise, you, as an individual or your family members, can earn interest on it. And if you avail the loan in the names of a number of family members, tax liability of every member gets reduced.

Now one of the problems here is that the interest paid by you or your family members is not a tax deductible expenditure for your business if yours is a proprietary or partnership firm. But if your company is a private limited or public limited one, it (the interest) is deductible from the gross income of the enterprise. This reduces the tax liability of each individual.

The second problem or disadvantage is that the loan given by you to your enterprise is an unsecured loan. And if your enterprise is in financial trouble, the loan given by you will be returned after all other secured creditors, like financial institutions, banks, or other agencies etc. are paid off.

Look at the following:

Aravind, a small scale entrepreneur, is a classic case of using up his own money for expansion. Why did he do that ? - Fear of losing control over his enterprise. His was a small company manufacturing electrical laminations. Now he wanted to launch production of motor stampings for fans. Because of his fear of losing control, he neither approached the financial institutions nor looked for a financial partner. He invested all the money that he could spare from the unit as well as his savings in the new venture.

In the beginning, he had some problem with the dies for making the stampings. So production





was delayed. The problem was finally solved, but still the stampings did not take off immediately in the market as the quality was not up to the prevailing standards. He needed to consult a technical expert for the required modifications. Money again was needed for this.

He approached his banker for finance but they refused as the performance of the unit was not good. Aravind was in a problem.

Aravind could have gone to the Bank in the beginning itself when he needed money for the new stampings project and kept his own funds for contingencies of this sort.

Learn from this that you should always keep some reserve funds for unforeseen circumstances.

## **Finance from Public**

This is another source for raising money. You can float a public issue (shares) or invite fixed deposits from public. This should be done when you need a large amount.

Here the advantages are that :

- Your company can get funds without substantially increasing its own equity. Do not fear that by inviting money from public you would lose control over the company. It can be avoided by retaining 20% of 30% of the shares with you.
- By becoming, thus, a public limited company, you can get the opportunity of inviting experts on your board of directors. The money acquired through shares would also increase the total equity of the company, which would also make you eligible for borrowing more money. This is because your debt equity ratio also becomes healthier.

Another way, as mentioned, is inviting public to place deposits with your company for certain fixed period - one year or three years. Here you pay interest to the depositors at the market rate. This source is possible when your company has a good credit rating. Though you have to pay interest for the money, it is an expenditure deductible from your profits. One more advantage here is that fixed deposits are unsecured loans, so in times of trouble, the assets of your company will not be attached to recover the money deposited with your company.

But hold on, like every good thing this also has a dark side.

Though everything sound so easy, raising of funds from public is not a simple matter. You require approval from Securities and Exchange Board of India (SEBI) and also the financial institutions if you have taken any loan from them in the past which has not yet been repaid.

If you want to float a public issue and raise required money, you need to be cautious and knowledgeable about all aspects involved before taking the plunge. Look at the example of Sudeep Panchal.



Panchals are an entrepreneurial community of Gujarat specialising in fabrication and manufacture of engineering components and our Sudeep Panchal was no exception. He was an established entrepreneur who had been a very successful manufacturer of precision instruments.

But the trouble started when under advice of share-brokers he floated a public issue and raised about a crore of rupees. Of course he could expand and acquire two more companies. But now the activities also expanded and Sudeep tried to look after all the day to day activities of administration, production and marketing. And this was not possible. And the company began to make losses from the very year of the public issue.

This was very disappointing. Sudeep was a capable, motivated and enthusiastic person. Unfortunately, Sudeep had not experience or knowledge about the business of the two companies he had acquired. Besides, the production processes of these products were complex and needed experience of number of years which he did not have. So he could not really manage the businesses.

Another reason for the losses was that neither Sudeep nor his merchant bankers knew much about acquisition of new companies. They had made certain mistakes because of his ignorance.

At present, the scenario for Sudeep is that both the new companies have gone into liquidation. His original precision instruments unit is doing well, but most of the profits from that company go towards paying the liabilities of the acquired companies

Besides, floating a public issue means that numerous procedures have to be followed and considerable expenditure has to be incurred. Only if your company has reached a stage of growth, i.e., if your project/company is worth Rs. 1-2 crore, then this source would be suitable for you.

Another disadvantage is that by going to the public for money, your company gets listed on the stock exchange. So there is a danger of speculation and even a take over by somebody who acquires majority shares. You might be saddled with him or directors appointed by him on your board of directors. You may even lose your voice in the company.

As regards public deposit, it all depends on the credit-worthiness of your company and rate of interest offered. Here too the Reserve Bank of India has prescribed certain guidelines. And do not forget that in case of deposits, you have to pay regular interest to the depositors.

To put it briefly, we would like to caution you, a small scale entrepreneur, to consider the following:

1. Do not go in for these two sources unless you have crossed both the delegation crisis and developed a team of managers
2. If you want to go public, do not do it in haste. Try other sources of finance first. You might face a problems if the share price of your company goes down. You would not be in a position to raise money then from elsewhere.



3. The responsibilities of your company would also increase. You have to be accountable to your share-holders and government departments

## **Finance from Financial Institutions**

We, in India, have both national and state level financial institutions which provide loans to entrepreneurs. The state level institutions give loans for projects up to say, Rs. 3 crores while the national ones to projects worth more than Rs. 3 crores.

The advantage to raising funds from financial institutions is that the repayment period for the loan is quite long. On top of it there is a moratorium period for repayment in the beginning, which allows you time to establish yourself and then start paying.

Besides, in case of temporary requirement for money, the financial institutions are not very reluctant to help out. And when you apply to them for funds they go through your project minutely and examine all aspects before giving you the money. Once they loan you the money, you can assure yourself that your project is viable.

