



MANAGEMENT OF FISHERFOLK MICROENTERPRISES

A manual for training of trainers



**MANAGEMENT OF
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The Bay of Bengal Programme for Small-scale Fisheries Development (BOBP) has, in its work with small-scale fishing communities, seen a need for alternative employment opportunities in coastal areas where fish resources are heavily exploited. The creation of small village businesses is one strategy for individual upliftment as well as strengthening village-level economic development. Experience has shown that many very small businesses or microenterprises fail due to lack of managerial skills. The idea of imparting basic business skills through experienced field workers of Non-Governmental Organizations (NGOs) was thought of as a means to provide already existing as well as future microenterprises with on-the-spot managerial advice. This practical manual on small business development is the outcome of this belief.

The manual will be of help to NGOs already involved with fisherfolk as well as those interested in such work, in the training of village-level field workers. Translation, adaptation and reproduction of this document is encouraged.

The Bay of Bengal Programme (BOBP) is a multiagency regional fisheries programme which covers seven countries around the Bay of Bengal: Bangladesh, India, Indonesia, Malaysia, Maldives, Sri Lanka and Thailand. The Programme plays a catalytic and consultative role: it develops, demonstrates and promotes new technologies, methodologies and ideas to help improve the conditions of small-scale fisherfolk communities in member countries. The BOBP is sponsored by the governments of Denmark, Sweden and the United Kingdom, and also by UNDP (United Nations Development Programme). The main executing agency is the FAO (Food and Agriculture Organization of the United Nations).

This document is a training manual and has not been cleared by the Governments concerned or the FAO.

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INTRODUCTION

What is the need for fisherfolk to generate additional incomes from nonfishing activities? Why not concentrate on increasing production of fish?

Fish are a natural resource and, like other natural resources, are prone to over-exploitation. Increased production would mean depletion of this resource as is already being felt in many countries.

REMEMBER:

- YOU CAN CATCH FISH ONLY ONCE.
- IF YOU CATCH THEM ALL TODAY, YOU CAN'T CATCH ANY TOMORROW.
- IF YOU CATCH THEM SMALL, YOU CAN'T CATCH THEM BIG.

It must also be remembered that income from fishing is seasonal. Then how does a fisher-family survive? The answer to this may lie in **generating income** from nonfishing activities.

What do we mean by 'income' from 'nonfishing activities'?

The most common such activity is to work as a labourer in a nearby agricultural village, factory or city. But employment opportunities are not always available.

The second possibility is for the fisherman to use his spare time for some income-generating activity of his own, *e.g.*: *A fisherman growing vegetables*. By growing vegetables

- he could use them for personal consumption, which means the family would not have to buy vegetables, thus saving money;
- alternatively, the vegetables could be sold and with the money (income) earned he could buy other necessities: and
- of course, he could always do a little of both.

Let us take a look at what income means. By 'income' we mean 'money' or 'goods' that are received by a person for doing work, producing something, or giving someone something they want.

By 'non-fishing activities', we mean any other work possible in the locality, or in easily accessible nearby localities, but which

does not have anything to do with fishing. Some such activities could include:

- Handicrafts manufacturing.
- Food processing.
- Fruit, vegetable or fish farming.
- Animal husbandry.
- Trading.
- Repair services.

What is an ‘enterprise’?

An ‘enterprise’ or ‘business’ may be defined as an organization which employs resources like money, materials and skills to provide goods and services to others and whose goals are to produce a profit for its owner so that, essentially, he can survive and grow.

The enterprise, to start with, would depend on what the individual is capable of and what the needs are in the area he plans to start the business in. The ‘size’ of the enterprise envisioned here would be very **small**, involving a minimum investment and which the owner himself would be comfortable managing. This is what we call a **microenterprise**.

What do we mean by ‘micro’ and why should we have a microenterprise?

By **microenterprise** we mean a business which is very small and within the financial means and capabilities of fisherfolk who may not have business experience. The ‘manager’ of such an enterprise will be the main person, if not the only person, carrying out all the work. Though a microenterprise is small to begin with, it can grow, depending on the success the owner/manager makes of it.

What should the microenterprise do for the owner, and how?

The enterprise should be such that it helps the owner to increase his earnings.

Earnings can be increased by

- utilizing all resources in the owner’s household in terms of skills, money etc., and
- minimizing the risks in the business, *i.e.* by being in a viable business and managing it effectively.

However, experience has shown that microenterprises often fall far short of their potential, essentially due to lack of managerial skills in the entrepreneurs and lack of access to people with these skills.

A microenterprise seems so small and familiar to the one or two people running it. What is the necessity for management inputs?

A business, however small, would benefit from management inputs, which take a fresh look at how healthy the enterprise is and how to make it stronger.

Management should be seen as a tool which will enable the owner to comprehend the entire business and ensure that the business is successful and makes money.

There are many situations where attention not paid to certain aspects has meant bankruptcy or non-profitability, *e.g. the woman who wanted to rear ducks, but invested all her money in buying ducklings, leaving no money to buy their feed*. Anyone, in hindsight, would tell her she had to plan for a place to keep the birds, estimate the time it would take for them to grow to a size where she could either sell their eggs or the birds themselves, and how much feed she would have to invest in before the ducks would bring in money. In short, she would have to consider the entire business cycle. But must this be in hindsight? Of course, not! Such concepts could be conveyed to fisherfolk interested in starting any business by nongovernmental organizations (NGOs) who are in regular touch with them.

A successful small business can play a valuable role in increasing the standard of living of the fisherman involved. But the business will, most likely, be new to the individual. He would have had no natural opportunity to learn from his parents or by apprenticeship — a normal way of learning. This makes microentrepreneurs very vulnerable in their ventures. NGOs could play a vital role in helping them make a success of their business.

What kind of help can an NGO provide?

The NGO could play an important role in all aspects of business development amongst fisherfolk — right from encouraging the business spirit, to helping them identify businesses, set them up and run them.

How can an NGO provide this kind of help?

The best way would be through a team of dedicated field workers who would act as advisers to the fisherfolk.

These field workers would, in turn, be given inputs from time to time to strengthen their confidence in the role they play in helping microenterprises. Of course, no amount of training can substitute for actual experience — and that they will, eventually, gain on the job.

What kind of training can be given to these fieldworkers?

Fieldworkers can be trained to:

- Understand the various aspects involved in starting and running a business.
- Understand their role in helping microenterprises and how best they can do it.
- Learn from their own experience, as no amount of training can substitute for experience.

This manual is the first step in the development of training inputs for the consultant. With use over a period of time, the manual should evolve and become fine-tuned to the needs of the consultant.

Will the manual help the fieldworker become an ‘expert’?

The answer is ‘No’. Though certain basic features are common to all businesses, each business and its particular situation varies. This manual attempts to

- highlight the various concepts involved in managing a business;
- apply the concepts in different situations; and
- help the consultant to transfer the concepts into the actual business situation

As the consultant is unlikely to be an expert in the ‘techniques’ of the particular business, he should be able to obtain expertise whenever required. Over a period of time, the consultant will be able to build up a wealth of experience.

How is the manual organized?

The material has been organized in three sections:

- Section I — Starting a Business.
- Section II — Running a Business.
- Section III — The Fieldworker Consultant

The sections include:

- Reading material which could be shared with the trainees.
- Activities for the participants.
- Instructions for the trainer.

This is in as simple a language as possible and conveys the basic concept. Each chapter outlines at the beginning what is to be covered in it and highlights at the end the main points discussed.

Illustrations have been given wherever possible.

It would be necessary for the trainers and the field workers to make the material more location-specific.

In using the material, the trainer would have to build around it, using his own experiences.

Increasing participation will lead to clearer business ideas and better learning. The trainer can encourage participation by

- obtaining ideas from participants; and
- helping participants to reflect on their field locality and identify situations where the ideas would be applicable.

Activities

Each activity is to be explained to the group.

Everyone is to be encouraged to participate.

Each activity has outlined for the trainer

- its objective,
- the materials required, and
- the role of the trainer in guiding it.

Note: The trainer may alter the actual activity, as long as the objective is achieved.

Instructions for Trainers

Notes for the trainer are included in the material and have been put alongside the text. These essentially relate to

- the use of the reading material, and
- the points to be 'highlighted'.

How many consultants should be trained in one session?

Though the manual has not been used as yet, we would recommend 10-12 persons in one session.

Flow long will the entire training programme take?

Again, this manual has not been used for any training as yet. However, we feel a minimum of 8-10 days would be required to convey the basic concepts. Long-term training, with field visits and practical activities, might take upto 4 weeks, and would give the field worker more confidence than a shorter course.

The manual is to be used as a reference point to which material may be added or subtracted. The trainer may choose to cover some aspects in greater depth and some to a lesser extent. The trainer may also choose to cover any specific section or specific aspect of a section in depth.

Where should the training be done?

The training could be done in the conference room of the NGO. However, if this would mean interruption of the sessions, it would be better in a place away from the office. Field locations can offer more peace, lower costs and the opportunity of field visits.

Who would do the training?

Obviously a 'Trainer' who is familiar with business concepts and who has some experience in working with microenterprises. It would be preferable if he has at least been exposed to fisherfolk and fisheries before undertaking the task.

However, the participants should be exposed to senior members of the NGO they belong to, who should convey to them

- the importance of their task, and
- their willingness to reply to queries from the participants, especially those seeking help/assistance.

It may be a good idea to have a few sessions with:

- Experts in fields where fisherfolk microenterprises could be successful.
- Government programmes and funding NGOs, to outline the help they can give.
- Banks, cooperatives, etc., to outline what role they could play.

Is the training to be a 'one-time effort'?

No training programme can be successful if it is just a one-time effort.

The objective of the training is to give inputs to the field workers to help them to be effective.

What we envisage is a 'Training System' for consultants which could be described as follows:

NOTES

I

1. First Training Session

A. Give basic inputs.

B. Prepare a plan of action.

2. Field Experience

A. Record experience.

B. Note down problems faced.

C. Whether solved — Yes / No.

D. If 'yes', how they were solved.

3. Second Training Session

A. Brings his < > Group learns from each other experience and shares it.

B. Group identifies the problem

areas and the inputs they would like in terms of:

- Managerial concepts.
- Technical expertise.
- Contacts with funding NGOs/government programmes/financial institutions.

4. More Field Experience

5. Third Training Session

A. Additional training inputs identified in second session

B. Activity plan drawn up by consultants;

- Their role.
- The help they'll need from organizations/and experts.

This process is obviously endless. But, essentially, a minimum of three sessions will be required to

- Get any practical results from the training; and
- Reinforce the seriousness of the effort.

Incidentally, this will also help in firming up the training modules by determining:

- Which concepts are required at which stage of a field worker's efforts.
- In what depth each concept is to be covered for field workers with different levels of experience.
- Additional concepts/areas to be covered in the manual.

SECTION I: Starting a business

1. Identification of small business ideas
2. Preliminary feasibility of business ideas
3. Financial feasibility
4. Appropriate ownership form
5. Implementing a business idea

STARTING A BUSINESS

What do we mean by ‘starting a business’?

Before starting a business, you must consider what running a business entails in comparison to doing wage labour. Whereas you can hope to improve your situation by starting a business, you can end up doing the opposite. **There are no guarantees.** What are the characteristics needed of a person wishing to start a business?

- Willingness to take risks.
- Willingness to work long hours without immediate reward.
- Willingness to learn new skills.
- A friendly disposition.
- Self-discipline.
- Well-organized.

If you decide to start a business, you must first identify the business to be in. You should ensure that the business has got a **chance** of being successful, *i.e.* making profits. Thereafter, you can begin the process of starting the business. This involves a considerable amount of planning, setting up and then actually starting the business, *e.g.* *the woman who plans to rear ducks would have to plan to buy the ducklings, find a place to keep them and ensure food to feed them. She will have to plan for money for all three activities if she does not have the facilities freely available to her. She will start setting up once she knows where she can sell the ducks/eggs and how long it will take to get to that stage.*

What is covered in this section?

This section covers identification of a business as well as actually setting it up for the first time and starting it up.

The ‘identification of an enterprise’ starts with the definition of business, goes on to talk of the different types of businesses and then gets down to the actual identification. This has been handled in five stages:

- i) Drawing up an exhaustive list of possible ideas for a business.
- ii) Assessing technical feasibility: Is the project possible?
- iii) Assessing market feasibility: Is there a market for the product?

iv) Matching resources available with resources required and making a preliminary short list of feasible ideas.

v) Making a detailed financial study to see if the ideas short-listed are financially viable. That is:

— Is the money required to start the business available?

— Will the cash that comes in. in the business, be sufficient to repay loans and replace permanent fixtures bought for the project?

— Will the business make more money for the owner than he spends on it?

The chapter on 'Starting Up' discusses the appropriate forms of ownership and the various activities involved in commencing a business, the nature of such activities, their order — whether sequential/parallel — and the scheduling of activities so that operations can begin at a specified time.

Let us now look at each of these separately.

Identification of small business ideas for fisherfolk

What are we going to look at in this chapter?

- What we mean by a 'small business', the different kinds of businesses and the areas of business which might be appropriate for fishing communities.
- What is a good business idea.
- How to systematically look at all possible good business ideas.

What is a 'small business'?

Let us look at what we mean by small business and what the different kinds of small businesses are.

A business is an organization which should create profit for the owner, offer some employment opportunities and, essentially, enable him to survive and grow.

Some examples of small businesses are:



Vegetable selling



Tea shop

Discussion on the features of each type of business and on the advantages and risks of each would be useful



Raising poultry

Growing vegetables



Engine repairing



Net making

We see that in all these businesses, one person is the main and, most probably, the only person carrying on the business. Each of these businesses is easy to understand and control because it is small.

Are there different kinds of businesses?

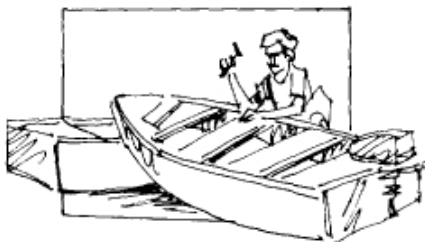
Yes. They could be broadly classified into three different types.

Initiate discussion on the three basic types of businesses viz production, service and trading

This can be done by asking for numerous examples of businesses and then helping the group to classify them in the three categories.



This is a production business. She produces the goods and then sells them.



This is a service business. He is selling his 'services', his skills, to customers.



This is a **trading business**. He buys from a source and re-sells at a different place.

*What are the special features of a **production business**?*

1. A production business is involved in making a product by using raw materials, labour and other resources and then selling the product.
2. Production requires money to be put into raw materials and equipment for a longer period of time *i.e.* till the products are sold.
3. Small businesses normally produce goods using raw materials, labour and skills available locally.
4. The goods may be sold by the business to an intermediary or directly to the final buyer.

*What are the special features of a **service business**?*

A service business is dependent on a constant need in the location for the particular service offered.

2. The service normally involves a skill not generally possessed by others or is a task which people are willing to pay for to avoid having to do it themselves.

e.g.

A cycle repair 'hop' — needed where cycles are used extensively.

An engine repair shop — needed where boats, irrigation pumps and other motors are used.

A hairdresser's chop — needed where women can afford to get their hair dressed professionally (as in Thailand).

3. The service business may require purchase of tools/equipment to start up. But, normally, this is the cheapest type of business to start.

*What are the special features of a **trading business**?*

In a trading business, you buy from one source and sell to another. It is **the easiest to start**, as no time is spent in producing the goods to be sold.