There are some disadvantages of borrowing from financial institutions. When you take a loan from the financial institutions all the existing as well as future assets of your company have to be mortgaged to them. And once that is done it becomes difficult to raise money from any other source. No one will advance it to you as all your assets are already mortgaged.

The example of Nikhil is a case in point.

Nikhil has been manufacturing blow-moulded plastic carboys etc. for years. His once established market is in danger due to considerable competition from other manufacturers of the same items. He has to make changes in the design of the items to cope with them and regain his lost market. But for this he needs money which he does not have.

How can he raise the required money? All his machinery has been hypothecated/mortgaged to the financial institution from whom he had taken his loan. So it would be almost impossible to get finance by giving it as security.

Now, because of this problem Nikhil has to try and get finance from private sources at a high interest rate.

This source still is the main and acceptable funding source for all entrepreneurs

## **Finance from Commercial Banks**

Normally commercial banks provide money/finance for working capital and not for fixed assets like land, building, machinery etc. But in some cases they do give long-term finance for fixed assets too. The period for repayment, however, is 5 to 6 years and not 8 to 10 years as in the case of the financial institutions.

The advantages and disadvantages here are similar to those of the financial institutions.



The only difference that the repayment period for the loan is shorter than that of the financial institution and the rate of lending interest is higher. The moratorium period is also short.

One specific advantage with banks is that branches of various banks are spread all over the country. This means that it is easier for you to visit them frequently when needed. Their rules are also a little more flexible than those of the financial institutions.

## **Finance from Suppliers and Distributors**

This source is not yet popular in our country. But you can consider it especially when your company is growing. The catch here is that you can avail of it only when your need for money is temporary.

Your suppliers can give you credit for machinery and equipment, raw material and even technical know-how.

Here there are many advantages and almost no formalities. This source can be tapped if the requirement is for buying machinery, raw material and equipment or technical know-how.

Another advantage is that if the machinery supplied by the supplier is defective, the supplier, has to correct the defect or replace it as the payment period is spread over three to four years. Apart from this, since the machinery is purchased under credit to the suppliers, depreciation can also be claimed. Besides, sometimes, the profit margin on some machinery is so high that the supplier may not even charge you interest.

Another source similar to that of suppliers is distributors. If your product has good market and you have an established network, then for your new product, which is introduced by through growth, you can even ask your distributors to deposit a considerable amount of money with you to ensure stocks. They can also be appointed as agents for the product, in which case also they have to make a deposit.

Of course, this amount cannot meet all your needs, but some of your working capital requirements can thus be fulfilled.

## **Finance from Leasing Companies**

In recent years the number of leasing companies has grown by leaps and bound. And these companies are prepared to meet the needs of expansion of small and medium scale enterprises. Lease finance can be availed for installing machinery and equipment, R & D facilities, computers and vehicles.

If your growth requirement is for investment in new machinery, then this is the best source. Because, by investing only 15% to 20% of the cost you can have the required facilities. And the procedure is also simple.

As the lease is generally for three to four years, if the equipment becomes obsolete by that time, you can lease/buy that time, you can lease/buy new machinery with latest technology.



Another advantage is that only the leased machinery or equipment has to be hypothecated to the leasing company. When you need to borrow any money, you can borrow against other assets of the company.

## Finance from Venture Capital Funding Scheme

This source of acquiring funds is very popular in the West. But in India it is just emerging and not yet utilised widely.

The Small Industries Development Bank of India (SIDBI) has introduced a scheme of direct assistance under Venture Capital Fund (VCF) scheme. The scheme is designed to provide VCF assistance to new or existing industries for :

1. encouraging commercial application of indigenously developed technology
2. adopting imported technology to widen domestic applications and
3. all matters connected with or incidental to the above.

Above-mentioned objectives limit the utilisation of the scheme as a funding resource. Besides, the size of investment under this scheme should range between Rs. 5 lakhs and Rs. 250 lakhs. Anyway, if you have a unique, innovative project in mind, you can think of this source too.

### SAQ 9.1

Present your knowledge in two sentences each on factors that could lead to 'finance crisis'.

1.	_____
2.	_____
3.	_____
4.	_____

## How to Avoid Finance Crisis

What preparation should you make in order to avoid getting into the crisis? Here are some pointers:

- Sufficient delegation, good team and monitoring help effective planning to avoid finance crisis
- Consult experts and bankers to choose best source, time and mode of expansion funds
- Do not be afraid to go public
- Remember, 80% ownership of a growing firm is better than 100% ownership of a stagnant or declining one



- Let us reiterate that however competent you are, you would at this stage need someone to assist you in managing your unit. And do not be afraid of losing power. So long as you perform well, the real control will always be with you.

Let us reiterate that however competent you are, you would at this stage need someone to assist you in managing your unit. And do not be afraid of losing power. So long as you perform well, the real control will always be with you.

### **Exercise Caution in Time**

Please remember that when you need more money/funds for your business; do not delay in getting them from the financial institutions. Otherwise the delay would cause 'cash crisis' or worse, your creditors would file a suit against you. And then nobody would help you.

### **How to Obtain Funds**

We have suggested various sources for expansion or growth and their advantages and disadvantages.

However it depends on you to decide which source is the best for you. That would depend on the size of your company, your product, the amount of money required, period of requirement etc.

You may therefore consider the following major factors for selecting your source of additional funds :

- 1) Cost of raising funds
- 2) Cost of retaining funds
- 3) Time taken for raising funds
- 4) Tax implications
- 5) Terms and conditions for getting funds.

We are sure that this will help you in avoiding this crisis or facing it squarely.

### **SAQ 9.2**

How do you propose to prevent finance crisis ?

1. _____
2. _____
3. _____
4. _____



# UNIT

## 7

### Contents

#### Chapter X

1. What is Communication
2. Communication Process
3. When does Miscommunication occur
4. Meta-Verbal Communication
5. Developing Communication Skills
6. Importance of Communication Skills

**The aim of this chapter is to:**

- help you become good communicators - to develop your communications skills.

#### Objectives:

On completion of this chapter you will be able to

- recognise the process of communication
- realise the importance of Meta-verbal communication
- develop your communication skills
- realise importance of effective communication and listening.



## What is Communication?

Communication is the medium through which we transfer out thoughts, needs, feelings, ideas and messages to others.

Till yesterday communication was either verbal, written or through telephone, public speeches, radio etc. But, today there have been and continue to be great advancements in the area of communication. With communications satellites we are in a position to establish not merely audio but also visual contacts anywhere on the earth.

But what about communication among people? One still needs to make progress here. All said and done, whatever may be the medium, the sender (one who communicates) and the receiver (one who receives the message) are human being. What happens when people talk together, when they write to one another, when they read? I sometimes happens that they are unsuccessful in exchanging their thoughts clearly and understandably. How is it that when one person speaks, the other person does not understand him/her properly? Because, both are complex beings with different feelings, values, ideas, attitudes, needs and motives. And each person understands and accepts the communication which he/she makes or receives depending upon his/her capacity to interpret, based on his/her objectives, interests, needs, desired and so on. And that is the reasons why skills are required to communicate - to be direct, precise, honest and understandable.

## The Communication Process

SENDER-> MESSAGE -> CHANNEL -> RECEIVER -> PERCEPTION -> FEEDBACK  
(encoder) (decoder)

This means that when you send a message to other person or persons, it involves a channel. This channel could be spoken or written word, TV, radio, newspaper etc. The receiver (for whom it is intended) receives the message based on his/her preception and gives a feedback (an answer or understanding of the message).

So, as we mentioned earlier, a lot depends on how if is sent and how it is received.

The problem is that we all consider ourselves to be good communicators. We think that we can put across to others what we want to, or intend to. Do we? The image of over selves which is a kind of defence mechanism. requires that we see ourselves as straight-talking, level head, able, honest and above all effective communication. Yet, how often do we fail to see ourselves as others see use!

Look at the following comments:

- "Every time she opens her mouth, she puts her foot into it...."
- "He is alright as long as it is the computer he is talking to!"
- "If you come late to-day, we shall take action against you"





These are just a few examples of the fact that all too often there is difference between what we say and what we really mean and between how we feel we have handled people and how they think they have been handled, - when such gap occurs between our intention and action, it is said that there is a 'breakdown' in communication.

## The Six Stages of Communication

### **Stage 1: Conceiving the message**

At this stage decision is made by the sender to communicate a message. Some messages are made involuntarily, e.g., a scream of fright or pain. Some might be impulsive. Other (messages) may be the careful result of reasoning and pre-thinking or response to external factors.

### **Stage 2: Language of the message**

Before message is sent to the receiver, the sender has to put it (encode) in an appropriate language. The languages of communication include:

- The spoken word
- The written work
- The number
- The picture, drawing and symbol
- The non-verbal communication, expression, gestures, posture.

### **Stage 3: Selecting the communication medium**

Once an appropriate language has been chosen by the sender, he/she needs to select the right medium. Some messages need to be written and transmitted. Alternatively, for quick exchange of opinions, a meeting would be the best medium.

Some major factors influencing the choice of medium are:

- effectiveness
- need for tact
- simultaneous reception of information by receivers
- need for written record
- need for instant feedback
- complexities of message
- time
- cost
- need for speed

### **Stage 4: Decoding the message**

A message has to be understood before it can be absorbed or acted upon. Messages can become ineffective if they are not properly understood by the receiver. Some of the reasons for the failure to understand a message are:



- lack of knowledge of the sender's language
- the sender's vocabulary (words or phrases) is unknown to the receiver
- the sender is a specialist and the receiver is a layman

Education, culture, outlook and attitude also create a block between the sender and the receiver.

### **Stage 5: Interpreting the message**

Apart from understanding the language of the sender, the receiver also needs to be able to interpret it correctly. The underlying or actual message may be rather different from the words actually spoken. For example:

"I liked Mr. Parikh, head of the marketing division, a lot. I am sure now they will be looking for someone with experience of marketing to head the division."

What is the real message here? The remark on Mr. Parikh is sarcastic, and not real.

### **Stage 6: Providing Feedback**

All the above stages are important. But, the need for feedback from the receiver is most essential. Feedback from the receiver is a means of reassuring the sender that:

- the message has been received
- it has been understood
- it has been correctly interpreted
- the receiver is ready for the next one.

So now you know what is communication, and what is the process of communication.

## **When does Miscommunication Occur?**

Miscommunication occurs when:

1. you infer something and make an observation
2. you miss each other with your meanings
3. you think that you know everything about something and what you say is important
4. you suffer emotional disturbance.



Look at the following example of communication mismatch:

Raman Kumar is a supervisor of the claims department of an insurance company. He felt that his department was working inefficiently due to outdated office equipment. He explored and studied sophisticated systems being used by other insurance companies. Raman then concluded that his company's efficiency could be considerably increased if they purchased visual display terminals (VDTs)

He also felt that by installing VDTs, three operators could do the same amount of work done manually by twelve employees. Automation was the key to success in the long run.

Raman also knew that his boss, Mr. Joshi was concerned about costs. But he felt that here the advantages were obvious, and he could get Mr. Joshi's approval for the purchase. He went to see Mr. Joshi personally and the following conversation took place:

Mr. Joshi: Raman, I have looked at your note requesting those VDTs. Unfortunately, I need more information.

Raman: The advantages are clear cut. What more information could you need?

Mr. Joshi: Well, some cost figures are needed to justify this expense to the Director.

Raman: Mr. Joshi, my department is overworked we never get the attention we deserve. Beside, why should you doubt my credibility? It is not fair.