2. You normally expand the business if it is successful.
3. You can pull out of the business more easily, as there is little equipment in it. It can even be a one-time operation. If you find it is not profitable to buy and sell an item, you can stop doing so. You can close down easily.
4. The trading business often uses less of local resources (raw material / manpower). You normally invest in products from outside the village and earn by reselling them at prices more than you paid for them.
5. You have to invest more in the business as you need to buy certain minimum quantities of a number of articles.
6. There should be a secure place to stock the products for sale.
7. The risk in the business is that damage to the stock could result in the goods not being saleable and you could, thus, lose the money you invested on them.

Again initiate a discussion on the areas in which they think fisherfolk businesses could be and why they think so

What are the different areas in which fisherfolk businesses could be?

Fisherfolk businesses need **not** be only related to fishing. They could be in any area. Such as:

Making dry fish, Ma/dive fish and salted fish. Fish vending. Selling fishery-related goods.

Repairing craft, engines, nets and fishing gear.

Coconut fibre- and vain-based activities.

Metal and mechanical repair workshop, bicycle repair shop.

Carpentry. furniture-making toy—making.

Garment— and lace-manufacture. embroidery

Making artefacts for tourists.

Cement blocks, roof tiles, toilet manufacture.

Handicraft carving wood or stone.

Resale of food sweets, tobacco, pan, plastic items.

Making and selling of sweets, pickles, chutneys, snack foods, curd bread.

Growing at traits, vegetables, spices and flowers

Raising cattle, goats, poultry, pigs, ducks, fish, shrimp.

Milling or husking rice and other grains, spices etc.

Small-time trading in fish, chillies, rice, etc.

Childcare.

In each area encourage all participants to think back to the environment they work in and bring out different kinds of farming, poultry/livestock rearing, trading, culture and capture fishing activities, service business. These could be on going or planned for the future.

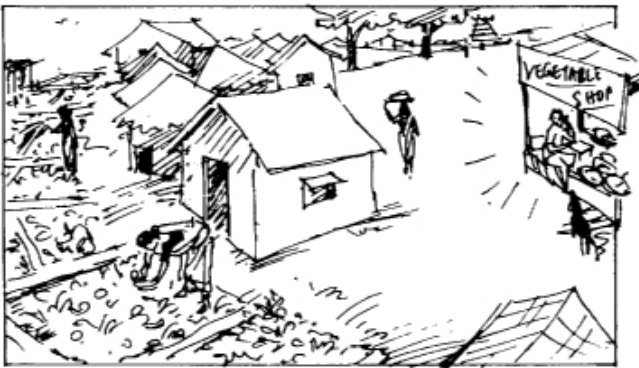
What is necessary for any business to be a success?

NOTES

For any business to be successful, there has to be a market for the product or service.



If no one has cycles, the cycle repair shop would not be needed.



If there are many vegetable gardens in the village, it might not need a vegetable shop.

What is important in identifying a business?



It is important to identify the 'best idea' for the business to be most successful.

This is a village on the coast.

Many fishermen have taken loans and acquired boats with outboard motors. This has helped them in their fishing. Many more fishermen are planning to buy boats with outboard motors,

Rajulu's motor has broken down and needs to be repaired, but there is no one to repair it. He has to take it 100 km for repair.

Venkatesan is a fisherman in the village. He is interested in mechanical things. Do you think it is a 'good idea' for him to consider setting up an 'engine repair shop'?

Venkatesan may not already be a good engine repair mechanic, but he could be trained to be one.

Yes, it might be a 'good idea'. There is an increasing problem faced by hshermu owning motorized boats and this is opportunity for business. Venkatesan is interested in mechanical things and could be successful running an engine repair shop. Hence it is a 'good idea' for him to consider.

ACTIVITIES

A

Let us divide into three *groups* (of 3 members each). Group 1 should list three good ideas for small 'Trading' businesses and the reasons why they consider them 'good ideas'. Similarly Group 2 should list three small 'Production' businesses and Group 3 small 'Service' businesses. Each group should then present its ideas.

B

The activity is to be repeated. Each group should handle a different type of business and list three good ideas other than the ones already mentioned. Each group should again present their ideas,

Objective to be achieved

To familiarize participants with the three basic types of businesses.

To introduce them to the reasons for the likely need for a specific business (this will be covered in detail in a later chapter).

Material required

- * Three charts
- * Marker pens

Discussion

1. The instructor should put up three charts. 'Production', 'Trading', and 'Service', and note the ideas generated by the participants on each.
2. The number of members in each group will depend on the number of participants.
3. Each group must present its ideas and explain the circumstances under which the business idea is likely to be successful.
4. The trainer should lead a discussion on why they consider a particular option a good business idea. The discussion should focus on:
 - The needs of the community.
 - Problems faced by the community.
 - Resources available with the entrepreneur, such as
 - manpower,
 - technical expertise/skills,
 - land, and
 - money

On what basis would you draw up a list of possible business ideas?

A list can be made by looking at each of these aspects:

Problems facing the people/community.

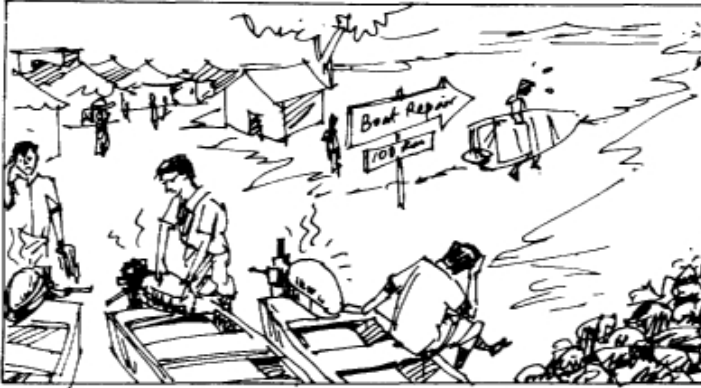
Needs of the people, today/in the future.

Raw materials available locally/skills of individuals.

Let us look at each of these in a little more detail

Problems facing the people/community

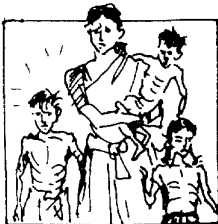
Solutions to problems give rise to opportunities.



Many fishermen have motorized boats but to repair their engines they have to go to a town far away. **Opportunity:** An engine repair shop.

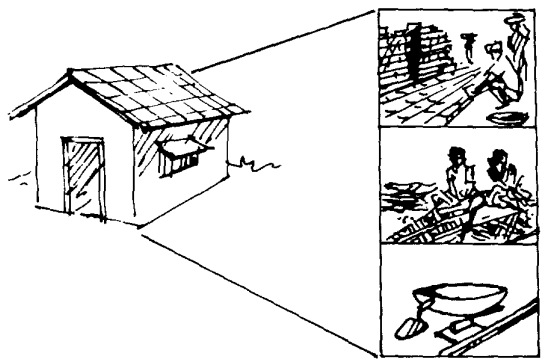
How do you identify the needs of the people?

Their needs today and in the near future



- * People need to supplement their food/nutritional requirements and nothing other than fish is available locally. They have to go long distances to fetch anything else.

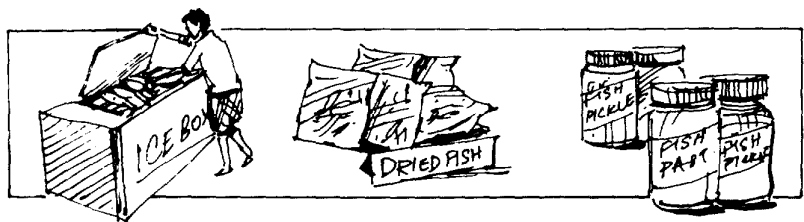
Opportunity: Vegetable vending/producing. 'Rearing poultry/selling chicken and eggs'.



- * People hope to have some sort of shelter.

Opportunity: Manufacture of handmade bricks. Supply thatch for roofs. Work as masons.

Raw materials available local/v/skills of individuals



- * Fish

Opportunity: Fish vending — selling fish in bigger market. Processing fish — smoked/pickled/dried/sauce/powder/oil. Making animal/shrimp feeds and fertilizers. Collecting air bladders, shark liver oil, shark teeth/jaws, cuttlefish bones etc.



- * Coconuts

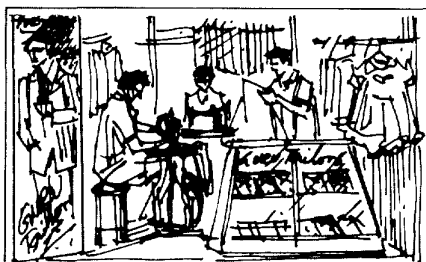
Opportunity: Making ropes, leaf mats; shell handicrafts, sweets, coir decorations etc. Selling tender coconut water. Using the timber to make furniture etc.

COOKING



Snack shop

SEWING



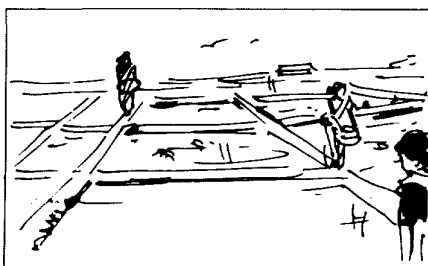
Making clothes

AGRICULTURE



Growing vegetables

AQUACULTURE



Rearing fish/shrimp

ACTIVITIES

Analysis of environment

Let each of the three groups earlier formed identify ideas for microenterprises (other than the ones given in the examples) by considering one of these aspects:

Group 1	Problems facing the people
Group 2	Needs of the people (today/future)
Group 3	Raw materials/skills available

Their responses should be based on their experiences in their villages and their knowledge of their folk.

Each group should present at least five new ideas for microenterprises and give reasons as to why it considers each an opportunity. It should also identify each suggestion as a Trading, Production or Service enterprise.

Objective to be achieved

Participants are expected to learn to identify business ideas systematically, using different ways of brainstorming. Participants also create in this manner a location-specific ideas list.

Materials required

- * Three charts
- * Marker pens.

Trainer to put up the charts marked:

- 1) Problems facing the people
- 2) Needs of the people (today/future)
- 3) Raw materials/skills available

Discussion

Each group must present its Ideas, explain the classification of each and why it considers them feasible.

THINGS TO REMEMBER

- A business makes money for the owner by providing goods or services to those willing to pay.
- A small business is simple and is relatively easy to understand, handle and control. Most often there is only one person required to carry on the business.
- There are three basic types of businesses:
 - Production: the person makes and sells (*e.g. basket-making, vegetable-growing*)
 - Services: the person sells services (*e.g. repairs*)
 - **Trading:** the person buys from one source and sells to others (*e.g. selling household items and foodstuffs*).
- How do you identify a business?
 - * **For** a business to be successful there should be a need for it (a market).
 - * **The need could be a current one** or one which is likely to be felt in the near future.
- How do you draw up an exhaustive list of possible business ideas? To draw up an exhaustive list of ideas for business, you should consider:
 - * Problems facing the community.
 - * Needs of the people today/in the future.
 - * **Raw materials/skills of individuals available.**

Preliminary feasibility of business ideas 2

Having made an exhaustive list of possible business ideas, the task now remains to eliminate the ones which are not possible to implement. Elimination becomes necessary because

The idea is not technically feasible or 'possible'

- **The technical feasibility**

There is no demand for the idea; that is, there is no 'market'

- **The market feasibility**

The individuals behind the idea are not likely to have the required resources

- **Matching of resources**

What are we going to look at in this chapter?

- What 'technical feasibility' is, why it is important, and how we should assess it.
- What 'market feasibility' is, how an individual can check the demand for a product/idea and the factors that affect the demand.
- What resources are required for a project and whether they are sufficient or not.

TECHNICAL FEASIBILITY

What do we mean by 'technical feasibility'?

Technical feasibility refers to the process by which we assess whether the project is capable of being implemented — whether the desired 'outputs' can be achieved with the given 'inputs'. The 'process' of production of the goods or services must be clearly understood and it must be determined whether the fisherman involved has the necessary 'skills' to execute the process.

The broad aspects a technical feasibility study should look at are:

- * **INFRASTRUCTURE** : Land, building/shed, water, power, equipment and raw materials required.
- * **TECHNICAL EXPERTISE**: Specialised knowledge required for any field.
- * **MANPOWER/LABOUR** : Skills required.

Infrastructure

LAND

For a project to be implemented, a certain minimum land area may be required. **The area required should be available.**

For certain projects, a specific type of soil or water or climate may be required. *E.g shrimp culture would require a substantial land area with soil having a degree of clay content; there should also be brackishwater available. The area available should be suitable.*

BUILDING

The building/shed **necessary should be available and suitable.** Suitability could be in terms of the layout, storage facilities etc. It is important that raw materials and finished goods be kept safe from damage or theft. *E.g. a group of women decide to sell flour as a business. However, further discussion makes them realize that the flour has to be stocked in their houses, none of which are really suitable, as the roofs leak. The flour is, thus, in danger of being spoilt. A suitable stocking place is therefore necessary.*

WATER/POWER

The building chosen should have the necessary power and water available to run the business.

EQUIPMENT

The machines and tools that would be required to run the business and the ease with which maintenance can be done need to be considered. *E.g. a number of fishermen bought outboard motors, but more than 50 per cent of the boats remained idle as motors broke down often and the spares required could not be easily obtained.*

Before buying machinery, these points should be considered:

- Is it easily available?
- Is it within the budget of the entrepreneur?

- In case of equipment not being within the budget, is alternate equipment available or can manpower be used to obtain production of equivalent quality and at what annual cost?
- Is the equipment reasonably easy and inexpensive to maintain?
- Are the spares required to maintain the machine easily available?

RAW MATERIALS

Are the raw materials required

- available locally or easily transportable?
- relatively inexpensive?
- capable of producing finished goods of a quality acceptable to the consumers?

Technical expertise

Technical expertise should be available either with the entrepreneur or he should at least be able to contact an expert who has sound knowledge of the process/business.

Lack of this knowledge may result in an unnecessary loss to the entrepreneur. *E.g. the individual who wanted to raise poultry and decided on 'Leghorns', only to later discover, one by one, the problems involved and the specialized help required in rearing them.*

It would have been easier for the chicken farmer to check the following with a person who reared poultry:

- Is any special food required, is it easily available and how expensive is it?
- What are the vaccination procedures and timings? And is a veterinarian available?
- What is the mortality rate of the young ones and, therefore, at what age should the chicks be bought — when 3 days old or 3 weeks old? It is likely that buying 3-week-old chicks will be more expensive than buying 3-day-old. However, considering that the mortality rate of 3-day-olds is far higher than 3-week-olds, it may, in fact, be more profitable to buy 3-week-olds than 3-day-olds.
- What are the likely diseases poultry may suffer from and how should they be handled?
- What is their breeding pattern?

Manpower/labour requirement

It is possible that a particular business may need manpower in addition to the individual involved in the business. Such manpower may be unskilled, semiskilled or highly skilled. Before starting the business it would be worthwhile to check on the specific manpower requirements. Usually unskilled and semiskilled labour are easier to get than skilled labour. Skilled labour may be expensive or just not available at all. If the business finds, after it has started, that it cannot get the required labour, this could lead to a loss/failure which could easily have been avoided.

We have now seen what we mean by **technical** feasibility. It may conic across as something which is highly complex and difficult to do. In reality, however, it is possibly the easiest, as it is a common-sense approach to evaluating a business idea.

What do you think would be the best way of doing a technical feasibility study?

Guide the discussion along these lines:

The need for an expert

The different kinds of experts

- Technical/research experience

- Business experience

The role of the consultant in identifying available expertise and making it accessible to the fisherfolk requiring it.

A good way of doing a technical feasibility study would be to find out from an expert in the area the practical requirements and difficulties in the particular business. This picture will enable a decision to be taken on whether a project is 'possible' or not, *i.e.* whether it is technically feasible or not.

Who Is an expert ?

An **expert** is best described as a person who is already in the same business, is successful at it and has rich experience to share.

Other experts may be available with the Government agencies/institutes, universities, NGOs and aid agencies. These would be people who have actually studied the field, or worked in it.

How do fisherfolk get to meet these experts?

While fisherfolk could look around for people who are in the business, it might sometimes be difficult for them to contact the experts.

The role of the consultant then becomes very important. With his greater reach, he can get to these experts more easily and arrange a meeting between them and the fisherfolk.

What do we mean by ‘market feasibility’? Why do we need it?

Let us take the case of Rani who decided that she was good at making handicrafts and spent over a month in making some with shells. But she discovered later that there were really not many who wanted to buy them.

It would certainly have been better for Rani if she had found out basic facts, like the following:

- Whether anybody wanted to buy or was buying shell handicrafts. This is what we call a ‘market demand study’.
- If they were interested in buying such handicrafts, what types they were particularly interested in. This is what we call a ‘product study’.
- What the prevailing prices were for similar handicrafts and what prices people were willing to pay for her handicrafts. This is what we call a ‘price study’.

How many pieces could she get orders for at the prices at which she could afford to sell. This is what we call a ‘demand estimate’.

If she had known the answers to these *i.e.* had Rani done a **market feasibility study**, she would probably have taken one of the following decisions:

- Not to be in the shell handicraft business.
- Invest less time, effort and material and make only as much as she could sell. In this case, it would be only because she is very fond of making these handicrafts and does not want to lose touch with the craft.
- Lower her prices.
- Change the designs.

How would Rani have done a market feasibility study?

We saw that a market feasibility study essentially involves finding out the following:

- Demand for the product or service.
How acceptable the product is.
- At what price the product is acceptable.
- How many can be sold.

Guide discussions to focus on:

Need to identify the buyer/market

Need to make product samples to obtain reactions

Need to know how much it costs her to make the product and how the price she can sell at compares with the prevailing prices

- Need to know the minimum quantities she will be required to make and to obtain orders for them.

Please note the product could be one which is not available in the market or one where similar products are available.

If the answer to these questions are favourable, then it may be assumed that the product has a chance of being accepted in the market.

Now let us take a closer look at how we would go about finding these answers in the simplest way possible.

Demand for the product or service

The idea for the business arose only because there was a felt need. However, the need may not be strong enough or felt by enough people to make the business successful. Now, what do we mean by that?

Let us take the case of Chinong village, where some young women feel they would like to have a hairdresser in the village. Opening a hairdressing salon would be a good business idea only if many of the women felt the need to have their hair dressed and if they could afford it.

Similarly, the lack of a vegetable shop/vegetable gardens in the village may point to the need for vegetables to be sold in the village. This again would be a good business idea only if the women in the village felt the need for vegetables and realized that they needed to supplement their diet with vegetables.

We can therefore understand the demand for a product if we talk to the people who are going to actually buy it and use it.

Product acceptability

First of all what do we mean by 'acceptability' of the product? By **acceptability** we really mean that all features of the product are acceptable. *Let us take the case of Abdul who sells coffee at a roadside stall.*

WHAT WOULD BE THE FEATURES OF HIS PRODUCT?

The features of a cup of coffee would be its consistency, colour, sweetness, aroma, quantity and temperature.

Here we should note that a product could be entirely new or a modification of an existing one.

In the case of an entirely new product, it would be essential to get some samples made (say five to ten), get some people to use them and find out what they feel about the product. This would also help you to develop a better product in the end.

Thus, Abdul asks five friends to taste his coffee and give an honest opinion. Three complained it was not hot enough, one said it was too sweet and one had no complaints. With little effort Abdul had got some idea of what he might do to improve his product.

Modification of a product in the market can be done by finding out from the users of the product what they like and what they do not like about it. What are the features they would like changed or added? An answer will help you design a product which is better than the one already in the market.

Here again, we find out what we need by talking to the users in detail about the product.

WELL, THIS SOUNDS EASY WHEN THERE IS A PRODUCT. BUT WHAT DO YOU DO IN THE CASE OF A SERVICE?

Remember that a 'service' is similar to a 'product' and that, therefore, it also has features. In the case of a person having a repair service, the reliability, the speed and the quality of his work would be its features. Before a person were to start a vegetable shop, it would be better for him to talk to the housewives who are going to buy his vegetables and find out what kind of vegetables they need and around what time they should be available, etc.

An acceptable price

This is a very crucial question, as on this depends whether you will make a profit or a loss in the business, *i.e.* whether a business is viable or not. **Even if a product is good, if people are not willing to pay the price for it, then it may not be such a good business idea.**

Once you have arrived at a specific product to be made, it would be quite simple to arrive at the cost at which it can be made.

There are three points to be considered before arriving at the price of a product:

- What it costs to actually make.
- The market price of a similar product.
- The price you wish to fix for the product.

The price you wish to fix could be below or above the market price, but it **cannot be less than the cost of the product**, as you would then incur a loss.

Having decided on the price you are going to fix, it is necessary to check with the buyers whether the product is acceptable to them at that price, *i.e.* what they think of the price and whether they would buy it at that price.

Quantity saleable

Having decided on the price, it would also be safe to know, before commencing on a business venture, how much you can sell of the particular product.

Determining exact numbers is a very difficult exercise for anyone.

Guide discussion and focus on

- Whether prices are too high, too low or just right
- A willingness to try the product, but not willing to buy it even though the price is right could mean that the market may be not yet developed for that product. There is no Real Need.
- A willingness to try the product, but un-willingness to buy it because the price is too high could mean you need to re-look at the price. You can find out the reactions to various prices and see which one is most acceptable to the buyer and you. However, no price should be below your cost plus your minimum profit + margin required.

But what you really want to know is whether there is a market for the initial quantity with which you want to begin production.

The simplest way would be to approach buyers and, having shown them the product and indicated the price, find out how many they would be willing to buy. Once you are confident you can sell a particular number and that this will earn you a profit, you can then establish yourself and meet the increasing demand for your product by slowly increasing production. This would be the safest way to establish your business and ensure that you are successful.

We have now seen how a market feasibility study can help a business and how to go about it. The one thing you need to remember is that the buyer or user of your product will determine whether it is a success or not and, so, it is important for you to understand who is going to be your buyer/user.

Are there any other factors that could affect demand?

Yes. The other factors which could affect demand and which we should keep in mind are:

- * Seasonal factors that sometimes affect **demand**, *e.g. during the lean season in a fishing village, sales of everything that is not considered a necessity might fall as people have less money to spend.*
- * **Competition existing or about to enter into the same field**, *e.g. if Fatima opens a tea stall next to Abdul's coffee stall, Abdul can expect to lose some business to Fatima.*

MATCHING RESOURCES

What are the resources required for a business?

The three basic resources for any economic activity are:

- * **LAND:** A place to carry out the activity as well as access to the natural resources there.
- * **LABOUR:** Human work to produce the goods and services.
- * **CAPITAL:** All other forms of wealth and value needed to produce more goods or services.

All economic activities require these three inputs in different proportions. Often the input which you have in greatest abundance locally will determine which business idea to put into effect.

Let us look at *the example of a vegetable garden* and see what resources you might require.

Land

For a vegetable garden, a plot of land is the obvious requirement. **But not just any plot.** The following features of it must be considered

- Size and topography.
- Soil fertility.
- Exposure to sun and wind.
- Water source (rain and irrigation).
- Access to shelter (for supplies, equipment and crop).
- Availability of power (electricity, diesel or local source).
- Access to transport net.

Labour

A vegetable garden might need both unskilled and skilled labour. Consider who will till, plant, weed, water and harvest? Who will clean, pack, transport and sell the product? How much labour and at what time. Will the labour needed be available during the peak harvest season?

Capital

Capital is what makes it possible for the labour and the land to produce wealth. Sometimes the capital is raw materials and tools you already have, but often you don't have all you need. Thus you must find, barter or buy the capital inputs you need. For this reason people often think of money when we say 'capital'.

What are the capital inputs required for your vegetable garden and how will you get them?

<i>Items we have</i>	<i>Items to barter for</i>	<i>Items to buy</i>	<i>(Rs.) Cost</i>
Tools	Manure	Seeds	30
Storage	Fencing	Packaging	180
		Transport	40
		Wages	<u>3,000</u>
			<u>3,250</u>

You already have the tools and storage facility. Manure and fencing are available with neighbours and you can get them by paying in kind (vegetables) later on. However, the proper seeds, packaging, transport and wages you will have to pay, will come to Rs. 3,250, and this must be paid before the harvest, which brings in the money.

Do you have the land, labour and capital resources necessary? Can some capital resources that must be bought, be obtained by barter? If not, do you have access to the money necessary through your own funds and/or through loans? How much will the loans cost?

ACTIVITIES

Assessment of resources available for the microenterprise

The same three groups, based on their experience and knowledge of fisherfolk, draw the portraits of those whom they are helping to identify a microenterprise. For the purpose of this exercise it could be restricted to an individual. This portrait is then written on a chart and put up for all to see.

The chart should contain the following elements:

WHO IS BEHIND THE MICROENTERPRISE?

<i>Background of the individual</i>	<i>Resources available with him</i>
Family size	Land/Buildings
Education	Money-Savings/loans, etc.
Skills	Manpower

Main source of income
Total monthly household income
Income from main source
Income from other sources
Savings available

Deciding on the right idea

Each group picks any two of the ideas presented by them and which they feel are technically feasible.

They then take each idea and match the resources available with what is required.

	<i>Required</i>	<i>A available</i>
Skills		
Manpower		
Local resources/raw materials		
Land		
Money		

Based on the matching, they arrive at one, two or no project idea. They have to give reasons for their decision and convince the other groups about their decision.

THINGS TO REMEMBER

- A business idea may not be good because
 - it is not really possible (technical feasibility);
 - there is no market (market feasibility); and/or
 - the individual/group cannot generate the required resources.
- Technical feasibility is essentially ensuring that
 - the infrastructure (land, building, water, equipment) is both available and suitable;
 - the technical expertise required is available; and/or
 - the skilled labour required is available or can be trained.

The best way of doing a technical feasibility study would be to meet with an expert, who is

- a person already in the business; and/or
- a person who is studying the business

- Market feasibility is essentially to ensure that
 - there is a demand for your product;
 - your product features are acceptable;
 - the price at which your product is acceptable gets you a profit; and
 - you have an assured market to begin with for at least a minimum volume.

The best way of doing a market feasibility study would be to identify the buyers/users of the product and ask them about their views and intentions.

- Matching of resources should be done to ensure that sufficient resources are available to begin a business. The resources would be:
 - Land and access to the resources required,
 - Labour, and
 - Capital.

First, list what is required for a project and what you have available under each of the above headings. Then match what you require with what is available. Shortfalls, if any, should be looked at to see if they can be made good by collection, bartering, hiring, buying, borrowing.

Once a project idea is found to be technically feasible, has a market and there are sufficient resources, then it could certainly be classified as a good business idea.

However, there may be more than one idea which is good. We need to be sure we choose the best or the right idea and that is the one which will give the maximum profit. At this stage, you would need to do a detailed **‘Financial Feasibility’ study to select ‘The Right Idea’**. In the next chapter we will look at ‘Financial Feasibility’.

Financial feasibility

3

What are we going to look at in this chapter?

It is advisable to look at Chapters 13, 15 and 17 on Basic Accounting, Working Capital and Banking and Finance, before commencing this chapter.

- What is meant by 'financial feasibility'.
- Classification of expenses into one-time and recurring expenses.
- Whether the business thought of will be/is able, in terms of the money available, to:
 - Start up, and
 - Keep running.
- Whether the business thought of is likely to generate profits and to what extent.
- Whether the cash likely to be generated by the business will be sufficient to:
 - Repay loans;
 - Replace worn-out assets; and
 - Give the owner a profit at least equal to the profit of his second best idea.

What is 'financial feasibility'?

In Chapter 1 we made an exhaustive list of possible business ideas.

In Chapter 2 we saw that we could short list 'Good Ideas' by doing a technical feasibility study, market feasibility study and matching resources required with what is available.

The few projects thus short-listed may all be good ideas, but the 'Right Idea' will be the one which is 'financially viable'. We would need to do a financial feasibility study to evaluate the business and determine whether it is viable in terms of:

- Money required to start the business and to run it, and
- Whether the business will generate sufficient cash to repay the loans, replace the worn-out assets etc., and meet the owners' profit requirements.

How do you estimate the money required to start and run a business?

Before you determine whether a business is feasible, you should be able to estimate the money required to start it. In order to do so, you need to first list all items required in the business and put against each the costs likely to be incurred. Based on when and how often the expenses will be incurred, these costs can be classified as **one-time expenses and recurring expenses**.

One-time expenses

These expenses are incurred only once — that is, when you start the business. Thereafter, they are incurred only when certain assets are completely worn-out and have to be replaced. Examples of one-time expenses would be the following:

- Land.
- Building/Shed.
- Machinery, equipment, tools etc.
- Advances, deposits for rent, electricity.
- Transport and installation of equipment.

Recurring expenses

These are expenses which are incurred every day in the business. Examples of recurring expenses are:

- Rentals/utilities.
- Material required for production.
- Labour costs etc.

Also refer to discussion on classification of expenses in Chapter 16, Break-even analysis and Best Product Mix and Appendix I: Accounting Practices.

EXERCISE

Saroja, a fisherwoman, wants to start a tailoring shop in her village. Estimated expenses are given below. Can you classify them as one-time expenses (OTE) and recurring expenses (RE)

	ks.	OTE	RE
Sewing machine	5,000		
Purchase of thread, needles etc.	150		
Shop rent advance	1,000		
Shop rent	100		
Tools, like scissors, scales, measuring tapes etc.	500		
Electricity charges	20		
Sundry expenses	200		
Transportation of sewing machine from town	100		
Total expenses	7,070		

The object of this exercise is to enable the participants to differentiate between one-time expenses and recurring expenses.

Money required to start the business

Once the money required for one-time expenses (that is, the money to start the business) are estimated, the question of arranging for the money arises.

It is not possible nor advisable to start a business entirely on borrowed money. Therefore, the owner of the business has to bring in a portion of the money required, if not all of it, from his own sources, such as savings, sale of personal assets like land, jewels etc. The balance, if any, will have to be borrowed from a bank, government, funding NGO, friend, relative, pawnbroker or private moneylender.

The plan of going into business, thus, usually depends on someone being willing to lend the rest of the money needed. If no one is willing to do so, the idea is often not feasible, as it cannot be implemented without the required amount of money.

Illustration

Lucas proposes to produce a small, wooden component required by a nearby factory. Lucas has to buy a machine costing Rs. /0,000/- for this purpose. The cost of transport and erection of the machine is Rs.2,500/-. Lucas proposes to take a shed on rent. The rent advance is Rs.5,000/-. Lucas has Rs.10,000/- to invest. Evaluate the viability of starting the business.

	Rs.
One-time expenses	
Cost of machine	10,000
Transport and erection	2,500
Total Machine cost	12,500
Rent advance	5,000
Total	17,500
Available resources	
Lucas' savings	10,000
Total	10,000

Since the resources available with Lucas are not sufficient to meet the one-time expenses, the money required to start the business, the idea is not viable. However, if Lucas can raise an additional Rs.7,500/-, the proposal will be feasible on the count of availability of money to start the business.

Money required to run a business

In addition to the money required to start the business, some money will be required to meet the day-to-day expenses, the recurring expenses. For example. a vegetable vendor should have some money to buy the vegetables which he intends to sell. If he does not have this money, how can he buy the vegetables in the first place? A woman who wants to rear ducks requires money to buy the feed. otherwise the ducks will die of starvation.

Further, to readily cater to the needs of the customers, a business must buy goods and keep them in stock. It requires money to maintain stocks.