Mr. Joshi: Raman, please calm down. All I am asking for is some cost figures. If you are so certain about the benefit of the VDTs, those figures should not be a problem to produce. I would really appreciate it.

Raman: I am not an accountant, I work hard around here. Why couldn't you take my word for it?

Two days later, Raman received a letter from Mr. Joshi. The request had been turned down.

## SAQ 10.1

1. What went wrong in the conversation between Mr. Joshi and Raman.




2. Was Raman really listening to what Mr. Joshi said? Give your opinion, giving examples.


3. Could Raman have responded differently to Mr. Joshi's request? How?


## Meta-Verbal Communication

But remember, communication is more than words spoken or written. A new medium of conversation was discovered by psychologists in the 19th Century; and that is non-verbal communication - also known as meta-verbal, kinetics, body language or para language.

In fact, it has been observed that words contribute only 7% to total impact of the message, 38% is contributed by the tone of the voice and the balance 55% by facial expressions and gestures.

Before we go any further and discuss this, you must know that meta-verbal language can be learnt and used deliberately and consciously to supplement the meaning of words.

Meta-verbal communication consists of four major components:

**1. Your appearance:**How you appear is the first signal by which others try to understand you. your dress and grooming announces your profession, social and economic status, and attitude to tidiness and neatness.

**2. How you sound while talking:** Tone, pitch and rhythm of the sound supplement or contradict the verbal communication. Tone and pitch also depend on whom you are talking to - your subordinate, friend, colleague or boss. They also depend on the situation, e.g. conversation in a small group, a speech or a presentation in a conference.

**3. How you use body language:** Body language has three major parts - posture (standing or sitting), movement (walking), and gestures. When we speak, the whole body comes into action. Our face (eyes, eyebrows, nose, lips ears and facial muscles) and neck are most important communicative zones for our body. Shoulder, hands and fingers are the next zone. Legs and feet form the third zone. All these parts signal a host of emotions which convey more than words.



We will give you an example:

Ramesh met Suresh, his friend, after a long time in Suresh's office. Suresh received him with 'hello Ramesh, nice to see you'. But there was no smile on his face nor warmth in his tone. Ramesh started talking enthusiastically about his job, his promotion etc. Suresh sat slumped in his chair, kept glancing at the papers on his table, he had a bored expression on his face, though he responded mechanically to all the news.

After a while Ramesh felt that Suresh was not interested in what he was saying and took his leave.

**4. How you handle space:** The space that we maintain between us and others can be divided into four distances - intimate, personal, social and public.

The intimate space is reserved for close relationships like husband and wife, parents and children etc. Personal is with friends, colleagues, social with your boss, public with a gathering. One interesting aspect of space is that it is also used to include or exclude others from the group.

Take for example a group of three or four friends standing close to one another and talking, and a newcomer walks up to the group. If the group wants to share their discussion with the newcomer, it expands and allows him/her to join the group. But if it does not, then it will close in and not allow him to enter the group. This signals, "get lost".

### **Meta-Verbal Ability and Maturity**

What is important for you now is how you can improve your ability and maturity in non-verbal communication.

These are a few learning steps:

1. Become aware that we send messages beyond words while interacting with others
2. Become aware that non-verbal message, like words, have multiple meanings
3. Recognise the non-verbal message that originate from an individual
4. Look for non-verbal clues from others
5. Pay attention to your own non-verbal communication
6. Observe successful speakers and study their body language.

The following case of "Body Language" is interesting and can be useful.

Rajan, an entrepreneur, was very angry. Every time it looked as if he had been able to correct the ways of his production supervisor, Jaswant, would manage to fight with a worker. This time the same thing had happened and the worker had quit. And this affected the production.

Rajan called in Jaswant to talk with him. He really wanted to give him a good solid scolding.



Firing Jaswant, though, would cause trouble with the Union.

When Jaswant came in, Rajan kept on working on his papers for fifteen minutes. Then only he looked up and asked Jaswant to sit down. Then the telephone rang and Rajan talked on it for five minutes. Then he turned to Jaswant, folded his arms, leaned back in chair, and said, "Well tell me about this one".

Jaswant was upset by this kind of attitude of Rajan. He dropped his eyes, lifted his hands in a hopeless gesture and said, "Well, what can you do with some of these guys who think they know everything?"

## SAQ 10.2

1. What messages did Rajan convey to Jaswant?


2. How did Jaswant feel?


## Developing Communication Skills

Guidelines for developing communication skills:

### As a sender

1. When composing a message, carefully decide what sort of action or response you desire from the receiver.
2. Choose a language most suitable for your needs and the situation
3. When encoding (forming) the message, take time to put your ideas logically. Give a thought to the language you intend to use.
4. Select most appropriate medium, that is, whether to send a letter or circular letter, to make a telephone call, give a lecture, use radio or TV facilities
5. Make sure that you choose a language which is understood by the receiver.
6. Be careful to see to it that your message is clear enough to avoid any misinterpretation by the receiver.
7. Make sure to get a feedback from the receiver.

### As a receiver

1. Give full attention to the message being communicated.
2. Check that the medium of communication used by the sender is meeting your needs.
3. Make sure that you understand the message fully.



4. Take care to interpret the message correctly.

### Barriers to Communication

1. **Obstinacy** or unwillingness to discuss any problem or difference in opinion
2. **Prejudice** Fixed or rigid views or ignorance of the topic.
3. **Disinterest** Lack of interest in the topic.
4. **One way communication** Without caring for the other side's opinion.
5. **Anger, emotion, loud noise/tone or action** of abnormal type.
6. **Ego** of personal nature or status consciousness.

For example, let us take this conversation:

**Lalit:** Pradip, the proposal that you have made to the funding agency, FNST is very good. But going through it, I felt that the budget is inadequate.