Customers may not pay immediately for goods purchased. So the business has to give credit to customers. Money is required to extend credit to customers

From all this we see that money is required to meet the day-to-day keep stocks and extend credit to customers. This is called working capital.

Refer Chapter 15, Section expenses,

Estimating the money required to run a business

How much money is required if a business is to be run smoothly? This depends on the size of the business, the stock to be maintained. credit to be extended to the customers, credit you get from suppliers of goods and raw materials etc.

Illustration

Let us continue with Lucas’ wooden component business. The cost of each component is as follows:

	Rs.
Raw material	
Labour	2.00
Other expenses per unit, payable every day	1.00
Tootal cost	11.00

Lucas can produce 30 components a day and works for 25 days a month, 300 days a year.

Lucas has to keep at least 7 days’ stock of raw material to ensure smooth running Of the business. He also has to extend 15 days credit to the customer. The supplier of raw materials has agreed to extend seven days’ credit.

Assume Lucas can mobilize another Rs. 10,000 by selling his wife’s jewels. This would he needed to meet the shortfall of Rs.7,500 in the one-time expenses and the balance would go towards meeting recurring expenses. Sriram, a (lose friend of Lucas, has agreed to

lend Rs.1, 000. interest free, repayable after one year Evaluate if the proposal is viable as far as availability of money is concerned to start and run the business.

Daily production and sale = 30 components

Required stock of raw material = 7 days x 30 components x Rs.8
= Rs. 1,680

Cost of producing one unit of the wooden component
= Rs.11 (see previous page).

The customer will pay only after 15 days, but Lucas will have to continue to supply the components during those 15 days. Therefore, the money required to extend credit = 15 days x 30 units x Rs. 11.00 = Rs.4,950

Money required to run the business	Rs.
Money required to keep stock of raw material	1,680
Money required to extend credit to customer	4,950
Add. for safety, say	870
	7,500

Money available

Surplus after meeting one-time expenses (Rs. 10,000 - Rs.7,500)	2,500
Loan from Srirani	1,000
Credit extended by supplier (7 days x 30 units x Rs.8)	1,680
Total	5,180

The proposal is not viable as Lucas has only Rs.5,180 as against Rs.7,500 required to meet Recurring Expenses. **Lucas has to convince the customer to pay earlier, or the supplier to extend more credit or explore the possibility of reducing the level of stock without affecting the production. If not, the idea is not workable.**

Assume Lucas has arranged a loan with a local bank for the remaining amount of Rs.2,320 (Rs.7,500 - Rs.5,180) and the loan has to be repaid in two annual instalments of Rs. 1,160 each. Is this sufficient for Lucas to start his business?

Yes. The proposal is workable as far as availability of money to start and run the business is concerned.

Is the business idea profitable?

Once the viability of a business idea pertaining to availability of money to start and run the business is established, the next step is to examine whether the idea is **'profitable'**.

Profit, obtained only when income is greater than expenditure, is essential for any business. It is out of profits, that the loans taken

to start and run the business have to be repaid. The money needed by the owner for his living expenses, replacement of worn-out assets, etc., also depends on profits. Growth of a business organization depends on profitable conduct of the business.

It is profit that keeps the working capital (money provided to meet recurring expenses), which is the lifeblood of the business, intact. If a business is not profitable, the working capital will be gradually depleted and ultimately the business will have to be closed. Therefore, it is essential to evaluate whether a business idea is profitable or not.

Illustration

In the example of Lucas' business, *let us assume the selling price of each Unit is Rs./3* and estimate the profits the business is likely to yield in the next three years.

ESTIMATION OF PROFITS

	Year 1 Rs.	Year 2 Rs.	Year 3 Rs.
Income			
Income from sale of components =			
300 days x 30 units x Rs.]3 =	117,000	117,000	117,000
Total	117,000	117,000	117,000
Recurring expenses			
Cost of raw material			
= 300 days x 30 units x Rs.8 =	72,000	72,000	72,000
Labour			
= 300 days x 30 units x Rs.2 =	18,000	18,000	18,000
Other expenses			
= 300 days x 30 units x Rs.1 =	9,000	9,000	9,000
Interest at 10% per annum on bank loan of Rs.2,320 for the first year and on Rs.1,160 for the second year (original loan Rs.2,320 less first instalment Rs. 1,160)	232	116	
Depreciation (wear and tear) (Assuming the life of the machine, which cost Rs. 12,500. is two years and a new machine is purchased in the third year)	6,250	6,250	6,250
	105,482	105,366	105,250
Profit (Income-recurring exp.)	11,518	11,634	11,750

Refer to Appendix I for a detailed discussion on depreciation while studying this example.

The business proposal is expected to generate a profit of Rs.11,518 in the first year, Rs. 11,634 in the second year and Rs. 11,750 in the third year. Thus we see that the business idea is profitable.

Will the idea generate enough cash?

The cash profits, *i.e.* excluding expenses that are not incurred in cash, like depreciation (wear and tear) of assets, expected to be generated by a business should be sufficient to repay the loans taken to start and run the business, replace worn out assets and meet the living expenses of the owner. If the cash generated by a business is sufficient to meet all these, the idea is viable, if not, the idea should be dropped.

Continuing the example of Lucas' wooden components business, let us estimate what are the various sources of cash and whether they are sufficient to meet the commitments.

Let us first list the various sources from which Lucas is going to raise money in the next three years:

- Money invested by Lucas in the business.
- Loan promised by Sriram, Lucas' friend.
- Loan arranged from local bank.

The supplier has promised to extend credit for seven days to Lucas. but is this a source of cash? A little thinking will clarify that the supplier permitting Lucas to pay after seven days and his lending Lucas money to buy his raw material requirement for seven days and asking him to pay for the purchase immediately are one and the same. Therefore, any credit received from suppliers is a source of cash. Extending the logic further, any increase in credit extended is an additional source of cash and any reduction is use or outflow of cash.

Are there any more sources of cash? Yes, the most important source of cash, year after year, is the profit Lucas earns in the business.

Illustration

in our example, while computing the profits, we considered the expense on account of wear and tear of the machine in producing the component. This expense was not actually incurred in cash (during those years). It was already incurred at the time of commencement of the business. Therefore, while computing cash profit, this expense should be ignored. The amount allocated for depreciation and earned through the business is, in fact, treated as profit earned in cash.

First list the sources of cash for three years.

	Year 1 Rs.	Year 2 Rs.	Year 3 Rs.
Sources of cash			
Money invested by Lucas	20,000	—	—
Loan promised by Sriram	1,000	—	—
Loan from local bank	2,320	—	—
Credit given by supplier	1,680	—	—
Profits earned in cash (excluding noncash expenses including annual depreciation allocation)	17,768	17,884	18,000
Total	42,768	17,884	18,000

Now let us note down the requirements of cash

Requirement of cash

	Year 1	Year 2	Year 3
Purchase ^f Replacement of machine	10,000	—	10,000
Transport and erection	2,500	—	2,500
Rent advance	5,000	—	—
To keep stock	1,680	—	—
To extend credit to customers	4,950	1,000	—
Repayment of friend's loan	—	1,000	—
Repayment of bank loans	—	1,160	1,160
Lucas' managerial fee (12 x 1250*)	15,000	15,000	15,000
Total	39,130	17,160	28,660
Surplus/(Deficit)	3,638	724	(10,660)

* Assumed he requires a minimum of Rs.1,250 per month for his services.

We see that though the idea is profitable and Lucas has made arrangements for raising enough money for starting and running the business, the cash generated by the business is not sufficient to replace the machine after every two years.

The reason is simple. While the business is generating Cash Profits of about Rs. 18,000 a year, after meeting Lucas' home expenses of Rs.15,000 a year, the surplus is only about Rs.3,000. This is not sufficient to repay the loans and replace the worn-out equipment from time to time.

The idea would be feasible only if:

- Lucas can increase his selling price and generate more profits; or
- Reduce his costs and increase his profits; or
- Cut down his home expenses; or
- A combination of all these.

EXERCISE

Shuba wants to start a retail, door-to-door, fish-vending business. The estimated expenses are as follows:

Cost of cycle Rs.1,000. A daily requirement of 20 kgs of ice at 1.50 Rs/kg. Average cost of fish is 45Rs/kg. Cost of ice box is Rs.300. Average selling price of fish is 50 Rs/kg. 25 per cent of Shuba's sale will be on a month's credit. She will have to buy the fish only for cash. Shuba will be able to sell 10 kg of fish a day on an average. She will have negligible stock at the end of the day. Expenses for the day, like tea etc., will be Rs.5. Shuba will work for 300 days in a year.

Instructor to initiate a discussion and focus on alternatives like hiring, instead of purchase, of cycle.

The life of the ice box is two years and of the cycle is three years,

Shuba has got Rs.1000/- to invest. The local Bank Manager knows Shuba very well and is willing to give a loan if necessary. The loan will have to be repaid in three equal annual instalments and carries an interest of 10% per annum.

Shuba requires at least Rs1,000/- per month as her salary.

Examine the financial feasibility of this proposal.

THINGS TO REMEMBER

- It is not sufficient if a business idea is technically 'doable' and there is a market. The idea should be financially feasible.
- Financial feasibility of a business idea is tested by the following criteria:
 - Estimation of one-time expenses (money required to start a business) and finding out if the resources available are sufficient to meet the expenses.
 - Estimation of recurring expenses (money required for running the business) and comparing with available resources.
 - Estimation of the profits likely to be generated by the business.
 - Ascertaining if the profits generated by the business are sufficient to repay loans and replace assets when required and at the same time meet the owner's personal expenses.
- A business idea will be financially feasible only if it is viable on all the four criteria mentioned above. **If it does not satisfy any one of the criteria, the idea is not workable.**

Appropriate ownership form

4

What are we going to look at in this chapter?

- What we mean by ownership form.
- Three forms of ownership relevant to microenterprises.
- Their relative merits and demerits.
- How ownership form determines the resource strength and working style of the business.

What do we mean by ‘ownership form’?

Ownership form refers to how a business enterprise is owned. In other words, “Who owns the business”.

Ownership forms

Different forms of ownership exist by custom and are recognized by law. The ownership **form** determines the strength and style of the functioning of the business.

Ownership forms relevant to microenterprises are:

- Sole proprietorship (owned by one person).
- Partnership (owned by a few persons).
- Cooperative (owned by a large group).

Sole proprietorship

In this form of ownership, the entire business is owned by a single person. The owner enjoys all the profits of the business, but also accepts all losses. This single owner has absolute freedom to conduct the affairs of the business as desired, and is answerable to none. The owner’s liability is unlimited, *i.e.* in settling the debts of the business, if the business assets are insufficient, the personal assets will also be taken. Being owned by a single person, the resources of the business are limited.



Participants to be asked to identify sole proprietorship organisations in and around their localities.

Discussion to bring out the following key factors:

Individualistic attitude.

Major resource required is individual skill.

Even if not a skill-oriented business, the capital required is small

NOTES

A situation where a **sole proprietorship** would be a **suitable ownership** form is when a person has sufficient skills and money to carry on the business alone, *e.g. mechanic repairing engines; seamstress making garments.*

Partnership

Participants to be asked to identify partnership organizations in and around their localities.

Discussion to bring out the following key factors:

Results of combined effort, are generally more than the sum of the individual efforts.

- Sharing of risks.
 - Increase in efficiency due to division of tasks.
- Discuss likely sources of conflicts like

- individual attitudes;
- diverse backgrounds;
- lack of trust;
- ego problems.

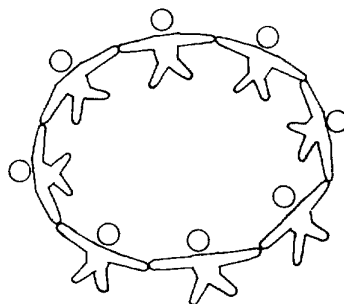
Here, two or more persons join together and start a business. The owners collectively are called the firm and, individually, partners. The profits and losses are shared by the partners in agreed proportions. Their liability towards the firm's debts is unlimited. Freedom of conducting the affairs of the business is restricted, as a partner is answerable to the other partners. Since more than one person is involved, the resources of the firm are usually more.



A partnership could also be formed to bring together the resources required for the enterprise. Resources could include skills, money, land, raw material etc., *e.g. Lakshmi has money to buy palm leaves; Saraswati has skills to weave a basket. Lakshmi and Saraswati can come together to form a partnership and start a basket-weaving business.*

Cooperative or group-ownership

In a cooperative form of ownership, a large number of persons collectively own the enterprise and are involved in its activities. The joint owners are called members. All the members contribute an equal sum towards capital, share the profits equally and have equal rights. Since a large number of members are involved, the management of the cooperative is entrusted to a small group of members who are elected by the many. The financial strength is significant. **The liability of the members is limited**, *i.e.* even if the assets of the cooperative are insufficient to satisfy the debts, the members' personal assets cannot be touched.



A cooperative is also much more influential than individuals or partnerships. It represents a big group of people and, quite often, this gives it access to Government programmes and developmental agencies which extend financial help in the form of grants or interest-free loans.

Ask participants to identify 'cooperative' ventures in which they have participated or which they are aware of.

Bring out the following points during discussion:

- Common interest.
- Need for larger resources.
- Better bargaining power.
- Discuss problems in co-operatives:
 - Nonparticipation by majority of members in the affairs of the cooperative, mainly due to apathy.
 - Slow & inefficient
 - Organizational politics.

EXERCISE

Trainers to list a few project ideas and ask the participants to suggest appropriate forms of ownership. The suggested forms to be discussed and the reasons to be identified why a particular form of ownership is more suitable

THINGS TO REMEMBER

- How a business is owned determines the resource strength and management style of the business.
- The business could be owned by a single person (sole proprietorship), a few persons (partnership) or a large group (cooperative).
- **Sole proprietary concerns**
 - Absolute freedom to act and make decisions.
 - Proprietor enjoys all the profits and accepts all the losses.
 - Resources limited.
 - Unlimited liability.
- **Partnership Firms**
 - Freedom of action and decision-making restricted.
 - Profits and losses shared by partners in agreed proportions.
 - More resources.
 - Unlimited liability.
- **Cooperatives/Large Groups**
 - Freedom of action and decision-making highly restricted.
 - Management entrusted to a few elected members.
 - Significant resources.
 - Limited liability.

Implementing a business idea 5

What are we going to look at in this chapter?

- What we mean by implementation and why it is crucial.
- Classification of activities into 'sequential' and 'parallel' categories.
- Importance of sequential activities.

What is 'implementation' and why is it crucial?

Once a 'business idea' has been selected, it has to be **implemented**. The implementation stage, up to start up of commercial operations, is very crucial to the success of the business, since any delay in implementation could lead to the owner being faced with several problems. Some of these are:

- Increases in the capital cost of the enterprise.
- Interest on borrowed money having to be paid. This could become a very heavy burden.
- Someone else entering the same line of business. You may then lose out to the competition.
- In a seasonal business, like fruit processing, you could miss the season.

The implementation process would consist of undertaking many individual 'activities' in order that the necessary infrastructure is in place before the business commences operations.

These activities could include:

- Making arrangements for adequate 'cash'.
- Getting the necessary permissions/licences, if applicable.
- Deciding on the location and acquiring the necessary place. In the case of a production activity, before deciding on the location you should keep in mind the sources of raw materials, labour and the market. In the case of trading and service activities, the market has to be kept in mind.
- Creating adequate infrastructure, like building/shed etc.
- Getting water supply.

- Getting power connections.
- Acquiring the necessary machinery/tools for the enterprise.
- Recruiting qualified manpower.

This activity list should be made as exhaustive as possible. Each of the activities should be broken up into subactivities. This could be done by asking very simple questions like Who? What? Why? Where? When? and How? Along with this list, it is also essential to determine the time required to complete each of the activities listed.