**Pradip:** Lalit, I have been preparing such proposals for years and I am a master at designing budgets. I know the budget is O.K.

**Lalit:** But Pradip, costs have gone up. Don't you think the figures should be revised, taking the costs into consideration?

**Pradip:** I know what I am doing.

### SAQ 10.3.

This communication has been ineffective. Why? Give reasons.

1. _____
2. _____
3. _____
_____

### Listening

Bear in mind, you can not be a good communicator unless you are a good listener too.

Listening is such a common activity that we often take it for granted. Frankly, we confuse it with hearing and think that listening is easy and natural.

But listening is a complex skill, you have to master it; this skill is necessary for everyone.



What is listening?

Listening is a complex, skilled behaviour that involves:

- Preparation - It is deliberate mental and physical preparation of the whole person
- Absorption - It is absorbing the message with complete ear, and brain involvement
- Processing - It is processing and interpreting received information
- Feeding back - It is feeding back verbal and non-verbal responses to the sender (speaker) to communicate that listening is happening.

There can be many barriers to listening effectively. What are they?

1. The inability to relax and concentrate at the moment at hand

You might be preoccupied with your thoughts and your mind wanders away, you can not listen (effectively). And the other person also can realise this and there is no real communication.

2. Preconceived ideas and thoughts

Sometimes you have your own ideas and thoughts about certain matters, so you do not really listen to the other person or this his/her ideas and they do not have any effect on you.

3. Talking too much, too often

This happens when you talk on and on and even if other person speaks or answers it does not register with you.

4. Thinking of responses during the communication process

5. Lack of interest in the conversation.

You would ask 'How to become a good listener and how to acquire listening skills?' Good question - Here are some points:

- Find are of interest
- Judge content, not delivery
- Hold your fire ( do not be impatient to speak)
- Listen for ideas
- Be flexible





- Resist distractions

- Exercise your mind.

Remember, listening improves attitudes, it builds positive relationships- it is a growth experience.

## **The Importance of Communication Skills**

You know what factors affect effective communication. We reiterate that effective communication is important to all of us, but more so for you as an entrepreneur. You would need to be a good communicator when you start the process of setting up your industry.

To give you an idea, you have to communicate with:

- Officers of financial institutions and banks
- Officers of support agencies when you need land, building, licenses, no objection certificates, etc.
- Later on your workers, suppliers, and customers
- And even other entrepreneurs in similar line of work.

Unless you can convince them, influence them and get your work done, and effectively convey your ideas, plans etc., you will have problems.

When you set up your enterprise the communication between you and your workers has to be cordial, complete and effective in order to ensure best productivity and achievement of your production target. Otherwise, due to lack of good communication, situations might develop into strikes or lock out.

Besides, make sure that the communication in your enterprise is a two way exercise, an upwards/downwards traffic. Regular discussions on any topic of importance affecting the mutual goodwill of the management and the personnel should be tackled by sitting across the table. Lack of knowledge of the system is not good for the health of the business. Both labour and management should be able to communicate their problems to one another and take decisions to avoid break in production.

Let us take a hypothetical situation. You go to a banker with your project report for the purpose of obtaining loan for your project. Here the importance of communication can not be under scored. Of course, the feasibility and viability of your project is very important, so are the projections made by you. But what is more important is how you put across your ideas to the banker to convince him about not only the viability but also your determination, your managerial ability and so on. Unless you are a good communicator, how will you manage it?

And do not forget your customers. You will produce goods, but what is the use of producing them if you cannot sell? You have to have a market - And for getting the market/customers you will have to convince your potential customers about the positive points of your product, or why it should be advisable for them to buy your product. You should be able to influence them. So here also the same argument holds- Be a good communicator to achieve your goal.

So keeping all the above in mind., develop yourself for the purpose.



So, now that we have brought home to you the importance of communication, verbal as well as non-verbal, how to develop communication skills and effective listening, we are sure that you will become a good communicator. And good, successful entrepreneur too.



# UNIT

## 7

### Contents

#### Chapter XI

##### 1. Ten Steps to Successful Negotiation

**The aim of this chapter is to:**

- acquaint you with the strategies and tactics of negotiation

#### **Objectives:**

On completion of this chapter you will be able to

- recognise various steps involved in the process of negotiation
- develop negotiation skills.



## Ten Steps to Successful Negotiation

Negotiation is a form of meeting between two or more parties in order to resolve conflicts to satisfaction of all the parties involved.

Negotiation depends on effective communication. You must while negotiating remember the ten steps listed on the right.:

1. Create the right environment
2. Research your objectives
3. Decide who you are and who your opponent is
4. Open the meeting
5. Talk and listen
6. Make proposals
7. Summarise
8. Close and confirm
9. Evaluate strengths and weaknesses
10. Continue on development

What do we mean by 'create the right environment'?

- Creating the right atmosphere
- Choosing the right time to negotiate
- Selecting the best place.

You must keep in mind that there are four possible outcomes to a negotiation:

I win	-	You lose
I lose	-	You win
I lose	-	You lose
We both win		

And if your aim is the continuous development of your business-goodwill or relationships you must adopt the collaborative style of negotiation and achieve the best deal for both or all parties rather than a competitive style where you want to win at everything.

Remember that if you want to achieve a win/win deal, your opponent needs to arrive at a satisfactory agreement too.

The 'right time' to negotiate is when you have least need for a deal and your opponent's need is greater. However, as a skilled negotiator you should choose your timing carefully and

- Patiently draw reluctant opponents for negotiation
- Avoid spontaneous negotiation
- Prepare your case carefully



## Researching your Objectives

Establishing your own objectives will be relatively easy but assessing your opponent's objectives means carrying out some research and guessing. The process requires the ability of putting yourself in your opponent's position.

For this you should do pre-meeting planning as per the checklist given below:

Opening:

- How should I open the meeting ?
- How interested is the other party/parties in the meeting ?
- What needs might exist ?
- Own
- Theirs
- What are the areas of common ground between us ?

Authority:

- Who am I meeting ?
- What is our relationship ?
- How much authority does he/she or they have ?

Power and Influence:

- What is his/her or their power over me ?
- What is my power ?
- How can I exploit my strength of mutual benefit ?

Commitment:

- How interested is the other party in the meeting ?
- How badly does he/she need an agreement ?
- Will a negotiated agreement stick ?

Competition/Exclusivity:

- How might market forces effect the negotiation ?
- What leverage might be used ?

Innovation & Promotion:

- What concessions am I likely to have to make to ensure success of the deal?
- Who will contribute what help ?

Now try out your plans for negotiating any deal, whether with banker, supplier, customer or any other

Success in negotiation is affected by certain skills and attributes, which are given in the following checklist:



You should

1. Present yourself as a person who likes people
2. Be positive
3. Be persistent
4. Be open minded
5. Develop a good sense of timing and tact
6. Develop high aspirations for deals
7. Present the case assertively
8. Choose the most persuasive words
9. Think clearly under stress
10. Influence the atmosphere of meetings
11. Maintain self-control
12. Take decisions.

Now rate yourself against the above factors on a scale of 1 to 5 and try to improve on those skills and attributes where you have scored low.

### **Personal Communications and Negotiations**

One facet of personal effectiveness ( you have learnt about in Unit 5), when applied in negotiations, is the use of appropriate communication style.

There are two specific styles which used by us all in everyday communication:

1. The extrovert style
2. The inductive style

The first style is about our attempts to persuade the other person(s) to do something by giving lots of information, in effect, to persuade by pushing him/ her or them into a position.

The inductive style is concerned with trying to encourage your opponent to do something by 'pulling' him/her or them towards that position. This approach is more subtle than the extrovert style.

The extrovert style can be most successful in the short term and in a competitive climate. However, if the relationship is dependent on goodwill for its continuing success, there is a likelihood of bruised feelings resulting from the negotiation. So, here it would be better to use the inductive style.

So, there is no perfect style which will work in every situation. Both have their advantages and disadvantages.

### **Opening the Meeting and Talking and Listening**

We have already seen that good preparation is essential for effective negotiation meeting. Now, we come to the actual presentation which plays a major part in achieving good results.



There are people who can achieve their results solely through their personality and interpersonal skills. Most of us, however, need to be good at both.

**The early stages of a meeting are:**

1. Opening the meeting
2. Talking and listening.

Creating the right atmosphere for the meeting is important if subsequent parts of the meeting are to end in agreement. Though issues can be sorted out, important points to consider here are:

1. Establishing rapport
2. Common ground
3. Common agenda
4. Physical comfort.

How we talk in a negotiation meeting can have quite an effect on how the other party perceives us. Our chapter on communications skills has already dealt with how we should communicate by words as well as non-verbal communication like, body language, gestures and facial expressions. All that can be brought into play here.

We have talked at length about 'effective listening' in our chapter on 'communication skills', all the principles given there should be applied here

### **Proposing**

Negotiation meetings are about mutual needs. So, what we should consider here is :

- Timing
- Encouraging proposals
- The best formula
- Defending principles
- Meeting inhibitions.

It is at this vitally important stage that all your preparation will prove its value.

There is a right time for proposals in a negotiation meeting and you must be able to sense when the moment is right.

If you feel that the time is right for proposals to be made but are not sure whether the feeling is mutual, you can always ask. This open atmosphere will help progress to be made.

The best formula is to present your proposals using a conditional approach. This will suggest tentative ways forward.

At a certain stage you may find that your bottom line is under attack or in threat of being compromised. This should not be accepted and you and the other party would have to make it clear that compromises on matters of principles would jeopardise agreements on other issues.

Similarly, keep in view the inhibitions that the other party may have while proposing actions.



## Summarising, Closing and Confirming

There is hardly any point in investing time in negotiation meeting if you cannot close it with satisfactory agreements.

So, what are the skills you need to develop in closing off a negotiation satisfactorily?

The following checklist may provide a useful insight :

- Summarising progress
- Resurrecting earlier issues for agreement
- Using concessions to improve the agreement
- Choosing appropriate persuasion strategies
- Linking issues in agreement
- Listening for concessions
- Using appropriate closing techniques.

Mistakes at the last moment can be very expensive and frustrating. Make sure that you are satisfied with your performance.

It is not possible to do too much summarising in a meeting. It can also happen that even though one party has a clear belief on what has been agreed, the other party has a very different view of the same agreement and this is very dangerous when the agreement is actually implemented. So, accuracy in summaries is very important. Similarly, it is very important to listen to summary given by the other party.

Resurrection here provides a last opportunity to raise any items on which no progress was made earlier.

Linking one item with another is a further method of obtaining movement on difficult issues.

Concessions may provide a way of obtaining additional movement towards the end of the meeting. Skilled negotiators know to keep additional concessions up their sleeves to use in closing a meeting.

Sometimes it may happen that both parties have not achieved what they set out to achieve and then it becomes necessary for the meeting to be nudged towards a closure

The common ways for achieving closure are :

- calling a recess
- imposing a deadline
- threats to pull out
- asking for agreement
- the summary close.

Even when your meeting seems to have closed with a full agreement, there still is a risk that the implementation of the agreement is faulty.

Solution to this include :

- taking and exchanging notes





- getting the agreement in writing
- checking that minutes and opposite party's notes agree with your notes
- taking care of the small points

So these are some of the tips to acquire, develop or improve your negotiation skills and we hope that you benefit by them.