Once this detailed listing is done, you should then determine the sequence of the activities and separate them into **parallel activities**, those which could be done at the same time, and **sequential activities**, those which can be done or performed only after some other activity is completed. *E.g. The fish pond cannot be filled before it is dug (sequential) but it can be done along with some other activity (parallel activity), e.g. tile pond and the well can be dug simultaneously (parallel). However, the well can be dug only after the proper location has been identified (sequential).*

The implementation of a project progresses along with the completion of the parallel and sequential activities. However, the time taken to complete the sequential activities will normally be the time required to complete the project.

Illustration

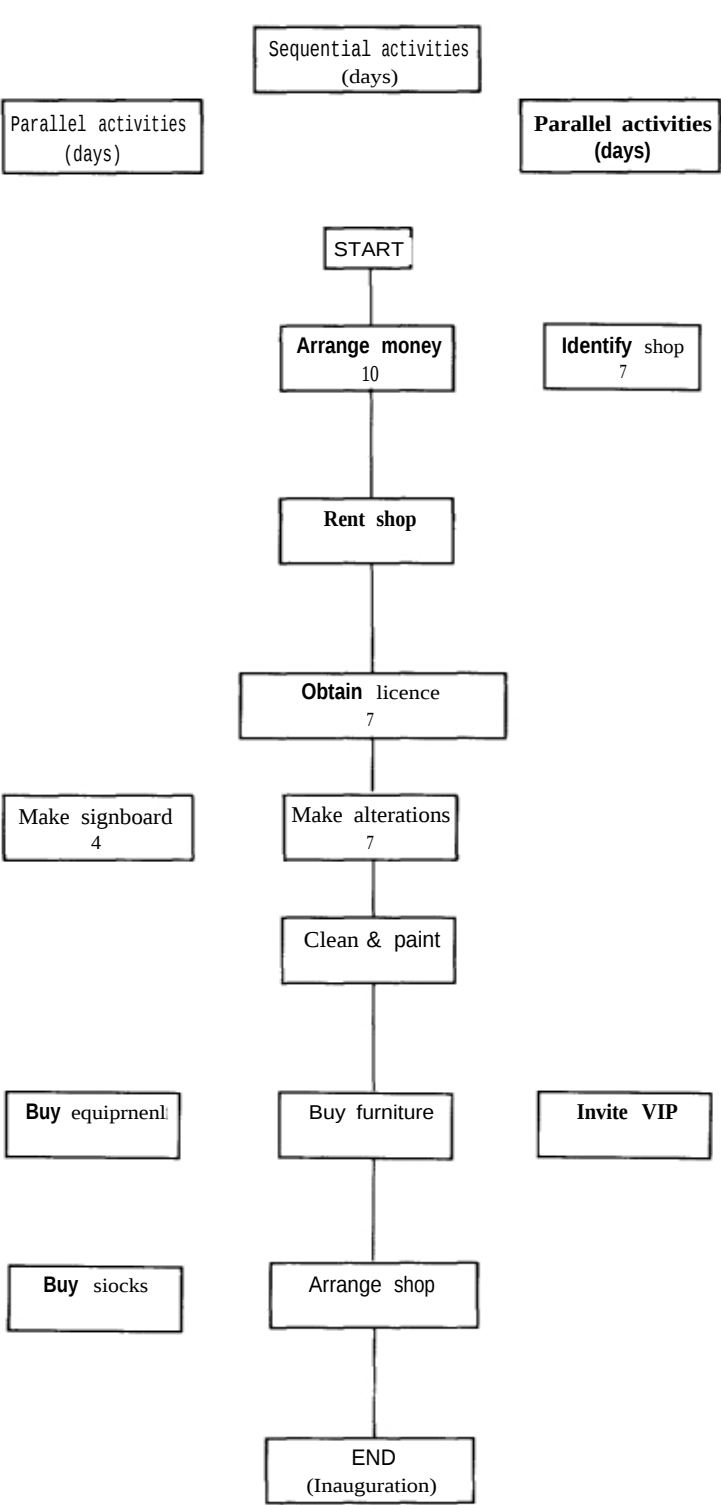
Let us take the example of Fatima who wants to set up a tea stall. The activities involved and the time for each activity is as follows:

Activity duration in

Identify shop	7
Rent shop	
Arrange money	10
Alterations to shop	7
Obtain licence	7
Clean and paint	
Buy equipment	
Buy furniture	
Buy stocks — tea leaves, sugar etc.	
Make signboard	4
Invite VIP	
Arranging shop	
Total	44

Note: The 44 days of activity can, however, be done in 30 days, as some of the work can be done in parallel.

Setting up Fatima’s Tea Stall



The minimum time to set up Fatima’s tea stall will be the sum of the time taken to complete the sequential activities. i.e. 30 days. Any delay in the sequential activities will result in delay in completing the project.

EXERCISE 1

List all the activities and subactivities involved in a project of your choice.

Estimate the time required for each of the activities.

Determine the sequential and parallel activities.

Determine the time required to complete the project and commence operations.

EXERCISE 2

Damodran wants to raise chickens in his backyard. He has decided that there is enough place and that, with minor improvements, the idea would be feasible. He needs to buy some materials from the local store. The backyard needs to be levelled and a wooden fence built to enclose the space. He can buy chicks' from a hatchery 50 kms from his village. The feed is, however, available locally. He has to get some more money to meet his initial costs. He has a brother who can help him in this venture until the actual commencement.

List the activities, subactivities, estimate the time required for each activity, distinguish between sequential and parallel activities and calculate the overall time within which the business can commence operations.

THINGS TO REMEMBER

- Timely implementation of a business idea is very important because delays will cause increases in costs and allow competitors to enter the field.
- Implementing a business idea consists of completing many activities and subactivities in order that the necessary infrastructure is in place.
- Activities can be classified into parallel and sequential activities.
- The sum of the time required to complete the sequential activities is the time required to implement the business idea. Any delay in completing the sequential activities will result in delay in completing the project.

SECTION II: Running a business

6. Marketing
7. Production/Manufacturing
8. Purchasing/Buying
9. Stocking
10. Pricing
11. Selling
12. Distribution
13. Basic accounting
14. Bookkeeping
15. Working capital
16. Break-even analysis and
best product mix
17. Banking & Finance
18. Risk & Insurance

Appendix : Accounting practices

RUNNING A BUSINESS

Having identified and started a business is, by itself, not enough to ensure its success. Running it efficiently is essential to ensure that the business stays competitive and profitable.

This section covers topics relevant to the day-to-day management of the business, like:

- Understanding needs and wants of customers (communicating with the customer).
- Production/Manufacturing.
- Buying and stocking.
- Pricing the product/service.
- Accounting and managing day-to-day finances.

To be a successful consultant it is essential to understand the concepts and principles covered in this section and to develop the skill to apply them in diverse practical situations which may arise in the field.

Let us now take a look at these concepts and principles in detail.

Marketing

6

What are we going to look at in this chapter?

- Understand the needs and wants of people.
- How marketing is the process of providing the goods/ services to meet those needs/wants.
- The process of exchange involved in satisfying needs and wants identified.
- Understanding the consumer communication and its importance in the process of exchange.
- The actual process of marketing.

What is 'marketing'?

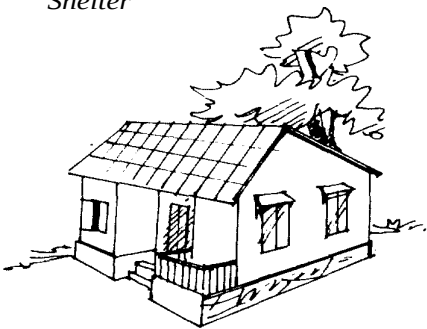
Marketing may be defined as satisfying the needs of consumers by a business enterprise, by providing them the goods and services they require in exchange for money. This involves understanding your customer/buyer and promoting your product.

What are 'needs'? And how are needs satisfied?

Needs are very basic.
like:

Objects/services which satisfy
these needs

Shelter



House to take shelter in

Needs are very basic.
like:

Objects/services which satisfy
these needs

Food



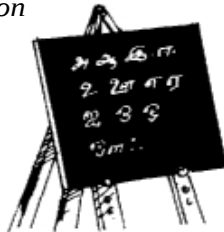
To satisfy hunger

Water



To quench thirst

Education



To achieve literacy and
numeracy

What are 'wants'? How do they differ from 'needs'?

A want is something a person desires, whether it is needed or not. It is more than a need. But 'need' can also be qualified with 'wants'.

Shelter



You may want a house which gives status/meets specific requirement.

A big house/A house with land for children to play.

Marketing

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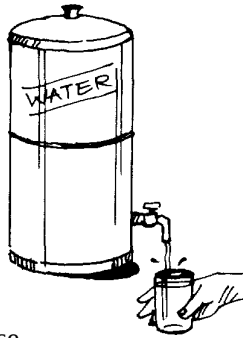


Food with nutritional value, like *dal*, rice, milk, egg, vegetables,

Tasty - Sweets, snacks

Convenient - When there is no time to make it

Water



Clean water to prevent disease

Education



Self-development to become something in life.

How is a need met?

A basic need may be satisfied by:

Self-production



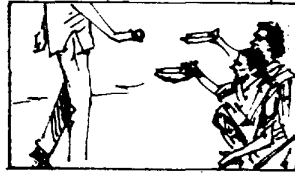
Cooking to meet hunger need.

Coercion



Grabbing from someone else.

Supplication



begging from someone else

Exchange



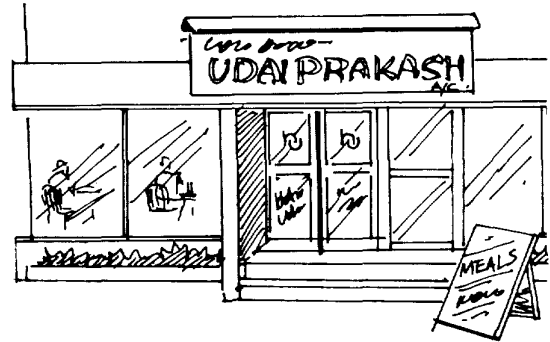
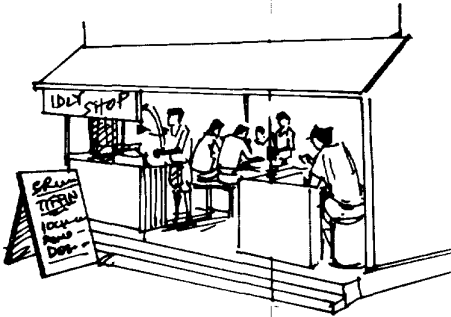
Exchanging some other resource for food. The resource may be money, other goods or services.

Society basically centres on the process of **exchange**.

Let us now look a little more closely at wants, needs and the process of exchange.

How does the process of exchange occur?

The individual knows his needs and wants as well as what he can give in exchange for them. *i.e.* **MONEY**.



Both the stalls are food stalls, but they satisfy different needs.

The decision to eat at one or the other would depend on a number of questions.

What time is it?

Early morning or evening or midday.

Why are you going there?

To while away your time or have a quick bite to eat.

Where is it?

Near workplace, near house.

How much money can be spared?

Having decided on a product which is needed by the people and having made it, can you safely assume that the product will now sell? *Let us c'onsider the story of Das.*



Das is veiy good with his hands. He likes making new implements.



Das lives in a village near Manakudy. There is a major problem of rats in his village and in the neighbouring villages.



Das decides that the people of the village need an effective rat trap to solve their problem.



He put his mind to it and made the most superior rat trap. Thereafter he sat at home and waited for orders for the rat trap. He waited a long time and none came.

Das was surprised. But, he shouldn't have been. How are people to know that he has got a solution to their problem? He has not marketed the product.

Marketing therefore assumes

- there are two parties;
- each has something of value to the other; and
- each is capable of communicating with the other.

Guide discussion to include

How will Das show that his rat trap works?

To whom will he prove this? To elders in the community? Or a shop-keeper through whom he could sell the traps?

What are the features he should stress: quality, reliability, fair price?

There are, of course different ways of communication. They could be by word of mouth, by demonstrating to a group of people, by using printed material (signs, posters etc.). The method chosen should be the one which most effectively reaches the customer at low cost and is received positively. *E.g. the people of the village may not be willing to buy his rat trap for Rs.20/- if he were to put up a notice in the village to that effect. They have each bought rat traps earlier which have not worked.* Now what should Das do?

Process of marketing

Having looked at what marketing is and why we need to market a product, let us see how you should set about it.

Before actually marketing a product, you should understand:

Who the customer is.

What the customer is really looking for.

What you wish to communicate to the customer and how you could do it most effectively.

Who is the customer?

Though the local market is a place to begin with, you should look beyond to see where the real market for the product is. *e.g. the best market for products like seafood. is probably the nearest town and not the village.*

What is the market looking for?

- A need satisfied,
- as well as other qualities.

e.g. if FOOD is the need and people need a hot meal near their work place, they would also expect

- *a certain quality of food;*
- *probably hot food;*
- *a clean location;*
- *cleanliness in preparation/serving;*
- *a reasonable price; and, perhaps.*
- *the food packed for them.*

What are we going to communicate and how are we going to communicate to the market?

There should be effective communication of the needs met by your product/service.

What is effective? This means that the message must reach the right people and be believable to them.

Who are the right people?

- People likely to buy the product/service.
- People likely to influence the buying.

What makes the message believable?

- Realistic claim, feasible idea, no exaggeration.
- Product should live up to the claim.

EXERCISE

Given below are a list of microenterprises which could be started by fisherfolk.

The product/service is mentioned. Write down against each

- the primary need met by the product;
- the other needs that could be met;
- the expectations from the product/service;
- the likely buyers of the product/service; and
- the communication process: What should be the message? whom should it be addressed to, and how?

<i>Products/ Services</i>	<i>Primary needs met</i>	<i>Expectations from product/ service</i>	<i>Main buyers</i>	<i>Message to be communi- cated</i>	<i>Who and how to be ad- dressed</i>
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1. Fish processing
2. Fish culture
3. Net-making
4. Engine repairing
5. Teashop with snacks
6. Vegetable vending
7. Coconut cultivation
8. Cycle repair shop

The discussions should enable the participants to understand each other's thoughts and, thus, clarify their own on the concept of primary needs, expectations, the buyer, and the effectiveness of message communicated.

Discuss why the messages and media suggested should be used.

THINGS TO REMEMBER

- Marketing is directed at satisfying needs and wants through a process of exchange.
- 'Needs' are basic, like shelter, food etc. 'Wants' are satisfaction of basic needs, are also more defined and show the aspirations of people.
- The process of exchange occurs when the individual translates his needs and wants into buying what is available in the market, if he can afford it.
- The process, therefore, assumes that the two parties understand each other and are able to communicate with one another.
- The process of marketing involves:
 - Understanding your customers;
 - Knowing what the customers are looking for; and
 - Communicating to the customers, *i.e.* ensuring that the message is truthful and that it reaches them.

Production / Manufacturing

7

What are we going to look at in this chapter9

- What is meant by a production or manufacturing enterprise
- The different kinds of production processes.
- Selection of a specific process.
- What production management is all about

What kind of enterprise is each of the activities shown below?



Among the activities shown in the pictures, only fish paste-making is a production or manufacturing enterprise.

A production **enterprise** is one where the raw material (fish) is bought or collected, is then processed (value added) or cultivated, and the product made. In some cases, the product is then packed in the required quantities and transported to the selling points, the traders/customers. In the vegetable shop, vegetables are bought and sold as they are and, hence, there is no production involved. It is only a buying and selling (trading) enterprise. In the cycle repair shop, the person is waiting for cycles needing repair to arrive. He offers his services, his skills, to put them in order. Therefore, this is a service enterprise.

What is it that is exclusive to production/manufacturing enterprises?

In production/manufacturing enterprises, value is added to raw material and a finished (end) product made.

There could be several types of processes to make the end product.

e.g. shoe-making or hook-and-line fishing is a job process, as each shoe has to be made or each fish caught by a person.

Aquaculture and agriculture deal with periodic crops. So, *growing shrimp or pumpkins* is a batch process. *Shrimp paste processing* is also a batch process. The shrimp are marinated in batches *i.e.* each batch is left to ferment for a time every day. The batch size would depend on the size of the container (production capacity) or the demand for the product.

Illustration

Quantity of shrimp paste which can be sold = 15 kgs

Capacity of container = 20 kgs

Only 15 kgs of shrimp paste should be produced as more than that would not be sold.

On the other hand, if the capacity of the container were only 10 kgs. the quantity which is processed might only be 10 kgs.

Batch size, could, thus, be limited by the production capacity or the customer demand, whichever is lower.

Continuous process, on the other hand, is a process which does not come to a stop at all. If it does, the cost of restarting would be high. These processes may require complex equipment if they are in manufacturing, but carp ponds, tea estates and dairies are simpler forms of continuous production processes.

The process selected is usually determined by the product and the skills, money and equipment available. *E.g. take the case of shoe manufacture. This could be a job process, with a person making one pair of shoes completely before starting on the next. This could also be done as a batch process, with several shoes being manufactured at a time.*

Let us assume there are three different steps in manufacturing shoes:

- Stitching the upper;
- Making the sole; and
- Joining the two.

There is a demand for 10 pairs of shoes.

If three people get together and each does what he is best at in this manner,

NOTES

Shoe upper
10 pairs

Soles
10 pairs

'C'
Stitching
10 pairs of shoes

the shoes will be ready in batches of 10 pairs a day.

What is production management?

Production management ensures that your production process does **NOT** come to a stop.

The process could come to a stop because of many reasons:

- Equipment breakdown and no one, or no spares, to repair it.
- There is no raw material to work with.
- There is a production bottleneck e.g. A' can make 10 pairs of shoe uppers and 'B' can make 10 pairs of shoe soles. But 'C' can only stitch 5 pairs of shoes in a day. This would mean that 'A' and 'B' should also make only 5 pairs of uppers and 5 pairs of soles. The other way to overcome this production bottleneck would be to have one more person stitching, thus increasing the capacity to handle 10 pairs of shoes a day.

You need to study the process, see where the bottleneck is and work out ways to remove it.

Solutions could lie in re-allocating work, training for better skills, getting additional manpower, getting better equipment, stocking carefully on spares, arranging for routine maintenance or even ensuring regular supplies of raw materials.

You should not produce too much

The quantity produced should also be saleable. It would therefore be a good idea to restrict production to demand level, unless you can do something to increase demand for the product.

What you produce must be of relevance to the market

Modification to suit customer requirements should be a continuous process.

The product you currently make may have some defects. Such defects should be rectified and a modified version produced. Also remember that modification is a continuous process.

What you produce should be produced as effectively/v a.c possible

Effective production can be had by optimizing the mix of land, labour and capital. This could be achieved by making changes in the working methods or by employing better tools, e.g. 'A' *could probably increase his production to 15 pairs of shoe uppers if he were to use better tools or implements.*

Raw material could be used more effectively, e.g. *if you are able to either use less of it or use a less expensive material without reducing the quality of the product.* This can be done with a bit of planning.

Finally, what you produce must be of a certain quality

Products should be made well: they should be of a certain quality to satisfy the customer. To ensure this quality is maintained, the products must be checked where they are made before they are sent out.

Check a certain number of units manufactured every day. The number could be fixed, say 5, or it could be a proportion, say 1 out of every 5 units. Obviously, the more you check the better the quality. However, the time and costs involved rule out a near 100% check and you will probably only check a representative sample of production. e.g. *if there are five hatches of production a day and you have decided to check 5 units for the day, you should ensure that you check one from each hatch.*

What do you do when there are defects?

Defects may arise due to faults in instructions given, machinery malfunction or mistakes made by people. The cause of the defect should first be identified and remedied so that the production of defectives can be stopped. Defective or flawed units could be rectified, if possible, and, if not reused, sold as 'seconds' at a discount. In the long run, it may be cheaper to work to avoid faults than to rectify or replace products after the faults are discovered.

THINGS TO REMEMBER

- Production is a means of adding value to raw materials and making a finished product.
- Different methods of production are:
 - Job process.
 - Batch process.
 - Continuous process.
- Selection of the method of production depends on
 - the product being manufactured, and
 - the resources available.
- Production management ensures
 - being able to produce the required amounts of products of acceptable quality in the required time, and
 - optimum utilization of resources available (land, raw material, labour, power, machinery, etc.) to reduce cost of production and improve quality of product.

Purchasing / Buying

8

What are we going to look at in this chapter?

- Where to buy.
- At what quality.
- At what price.
- How much to buy.
- When to buy.
- Advantages of collective buying.

What is 'purchasing'?

Purchasing raw materials or finished goods is an important function in a business as it affects the cost of goods produced or traded, the level of profit and customer satisfaction.

ACTIVITY

Group discussion

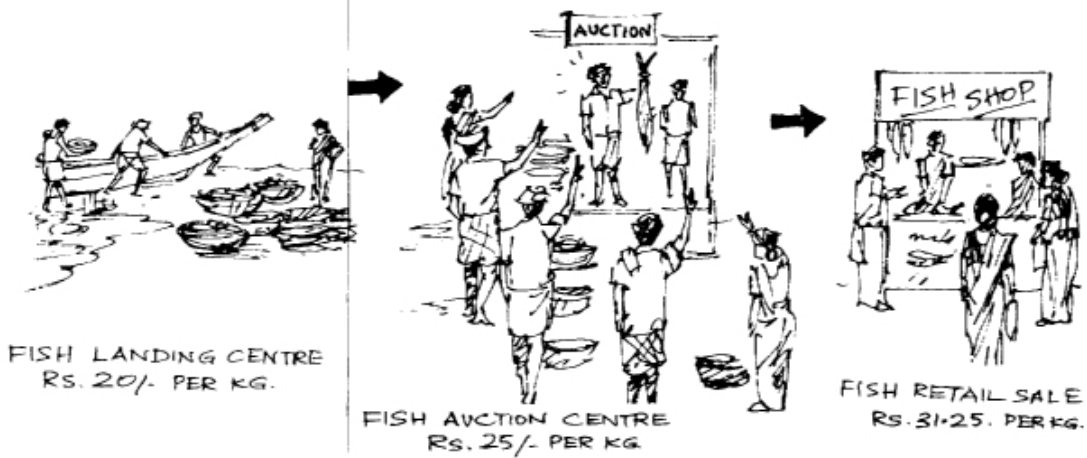
Divide the participants into 2 or 3 groups. Each group is given a specific business area and asked to list the various aspects to be considered before making a buying decision and to present them before the class. A general discussion should follow the presentations, guided by the trainer, who should ensure that the important aspects are brought out.

Some important aspects of purchasing

- Where to buy.
- Quality
- Price.
- How much to buy.
- When to buy.

Where to buy

Every product, before it reaches the consumer, goes through a number of hands. The sequence of exchanges from the primary source (place of production) to the consumer is called the **distribution chain**.



When you buy from the primary source, the price will be less compared to the price at any other point in the distribution chain. The difference in price is due to expenses on packing, loading and unloading, transport, warehousing and the profit of the middlemen at each stage. However, it is not easy for a small trader to buy from the primary source for these reasons:

- Goods will not be sold in small quantities at the primary sources.
- They may insist on cash payments.
- It may not be economical or convenient to transport small quantities.

RELIABILITY OF THE SUPPLIER

Reliability of the supplier is more important than price and payment terms. If the supplier is not reliable, the retailer will not be able to keep up supply commitments, leading to customer dissatisfaction. A fair assessment of the supplier can be made on the following basis:

- How long the supplier has been in business.
- What reputation he has got among his customers.
- How big the supplier's business is.

- Whether he would supply good quality material at a reasonable price.
- Whether he would be interested in doing business with you, considering the size of your requirements.
- Whether he would be interested in offering credit to you.

ALTERNATE SOURCES

Though a particular supplier is able to meet the requirements of a business, it is always advisable to find and maintain contact with additional suppliers. This will be of help if the main supplier fails to meet supply needs.

Quality

Quality is how well the product will stand up to its intended use – its ability to meet the requirements of a customer.

In a buying decision, price is not the only aspect to be considered. Besides price, quality is an important factor. The quality of the raw material will often determine the quality of the finished product, which, in turn, will determine customer satisfaction.

Generally, quality and price are directly correlated, *i.e.* the price of a product would vary with the quality of the product – lower if quality is poor and higher if quality is good. It is important to ensure that customers would be willing to pay a higher price for better quality.

Price

Price depends on the following factors:

- Quantity purchased.
- Payment terms.
- Quality.

QUANTITY PURCHASED AND PRICE

The price of a product depends on the quantity purchased. The more we buy, the more the profit to the supplier. Hence he may be interested in parting with a portion of his profit if he can sell larger volumes. This is called quantity discount.

An illustration may be introduced to explain how it may be more profitable to offer a discount for immediate payment than extending credit and charging interest for the credit period. The illustration should highlight:

- Normally the profit margin is higher than the rate of interest.
- Opportunity to turn round the money many times within the credit period earning the profit margin in each rotation.

Price also depends on the payment terms. The price offered for immediate cash payment will be much lower than credit price. The reasons for lower price for cash payment are:

- Cash payment is safe, from the supplier's angle.
- The supplier has to pay interest on the money locked in extending credit.
- Normally, the profit generated in a business is more than the interest rate. Therefore, if immediate payment is received, the supplier will be able to reinvest the money in his business and earn more profit.

How much to buy?

Every time something is bought, it involves some expenses, such as transport, travelling expenses of the person who goes to buy the material etc. This is called cost of buying or buying cost. Therefore, buying small quantities often means incurring more buying costs. Buying costs can be minimized by purchasing larger quantities each time and keeping the surplus, if any, in stock. However, keeping goods in stock means incurring certain expenses, such as interest on money locked in stocks, losses due to deterioration of quality, spoilage, spillage etc. These expenses are called **carrying costs**. Therefore, how much to buy is a question of minimizing the total of buying and carrying costs.

Consider the following example:

A trader sells 1800 pineapples at Rs.10/- per piece in a month of 30 days. Buying cost is Rs.11.25 every time he buys a stock of pineapples. Experience shows that the average cost of carrying stocks works out to Rs.0.10 per pineapple bought.

The following table shows the cost of buying a stock of pineapples, their carrying costs and total costs when the quantity of pineapples purchased at a time varies.

Qty. purchased at a time	No of purchases in a month	Cost of buying every time (Rs.)	Cost of buying for the month (Rs.)	Carrying costs (0.10 per fruit) (Rs.)	Total cost (Rs.)
1800	1	11.25	11.25	180.00	191.25
900	2	11.25	22.50	90.00	112.50
600	3	11.25	33.75	60.00	93.75
450	4	11.25	45.00	45.00	90.00
360	5	11.25	56.25	36.00	92.25
300	6	11.25	67.50	30.00	97.55

From the table it is evident that the most appropriate quantity to buy is 450 pineapples, when total cost is the least, i.e. Rs.90.

Note, however, that purchasing and stocking decisions should not be taken merely on consideration of cost savings alone. More important aspects, like demand, shelf-life of the products, (how long the product can be stored without it getting spoilt), storage space, possibility of business coming to a stop due to nonavailability of stocks, etc., should also be kept in mind.

When to buy

This depends on the minimum stock required to be maintained and the time taken to replace the material used.

Continuing the pineapple example, let us *assume it takes two days to get the material from the date of placing the order*. So at least two days' requirement should be in stock.

Daily sale = $1800/30 = 60$ pineapples

Minimum quantity required to be maintained in stock = 2 days' sale = 120 units.

Sale of the product during delivery period = $2 \times 60 = 120$ units.

Therefore, the trader should place an order whenever the stock level is 240 units. This level of stock is called the re-order level. If the trader places the order at this level it will take care of the sale during the delivery period as well as the minimum stock required.

Though concepts of economics in buying and stocking have been introduced to make the consultant aware of such tools, the practical problems of great distances, poor communication facilities, and transport problems may be crucial to a microenterprise. Under these conditions, the uninterrupted conduct of business is a more important consideration than advantages in purchasing.

Collective buying

Microenterprises are, generally, likely to be in a weak bargaining position due to their limited resources and size of operations. They can overcome this disadvantage by organizing themselves and buying collectively. Collective buying will help in negotiating better prices and payment terms.

For example, vegetable vendors in Indian towns and cities face difficulty in transporting their goods from the main markets to their shops. Due to the small quantities involved, they cannot afford to hire private transport and, therefore, depend on local bus transport. The bus operator.v know the vulnerability of the vendors and often cheat them. Vegetable vendors have, therefore, started hiring small motor vans collectively. This enables them to have

reliable and trouble-free transport for their purchases to their doorsteps.

Such co-operation may be extended to pooling their money to buy vegetables collectively, so that they get a better price (due to volume buying) as well as better terms of payment.

The consultant could play a catalytic role in organizing and motivating small businessmen in evolving such innovative ideas for their benefit.

For example, an outboard motor mechanic in a fishing village may not be able to afford to keep a stock of spare parts as the need for them may be irregular. Yet, the parts are available only in cities and towns that are far away. If a motor breaks down and spare parts are not available, the boat will be out of service and

the fishermen will lose their income. The consultant, in this instance, could persuade the local fishermen's cooperative, if any, to keep a stock of crucial spare parts. The mechanic could buy the parts readily from these cooperatives whenever a need arises. The cooperatives could add a small margin for their costs. Thus, everyone would gain.

THINGS TO REMEMBER

- Goods pass through a distribution chain before they reach the customer. The prices will be lowest at the primary source (place or production) and highest at the retail shop. But a retailer may not be able to buy at the primary source for these reasons:
 - Goods will not be sold in small quantities at the primary source.
 - It may not be economical to transport small quantities from the primary source.
- If the supplier is not reliable, the business will be affected and customers will be dissatisfied.
- It is advisable to have two or three suppliers for the smooth running of the business and to get better prices, payment terms and service.
- In a buying decision, price alone is not the consideration. Quality is an important aspect. Good quality will ensure customer satisfaction. However, customers should be willing to pay a higher price for better quality.
- Price depends on quality, quantity purchased and payment terms.
- If the number of times purchases are made during a certain period are many, buying expenses will increase but the expenses incurred on carrying stock will decrease. If the number of times purchases are made is few, buying expenses will be less, but stocking expenses will be more. The optimum number of purchases is when the total expenses (buying + stocking) are the least.
- When to buy (re-order level) depends on the minimum stock required to be maintained and the time it will take to replenish the stock.
- Purchasing decisions should be taken based not merely on economics but considering practical problems likely to be faced by microenterprises, such as great distances, and poor transport and communication facilities.
- Collective buying can improve the bargaining power of microenterprises.

Stocking

9

What are we going to look at in this chapter9

- What is meant by stocking
- Need for maintaining stock
- Consequences of inadequate stocking and overstocking.
- Estimation of optimum stock.
- Proper storing

What is 'stocking'?

Stocking may be defined as ensuring availability of raw materials, consumables and finished goods of the right kind in adequate quantities in order to meet the business requirements of production or sale,

Divide the participants into two groups. Let the two groups separately discuss the need for stocking and how to decide on how much

Stocking **ensures** the smooth and uninterrupted running of a business.

to stock. Then get them to present their views.