### SAQ 11.1

List major steps involved in the process of negotiation and write a line on the functionability of each of the steps

1.	_____
2.	_____
3.	_____
4.	_____
5.	_____
6.	_____
7.	_____



# UNIT

## 7

### Contents

#### Chapter XII

1. Build a Problem Solving Attitude
2. Recognise the Problem and its Seriousness
3. Specify and Understand the Problem
4. Formulate Possible Causes
5. Test the Possible Causes
6. Develop Alternative Solutions
7. Establish Objectives
8. Compare

#### The aim of this chapter is to:

- help you develop the skill to solve the problems that you may encounter

#### Objectives:

On completion of this chapter you will be able to

- recognise the steps involved in the process of systematically solving problems
- develop the skill to solve problems systematically



All of us experience problems of different nature and magnitude at different stages in our lives. In our daily life we encounter problems so often that we do not even pay heed to them. This is due to the fact that our desire to solve these problems and our experiences of dealing with them has equipped us with spontaneous reactions, which usually result into solutions. However, when we face an unusual or a difficult problem, our reactions fail to yield a solution. In such cases, alternative approaches and modes have to be practised.

As an entrepreneur you are likely to face a variety of problems in the course of implementation and management of your small scale enterprise. If an appropriate system, approach and methodology are developed of solving problems, it will help you to manage your affairs smoothly and you would not undergo stress and tension when you face these problems.

Various qualitative and quantitative approaches have been developed which help us in solving these problems. The basic objective of this chapter is to suggest a non-quantitative approach based on common sense and experiences in dealing with the problems which small scale entrepreneurs may face.

The right strategy would be to understand one's own environment, resources, capabilities, limitations, strengths and weaknesses in order to design an appropriate approach for solving problems. However, the approach suggested here will help you, initially in working on problems and at the later stage, in formulating your own strategy for solving them. The following steps are suggested for developing problem solving attitude and problem solving mechanism.

## **Build a Problem Solving Attitude**

We all possess certain skills, traits and motives. Our psychological makeup indicates the traits and motives we possess. These traits and motives can be identified and developed. Some people are inclined to work on the problems and hence attempt to solve them, while some do not have these traits and motives and therefore they unconsciously try to avoid problems. You will understand this better when you have read the following example:

Mr. Sikand was the owner of a small restaurant. Once he was served with a notice from the Department of Food and Drugs Administration for not having complied with necessary provision as per the Food and Drugs Act. When he received the first notice; he read it and filed it without taking any action. After a few days he received another notice. This time unconsciously he decided not to open the envelope and did not read the contents of the letter. Subsequently, even though he kept receiving notices frequently he did not even read them. After approximately a year, a team from the Food and Drugs Department came to the restaurant and locked it up. The department suspended the licence of Mr. Sikand for not responding to the notice and failing to take any corrective actions. Mr. Sikand's psychological composition directed his actions towards avoiding problems and taking steps to solve them.

You must have experienced this attitude in some of the government departments where people try to avoid taking decisions and solving problems.



We would like you to go back to your past and identify some situation where perhaps your behaviour was comparable to what is stated above. If you can identify many such incidents it is time for you to take note that you are in the process of developing a personality which is prone to avoiding problems. But there is no need be despondent. There is a way to change your attitude. What you need to do is to be 'aware of this facet' of your personality and make conscious efforts to seek solutions rather than succumb to your tendency to avoid problems.

## **Recognise the Problem and its Seriousness**

It is not only important for entrepreneur but also for each one of us to recognise a problem when it occurs. If you have a clear understanding of what is a normal situation, you will be able to identify the deviations and hence the problem. For example if you know that the standard production level of your unit should be one tonne per day if it reduces to 3/4 of a tonne, you would immediately realise that there is a deviation and therefore, there must be a problem.

Since some problems are of qualitative nature it may not always be possible to find out the deviation in terms of number. For example, you may experience that industrial relations in your plant are not harmonious, but you may not be able to quantify this problem. Therefore, it is very important for an entrepreneur to continuously observe all the situations he/she encounters.

Once you have recognised the problem, your next step is to examine the seriousness, growth trend and urgency of the problem. The seriousness of the problem will help you decide whether you need to work on the problem for a probable solution right away or can defer it for sometime. It will also help you to decide whether some temporary solution is feasible, till you have had a total understanding of the problem and have worked out a course of corrective action. Let us try to understand the whole process clearly with the help of following example:

Zenith Dyes, a small unit manufacturing pigments started experiencing approximately 30% rate of absenteeism in its factory after 2 years of its operation.

The owner immediately realised that the problem was serious and needed immediate action. In order to meet the customers' demands he first made arrangements for additional workers while he examined the cause and found solutions for the problem of absenteeism. His understanding of the seriousness of the problem helped him to take interim corrective action which resulted in prevention of another problem viz., loss of potential customers. If Zenith Dyes had not made arrangements for temporary staff in order to sustain the production level, they would probably have faced problem in marketing. Sales might have dropped and they would have lost a few customers.

The growth trend of this deviation is also important. If the intensity of the problem is on the increase then one would not only have to worry about the interim solution but would also to work towards a permanent solution immediately. The same is true in case the problem requires immediate the urgent action.



## Specify and Understand the Problem

If one can clearly identify the deviation or specify a problem, he is well on his way to solving the problem. The important thing to note is how to specify a problem. Many of you must have consulted physicians for a physical problem. I would like you to think about one of your meetings with a physician and the discussion you had with him about your illness.

When you go to a physician he will usually ask you questions about your physical discomfort the area of discomfort, the period when you face discomfort and the extent of such discomfort. The physician is in fact trying to understand your problem.

The same way an entrepreneur, when faced with a problem must ask questions not only to himself but to others too concerning what is happening and why it is happening.

When Zenith Dyes experienced 30% absenteeism, the entrepreneur called the heads of each department and the persons concerned and asked them why there was so much absenteeism. On probing he got a lot of information and found that there was no strike, no agitation or go slow all over the company and that the absenteeism had occurred only in the production department, generally on Friday. Thus he found out that the rate of absenteeism was more on Friday and was almost normal on other working days.