Need for maintaining stocks

- The source of supply may be far away from the place of business.
- If the material is 'made-to-order', it may take time to produce.
- Trading involves buying goods in large quantities and selling small quantities, as the individual requirements of customers are likely to be small, *e.g. bolts and nuts may be sold by wholesalers by weight, while they may be required only in small numbers by actual consumers.*
- The material is always in short supply or the availability of the material is seasonal.

How much to stock

We now know that stocking is essential for the smooth running of your business. But the question is how much to stock.

If the quantity stocked is inadequate, there will be not enough goods or raw materials available to sell and make the profit

necessary. On the other hand, if the stocks maintained are very large, then a lot of money may be locked up unproductively. In both instances, the business could lose.

Stock-out

Stock-out is a situation where there are no goods to sell or no material to carry on the production activity. This is caused by insufficient stocks. The stock-out situation results in loss of business, defaults in delivery commitments and customer dissatisfaction.



Overstocking

Overstocking is keeping substantially larger stocks than required. This results in money being unnecessarily locked up in stocks. The interest on the money so locked up eats away the profit. Money has a cost, even if it is not borrowed, as it will earn interest if it is invested elsewhere. Besides interest, overstocking may result in a product becoming outdated. There may also be losses due to spoilage, leakage and thefts.



Optimum stock is the ideal level of stocking at which the business will run smoothly, without interruption, and, at the same time, involve only the absolutely minimum amount of money necessary being locked up in stocks.

Optimum stock level depends on the following factors:

- The rate of consumption or sale.
- The time required to replace the material consumed.
- Perishability of the goods.

Illustration

Rukmini has a grocery shop in her village. Her experience shows that the average sale of a particular brand of beedis is ten bundles a day. The delivery man visits the village once in a week. At times he takes even ten days. She wants to know what is the optimum stock of beedis she should hold.

Daily consumption — 10 bundles
Replacement period — 7 days

	Bundles
Sales during replacement period	
10 bundles x 7 days	70
Add for safety: 10 bundles x 3 days (since experience shows he may take even ten days)	30
Optimum stock	100

Storage

It is very important to ensure that stocks are stored properly. Good storage helps in:

- Readily locating the material in stock when required.
- Minimizing the loss due to spoilage in the case of perishables, spillage in other cases.
- Preventing and detecting thefts.
- Giving an impression of neatness and order.

NEATLY STORED



DISORGANIZED



THINGS TO REMEMBER

- Stocking ensures smooth running of a business.
- Inadequate stocking results in customer dissatisfaction and loss of business.
- Overstocking causes erosion of profits due to interest cost. It also results in goods getting spoilt, losses due to leakage, spillage etc.
- Optimum stocking depends on the rate at which the goods are sold or consumed and the time taken to replenish the goods.
- Good storage is essential to store the goods with ease, and prevent loss due to spillage, leakage and thefts. Further, it gives a business an impression of neatness and order.

DEMAND & SUPPLY



↑ MORE DEMAND
HIGHER PRICE ↑



↓ LESS DEMAND
LOWER PRICE ↓



↑ MORE SUPPLY
LESS PRICE ↓



↓ LESS SUPPLY
MORE PRICE ↑

Pricing

10

What are we going to look at in this chapter?

- What pricing is.
- Factors that affect pricing.
 - Demand and supply.
 - Perishability of the product.
 - Seasonal factors.
 - Volume of sales.
- Elements of price.

What is 'pricing'?

Pricing refers to setting a 'cash' value, or price, on any product or service.

Pricing is a crucial decision in any business activity, because if it is not done properly, or elements of costs, like overheads, are ignored, then the business could be at risk with wrong pricing, there could be a mistaken impression that the entrepreneur is making profits whereas, in actuality, he would be incurring losses.

Factors that affect pricing

Several factors affect pricing, such as:

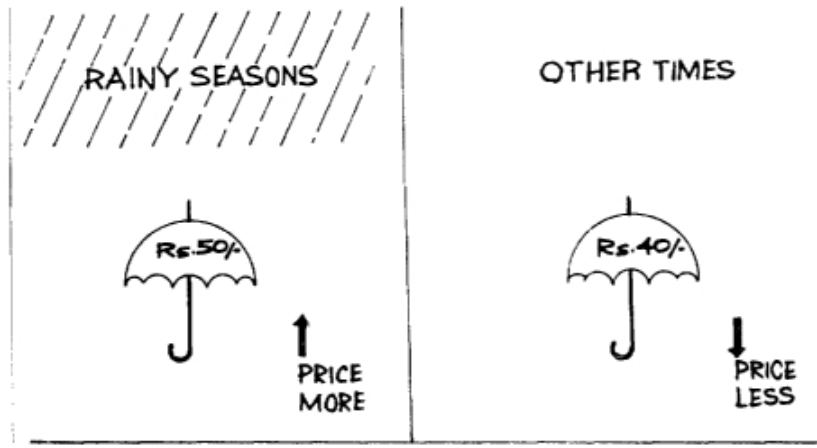
- Demand and supply.
- Nature of the product.
- Seasonal factors.
- Volume of sales.
- Terms of payment cash / credit.
- Cost of goods.

Let us consider them in detail

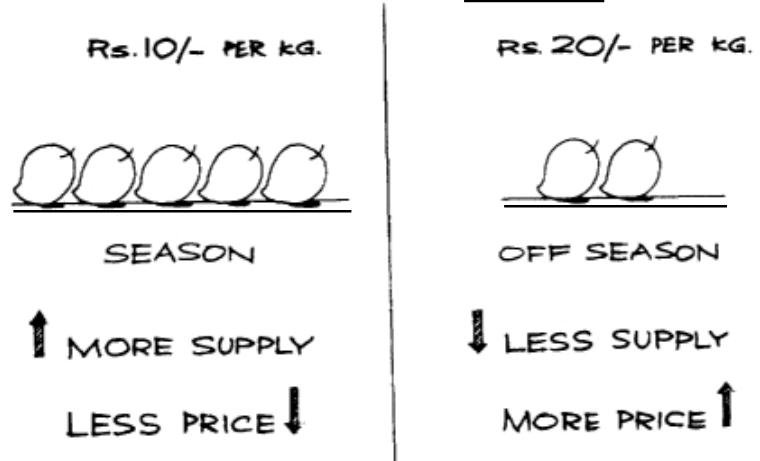
Demand and supply

The major factors affecting the price of a product are the demand and supply for it. **Demand** is the requirements or needs or wants of the people. Supply means the availability of the product or service. A fundamental rule of price behaviour is that, as the **demand for a product goes up, the price also goes up**. As **supply of the product increases in the market the price reduces**.

SEASONAL DEMAND



SEASONAL SUPPLY



By nature of the product we mean whether it is **perishable** (like fresh fish, fruits & vegetables) or **durable** like cloth or utensils.

Perishable products have very short shelf-life and have to be sold within that period, even at a lesser price, in order to minimize losses. If not, this will result in a total loss. This is not so in the case of durables. With durables, the seller only has to incur the additional carrying cost. This cost should be duly reflected in the price fixed.

A simple illustration to quantify the loss in the case of perishables and carrying cost in the case of durables may be introduced in a discussion.

Seasonal factors

Certain products are seasonal and are available in plenty during their season. Hence the price tends to be higher at the beginning and end of the season and lower during the peak of the season e.g. Seerfish.

Volume of sales

Volume of sales will also affect price. The higher the volume, the lower the price per unit. The reason is that, though the price and, consequently, the profit per unit is lower, the total amount of profit earned will be higher when the numbers sold are more.

Illustration

Sita is a fruit vendor. She purchases mangoes at Rs.24/- a dozen. If she sells the mangoes at Rs.30/- a dozen she can sell ten dozens. If she sells at Rs.29/- a dozen, she can sell 15 dozens. The results will be as follows:

Selling price (Rs.)	Profit per dozen (Rs.)	Sale qtv. (dozen)	Total profit (Rs.)
30	6	10	60
29	5	15	75

Raise the issue for discussion. Whether an entrepreneur should
- sell less at a higher price

or
- sell more at a lower price

This example illustrates that, under certain circumstances, selling larger volumes enables a product to be offered at a lower price, yet the seller's total profit is increased.

Elements of price

The price charged should cover — the cost of the goods, — the seller's fixed expenses, and — a reasonable profit.

These are the elements **of price**.

Let us examine the various elements in detail.

Cost of goods or 'direct cost'

The cost of goods should include the price the goods were bought at, local taxes levied, if any, and cost of freight incurred to transport the goods from the source to your place of business. If the freight is incurred on more than one type of goods, it should be spread over the different purchases. The cost arrived at by this method is also called, cost **of purchases** or **direct cost**. It is also called **variable** cost or **variable expense** as it varies, or changes, in direct proportion to the volume of business.

Illustration

Manikkam, a vegetable vendor, purchased 25 kg of potatoes at 5 Rs/kg and 20 kg of tomatoes at 7 Rs/kg and 20 kg of brinjal at 4 Rs/kg. He incurred a cost of Rs.15/- for transporting the vegetables from the market to his shop.

Let us compute the direct cost for each type of vegetable for the purpose of pricing.

Since Manikkam is going to sell all three types of vegetables by weight, let us adopt weight as the basis for distributing the transport cost.

Total freight incurred	-	Rs.15
Total weight of vegetables	-	65 kgs.
Cost of transport incurred per kg of vegetable	-	$\frac{15}{65} = \text{Rs.}0.23$

The direct cost per kg of vegetables would then be as follows:

	Potatoes	Tomatoes (Rs./kg)	Brinjal
Purchase price	5.00	7.00	4.00
Transport	0.23	0.23	0.23
Cost of goods or Direct cost	5.23	7.23	4.23

This is simple, because the case we have taken is a trading enterprise. Ascertaining direct cost in the case of a manufacturing or service enterprise is slightly more complicated.

Direct cost in the case of a manufacturing enterprise

In a production or manufacturing enterprise, the direct cost includes the cost of materials and labour and other expenses which can be directly identified or related to the activity of the enterprise.

Sagaya Mary is a basket-maker. She requires 1',kg of palm leaves to make one basket. She also requires 1 kg of pigment, at 10 Rs/kg to paint 100 baskets. She employs three persons to weave

baskets and pays Rs. 2.50 for weaving one basket. Sagaya Mary purchased 100 kg of palm leaves and one kg of pigment in the market and incurred a cost of Rs. 10 to transport them to her shed. Compute the direct cost of making one basket.

Since pigment is insignificant in weight and value compared to palm leaf, the cost of transport of pigment is ignored.

Total weight of palm leaf	100 kg		
Total freight incurred		Rs. 10	
		10	
Freight per kg of palm leaf	=		= Rs. 0.10
		100	

Cost of material per kg

	Price Rs.	Freight Rs.	Total Rs.
Palm leaf per kg	2.00	0.10	2.10
Pigment per kg	10.00	—	10.00

Direct cost of production of basket

item	Qty. Kg.	Rate Rs.	Value Rs.
Palm leaf	1.5	2.10	3.15
Pigment	0.01	10.00	0.10
Cost of materials			3.25
Labour			2.50
Direct cost per basket			5.75

DIRECT COST IN THE CASE OF A SERVICE ENTERPRISE

Raman is a fisherman who also owns a vulcanizing shop. The shop is looked after by his brother-in-law Krishnan, to whom Raman pays a monthly salary of Rs.600/-. In Raman's experience, the shop fixes about twenty punctures a day. The shop works for 25 days in a month. Cost of material required to fix one puncture is Rs.1.50. Raman wants to know the direct cost involved in fixing a puncture so as to fix a correct price.

Average number of punctures fixed/day	20
Average number of working days/month	25
Average number of punctures fixed/month (20x25)	500
Salary paid to Krishnan for a month	Rs.600

Average cost of labour for fixing a puncture =

$$\text{Rs. } \frac{600}{500} = \text{Rs.1.20}$$

	Rs.
Cost of material	1.50
Cost of labour	1.20
Direct cost	2.70

Fixed expenses

Besides direct costs, an enterprise also incurs certain **fixed expenses** or **overheads**, like rent, electricity, salaries (other than piece rate wages) etc. These expenses are termed fixed because they have to be necessarily incurred, irrespective of the volume of business. They have the following typical characteristics:

- They do not vary with the volume of business.
- They cannot be directly identified or related to a unit of product or service of the enterprise.
- They are generally related to a specific period and are, hence, also called **period** costs.

It is essential that the price should not only cover the direct costs but should be sufficient to recover the indirect expenses or overheads.

The subject of variable and fixed expenses is further discussed in Chapter 16, 'Break even analysis'.

Profit

Profit is the difference between the sale price and the cost of goods. Profit can be classified as:

- gross profit; and
- net profit.

GROSS PROFIT

The difference between the sale price and the direct cost is called the **mark-up** or **margin**. The mark-up multiplied by the quantity sold yields the gross profit or **contribution**. The mark-up is generally determined by market conditions.

NET PROFIT

Net profit is the difference between the value of sales and total cost (direct cost plus overheads). This is also the balance remaining after deducting the overheads from the gross profit or contribution.

Illustration

Mumtaz bought 100 kg of potatoes at 5 Rs/kg, 50 kgs of tomatoes at 6 Rs/kg, 40 kgs of brinjal at 4 Rs/kg. She sold them at 6, 7 and 5 Rs/kg respectively. Let us compute the mark-ups, gross profit or contribution for each of the products.

	Potatoes	Tomatoes	Brinjal
1. Quantity (kg)	100	50	40
2. Cost (Rs.)	5.00	6.00	4.00
3. Selling price (Rs.)	6.00	7.00	5.00
4. Mark up (Rs.)	1.00	1.00	1.00
- as % of cost	20%	16.67%	25%
Gross profit (1 x 4) in Rs.	100.00	50.00	40.00

Illustration

Vinod owns a fish shop. He normally sells about 500 kg of fish in a month. The present purchase price of fish is 15 Rs/kg. He employs a shop assistant on a salary of 350 Rs/month. He also pays a shop rent of 300 Rs/month. Electricity charges are 30 Rs/month. What price should Vinod sell his fish if he wants to make a net profit of 1000 Rs/month?

FIXED EXPENSES

	Rs.	Rs.
Salary	350	
Rent	300	
Electricity	30	
		680
Net profit required		1000
Gross profit required		1680

$$\text{Mark-up} = \frac{\text{Gross profit}}{\text{Sale quantity}} = \frac{1680.00}{500} = 3.36 \text{ Rs/kg}$$

$$\text{Sale Price} = \text{Direct cost} + \text{Mark-up} = \text{Rs.15.00} + \text{Rs.3.36} = \text{Rs.18.36}$$

EXERCISE

Nagamma has decided to set up a vegetable shop in a little village where there are about 120 families. Since there are no shops nearby, she guesses it will be a profitable thing to do.

She has decided to sell the following vegetables:

Potatoes. Tomatoes, Cabbage, Lady's fingers. Ginger, Onions. Greens, Chillies

She has made enquiries and identified a shop where she can make purchases at a good price. She has decided that her selling price should be cost + a margin of, say, 30% for the main vegetables and 100% for the smaller items (ginger, greens and chillies). She has also decided to round off the selling price for the sake of conveniently measuring out smaller quantities.

During one week, she bought the following vegetables at the rates indicated against them:

<i>Vegetable</i>	<i>Unit</i>	<i>Cost Rs</i>	<i>Margin %</i>	<i>Selling price</i>
Potatoes	Kg	3.00		
Tomatoes	Kg	4.00		
Cabbage	Kg	2.50		
Lady's fingers	Kg	3.00		
Onions	Kg	2.50		
Ginger	piece	0.25		
Greens	Bunch	0.50		
Chillies	heap	0.25		

She has to pay a rent of Rs.50 per week and, on an average, for a week incurs Rs.50 as transportation and conveyance charges.