## Formulate Possible Causes

Let us go back to the physician's examination process. The physician may not have an idea whether the fever is 'influenza', 'malaria', 'typhoid' or 'hay fever' if you complain of high temperature with associated affliction. If he wanted to identify the type of fever, he would have started working on formulating the causes of the fever such as cold, virus, allergy etc. In the same way when you face a problem you must try to formulate the possible relevant causes.

In the case of Zenith Dyes the probable causes for a high rate of absenteeism were :

- a) There was a higher proportion of Muslim workers in the factory. Friday is day for 'namaz' for the Muslims.
- b) It was the company's policy to make payment to the workers on Thursday. If the wages are paid on Thursday, it is likely that the workers would remain absent on Friday as they are flush with money.
- c) There is a change in the film shown in the local movie houses every Friday. If the proportion of young workers is high, it is possible that some of them may like to watch the film in the first show and therefore choose to remain absent.
- d) Perhaps the supervisor in-charge the shift on Friday was tough and not much liked by the workers.
- e) There is a higher work load in the factory usually on a Friday since Saturday being a holiday all shipments for customers were sent on Friday evening.



It is not important to pinpoint a number of causes but to be able to find out the relevance of the causes. The objective here is to get more insight into the possible reasons for occurrence of a problem. Once you have identified and examined the possible causes, you have completed the analysis of the problem. After identifying the causes, you must test these causes - not as we test any substance in the laboratory - but through analysis, reasoning, data and intuition.

## Test the Possible Causes

The process of testing formulated causes calls for intuition, creativity, analytical skill and reasoning. An individual with these qualities will be able to test the causes without using a laboratory type approach.

The causes of absenteeism as indicated earlier in the case of Zenith Dyes can be tested with the methods listed on the right:

- The hypothesis of 'higher rate of Muslim employees' could be tested by going through the list of the employees.

After verifying the profile of the employees working in the production department the owner found that even though there were many Muslim in this department, they were not absent of every Friday.

Therefore, there was not reason for him to worry about this or take a corrective action in this area.

- Regarding the wages, he found that the factory had fortnight wage payment system and therefore this also could not be the possible cause of the problem.
- Although there were changes in the movies shown in the local cinema halls every Friday, it was found through personal inquiry that the workforce was not movie-oriented.
- The profile of the supervisor was studied in detail and the owner learnt that the supervisor though very competent was tough when it came to handling people. He was particularly tougher on Fridays as he had the responsibility of despatching goods every Friday to the customers, Friday being the last working day of the week.

After getting detailed information on the supervisor's way of handling people, the owner determined that this was the only cause which had led to occurrence of the problem of absenteeism.

## Develop Alternative Solutions

Once you have determined the cause, the next step would be to look for a solution. Since every individual possesses different levels of information, knowledge, skills traits and motives, it is likely that everyone would come up with different solutions for a problem. Each solution will have some degree of merit. Therefore, there can be no right or wrong solution to any problem. The solution which fits into your objectives, your resources, your strengths, limitations,



constraints etc. is the best solution under the circumstances. Therefore, once you determine the cause or causes for a problem that you face it will be worthwhile to develop various solutions and then relate them to your objectives

## Establish Objectives

Once alternative solutions are developed, it will be necessary to establish your objectives. Clarity regarding objectives will help you to classify them in relation to the problem into two categories listed below:

1. Result to be produced
2. Resources to be used.

In case of Zenith Dyes the entrepreneur clearly indicated the following objectives:

### **Result to be Produced**

1. The rate of absenteeism had to be brought down to 8% which is normal in any chemical industry.
2. The work load cannot be reduced as the needs of the customers had to be catered to and shipments had to be made on Friday.
3. The supervisor cannot be dismissed because he is one of the best employees.

### **Resources to be Used**

1. More than Rs. 100 per week can not be spent to solve this problem.
2. More than four extra persons can not be assigned to the tasks to complete it.
3. Incentive payment system can not be made use of.
4. Overtime to the workers can not be provided.

Once you have established the objective you must classify them into three different categories such as 'MUST', 'DESIRABLE' and 'CAN BE IGNORED'.

Such a classification of objectives about the results to be produced and resources to be used would help in selecting an appropriate solution from the cluster of solutions thought of.

## Compare Solutions

When there is more than one solution, it may become a problem to select the best solution and therefore we get caught with another problem. In such a situation, the right way will be to compare various solutions in terms of results produced and resources used etc. However, this does not mean that one will have to experiment with each solution and thereafter decide the best course of action. The best way would be to use your reasoning, judgement, intuition, to decide the advantages and adverse consequences of each solution.



The analysis of effect of each possible solution should be quantitative wherever possible. Certain non-quantitative effects such as the impact on worker's morale, human relations etc. should also be thought of. Once all the solutions have been compared you will be able to choose the best solution to the problem.

But remember, you may not be able to solve a problem completely. You can quite often only reduce the magnitude of the problem and perhaps create another problem but of a smaller magnitude.

In the case of Zenith Dyes, the entrepreneur implemented the solution of employing 3 to 4 additional workers on Friday, but there was another problem of generating resources for paying extra wages to this additional man power.

### SAQ 12.1

List the major steps in the process of problem-solving and write one sentence on the functionality of each step in the process.

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_
4. \_\_\_\_\_
5. \_\_\_\_\_
6. \_\_\_\_\_
7. \_\_\_\_\_
8. \_\_\_\_\_
9. \_\_\_\_\_
10. \_\_\_\_\_





## ASSIGNMENT VII

1. How is small business management different from the management taught in business schools?

2. How is planning helpful in achieving success?

Enrollment No : \_\_\_\_\_