Work out the selling price of each of the above vegetables.

During another week, she bought the following:

<i>Vegetable</i>	<i>Qty. Kg.</i>	<i>Rate Rs.</i>	<i>Cost in Rs.</i>	<i>Sale value Rs.</i>
Potatoes	20	3.00	60	
Tomatoes	10	4.00	40	
Cabbage	6	2.50	15	
Lady's fingers	30	2.50	75	

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- 1) What should her total sales value be in order to recover her over-head costs of Rs.100 for the week.
- 2) What is her element of profit at this level?
- 3) Fix the sale price of each vegetable in order that she is able to recover her fixed costs of Rs.100 plus a profit of Rs.90 per week.

ACTIVITY

Rama Rao has a cycle repair shop in Chalapet, a fishing hamlet on the Andhra coast. He has been running this shop for the past three years and caters to about 200 cyclists in and around his village. Rao's shop has an excellent reputation and his customers are normally satisfied with his service. His customers normally do not complain about the charge that he asks.

Rao has his little shop near the main bazaar in the village and has two persons helping him. He has a large trunk in which he keeps his tools and materials. Rao renders the following services:

Filling air
Overhauling

Mending punctures
Minor repairs

Rao charges his customers more or less fixed prices, but gives a small discount to his 'old' (regular) customers.

One day, when the consultant visited him, she found him rather agitated. He came up to her and said 'Do you know Babu who used to work here?' He has left me and started his own cycle repair shop in the next lane. What do I do now? Of course, my regular customers are still coming to me, but I am still worried. Moreover, his charges are cheaper. Should I reduce my rates? Please advise me".

What would your advice be?

Discuss this case with respect to pricing, considering the following aspects:

Should Rao reduce his rates?

Should his rates be linked to Babu's rates?

Flexible pricing may also be introduced as a concept. Discuss the Entry Pricing strategy adopted by Babu, under what circumstances it will succeed etc.

CASE STUDY

Farhana is an enterprising person who is, today, the proud owner of a grocery shop in a town. Over the years she has managed to expand her business and, today, supplies to the hotel, revenue office and the cooperative bank in the town, besides, of course, the townsfolk. But a major share of her sales is to the P.W.D. travellers' bungalow which is a busy little place.

But Farhana was not a very happy woman when the consultant visited her. Their conversation ran as follows:

Farhana: I don't know what is wrong with my business. I keep selling and at good prices, but I am always out of cash.

Con: Credit is a normal feature in any business, provided you handle it carefully. You should probably be more careful in giving credit or, perhaps, you should keep a better record of your dues.

Farhana: That's really not my problem. None of my customers have defaulted till now. What I am surprised is how Sheru across the road, who supplies hardware to the same people I supply groceries to, doesn't seem to have this problem.

Con: Look here, Farhana, why don't you clearly identify your problem. Maybe we can do something about it.

Farhana went on to describe her problem:

Farhana: My problem is really the P.W.D. The travellers' bungalow accountant is unwilling to pay me cash and goes on extending the credit period. How do I tackle this?

(contd.)

(contd. from previous page)

Con: Have you approached the accountant in the P.W.D. office and discussed your problem? What exactly did you tell him?

Farhana: Of course, I did. I have told him several times to give me cash on delivery or, at least, pay me on the due date. But he only asks me to come back at a later date,

Con: Why don't we discuss it with him again tomorrow morning. Maybe he has not really understood your problem. Be sure to bring the details of how much he owes you.

The next morning Farhana goes to the P.W.D. office and the consultant accompanies her.

The conversation at the P.W.D. office ran as follows:

Farhana: Good morning, Mishraji. I have come to discuss with you the amounts that your department owes me and that too for a very long time.

Accountant: As long as you want to discuss it, I do not mind. But please do not ask me to pay you any amount this week. By the way, who is this person?

Farhana: This is Ms. Kumar. She is a friend of mine and helps me out with my business sometimes.

After the introductions are over. Farhana earnestly returns to the problem at hand.

Con: We are finding it increasingly difficult to supply you items for which you are not paying us cash. We cannot say the same to our supplier, who demands his payment in advance.

Accountant: I feel sorry for you. But considering the Government's position today, I have been instructed to make payments only after they have been specifically approved by my head office. Each time I forward your bills, he says he will pay it the next time. There is not much that I can do.

Farhana: But Sheru seems to be getting his dues on time!
(excitedly)

Accountant: Sheru agrees to give us a prompt payment discount up to 2% of the value of the bill. This is good enough for my officer to recommend immediate payment, since he would be able to explain that there has been some savings. I have, in fact, mentioned this to you.

Con: Why don't you, please, tell us what exactly we should do and we will consider whether we can do it.

The accountant explains the procedure. Farhana and the consultant go out and discuss the accountant's suggestion for a few minutes. When they return, Farhana promises to give him a letter offering to give a discount of 2% for immediate payment.

Farhana and the consultant leave the office. Outside, Farhana says. "Thank you, Ms. Kumar. You have really done me a great service".

This case will highlight flexible pricing.

Discount for prompt payment Why?

Cash inflow: Importance of cash today rather than tomorrow.

Cash is lifeblood of business.

Incidentally, also talk about discounts for large volume purchase:

Turnover discount: Why should we do this?

Larger turnover with one customer less time-consuming.

THINGS TO REMEMBER

- Pricing is assigning a monetary (cash) value, or price, to a product or service.
 - Pricing is a crucial function, as it affects:
 - Survival of the business in a competitive environment; and
 - Profits and growth
 - In a free economy, control over price is generally not in the hands of the business. It is determined by the demand and supply position.
 - More demand: higher price:
 - Less demand: lower price
 - More supply: lower price:
 - Less supply: higher price
 - Price should cover not only the direct cost. or expense. hut also the indirect, or fixed expense, as well, besides including a reasonable profit to the owner.
-

Selling

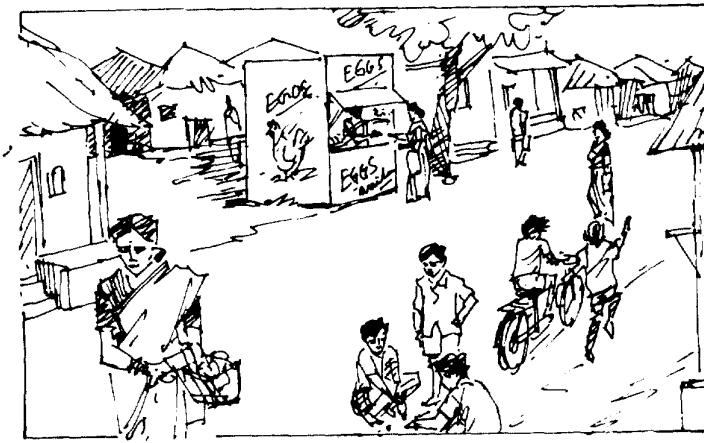
11

What are we going to look at in this chapter?

- Features of selling
- Rules for successful selling
- Attributes of a successful salesperson.

What are the special features of 'selling'?

You must know **the customer** and choose the **right location**.



The vendor knows the housewife is the person who decides on buying eggs. He knows that her childrens nutrition is a concern to her

Who will the mother buy eggs from?



Pleasant-looking, clean people attract customers. **Attractive display** of products increases sales.



Small things sold along with the main product make the product easier to sell.

People do come to a shop with a 'plan' to purchase an item — **planned purchase**. However, at the shop, they change their mind, depending on what they find there and make an **impulse purchase**.



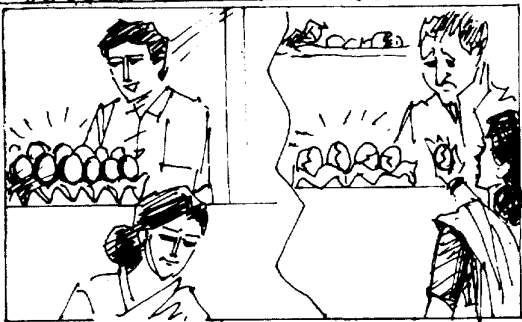
A **discount** in price can help this vendor sell his eggs faster. The discount is used to sell the products before they spoil, because after they spoil they will have no value.

A discount, or an incentive, can also be offered to people to make them try a new product.

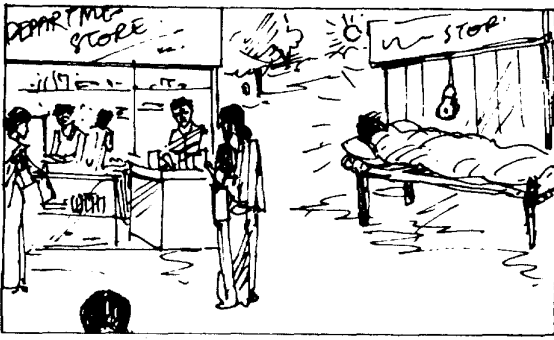


The vendor has built up the **confidence** of his customer with

- immediate service, and
- honesty: she trusts him because she knows he will not cheat her



Products should be of **good quality**.



The service should be prompt.

Rules for successful selling

Greet the customer courteously.

Ask questions, rather than recite facts.

Show the product and explain its features.

- Help the customer to come to a decision at his/her own speed.
- Allow the customer to say 'no' without disagreeing, if this is in the customer's best interest.
- Expect and welcome objections.

Answer questions and objections carefully and truthfully.

Understand each customer's wants.

A successful salesman NEVER

argues. The argument may be won, but the sale is lost.

loses his **temper**. Losing your temper will always result in loss of sale.

makes exaggerated claims. The truth will eventually come out.

forces the product on a customer.

- **interrupts the customer**.

shows disrespect to the customer, in the way s/he dresses, talks, looks etc.

- **allows credit** beyond the customer's ability to pay.

encourages more purchases than what the customer needs or can afford.

ACT! VITY

Divide the participants into three teams.

Team 1 to set up a tea shop

Team 2 to sell 25 tender and 25 mature coconuts produced in the farm.

Team 3 to sell a tailoring service.

Each team to work on

- to whom they would sell;
- what they would sell;
- where they would sell;
- how they would sell; and
- what the additional areas would be that they would take care of and how they would do it.

THINGS TO REMEMBER

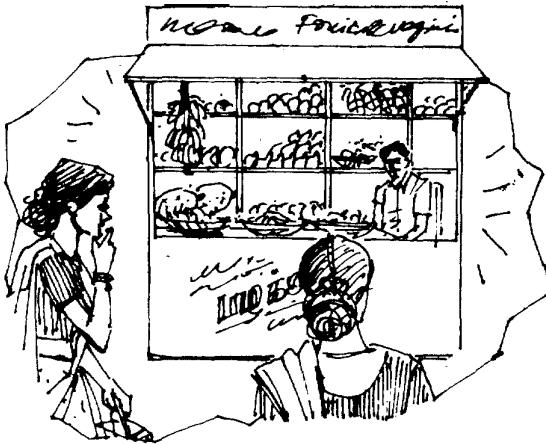
- To sell effectively you must know to whom you are going to sell.

You should sell to the person likely to use the product.

- What are you selling?

What is the need/requirement being met by your product?
What are the benefits of buying your product?

- Where should you sell? Where is your product most likely to be bought'?
- The person selling should be clean and pleasant. Cleanliness makes products attractive.
- The products/wares should be well-displayed and you should be able to explain what is special about them. Attractive displays attract the attention of customers and create a desire to buy.



- Products should be of good quality.
- Signboards attract customers: use them wherever possible,
- Products/Services should be made available on time. Service should also be prompt.
- Small items sold along with main items help to attract customers.
- The customer should be confident that you will never cheat him/her. You should win his/her trust,
- Discount sales help to clear old stock.
- Discounts/incentives help to make customers try your product.

Distribution

12

What are we going to look at in this chapter?

- The need for a distribution system
- The process by which the product reaches the buyers.
- The people involved in this process *i.e.* middlemen and their role.

What is 'distribution'?

The process by which the product reaches the consumer is called distribution. This can be seen clearly in the illustrated sequence alongside:

The important people in the distribution system are

Producers.

Middlemen - there could be several of them, depending on how far the consumer is from the place of production.

Retailers

The function of the distribution system is to **transport and store** the products till it reaches the consumer.

Ideally, a farmer growing grain should sell directly to the retailer. His grain will not have to pass through the hands of several middlemen and, thereby, he will be able to get a much better price.

Then why is there a distribution system?

D I S T R I B U T I O N



FARMER HARVESTING CROP

CROP BEING TAKEN
TO LOCAL MARKETS

BEING BOUGHT AND STORED BY
GRAIN MERCHANTS IN GODOWN

WHOLESALE FROM
VARIOUS PARTS OF THE
BUY FROM
THE GRAIN MERCHANTS.

TO THE RETAILER GODOWN

TRANSPORTING THEM
TO RETAILERS
AS AND
WHEN NECESSARY.

CUSTOMER BUYING FROM RETAILER
AT LOCAL SHOP.

The costs involved in **transportation and storage of** the produce till it reaches the consumer would be too high for the farmer to bear.

He will waste a lot of time which he would be otherwise able to use in producing more his area of expertise.

He may not be able to reach the buyer easily at the right time and the right place.

How does the distribution system reduce the costs, involved in reaching the consumer?

The middlemen make it possible for the system to work because they handle larger quantities.

They also have the money required to buy from many farmers, invest in a godown to store all their purchases and bear the transportation expenses. They also know where to sell the produce.

The middleman therefore leaves the farmer to concentrate on producing while he takes care of the rest.

ACTIVITY (Discussion Guide)

Initiate discussion on:

Select some examples for each:

- **Whether participants think middlemen and the distribution system are necessary for all products.**
- **When and for what products it would be necessary.**
- **When and for what products it would not be necessary.**

Guide discussion to highlight when middlemen are needed:

Middlemen necessary

Small quantity produced and market is far away.

Large quantity produced, but market is difficult to reach,

When money is required quickly to meet working expenses.

Middlemen not necessary

Small quantity produced and likely to be locally consumed.

Large quantity produced and market is not too far — provided transportation is available to reach the market in time and return at regular intervals.

Producer capable of investing in stocks and has enough for operating expenses.

What are the characteristics of a good middleman?

To BE HIGHLIGHTED: A good middleman would

- **Be a local person of good financial standing;**

- Be willing to hold stock (would be equipped to do so);
- Create a steady demand for the product;
- Be a good communicator (communicating the needs of the market to the producer and helping him to produce what the market needs); and
- Be able to take on the risks of a small-scale manufacturer! entrepreneur.

Ask for examples of how good middlemen have, in their experience of the participants, helped enterprises.

Who is a bad middleman?

TO BE HIGHLIGHTED: A bad middleman is one who

- Exploits the producer;
- Will not give a steady return to the producer;
- Will try to reduce the prices; and
- Has no interests in the welfare of the producer as he is not a local person. (As his roots are elsewhere, what happens locally does not bother him.)

Is it possible for you, as a consultant who advises the community, to help set up/find middlemen who could help the microenterprise entrepreneur. How would you do it?

TO BE HIGHLIGHTED: The way it could be done is by:

- Identifying the market for the product.
- Tracing the distribution system for the product.
- Finding persons of reasonable financial standing who would be able to communicate with the producers and the market.
- Negotiating and setting up the distribution system.

THINGS TO REMEMBER

- Ideally a producer should get the best (highest) price for his product from the buyer.
- However, in most cases, it is difficult for the producer to sell his product to the buyer because
 - He is far from the buyer.
 - He does not know when and where the buyer is.
 - He needs money immediately for his production.
- It is therefore better to use a middleman who has:
 - Enough money to invest in the products;
 - Storage facilities to store for a period of time; and
 - Transportation facilities to reach the consumer.
- Middlemen therefore are a must when:
 - A small quantity is produced and the market is far away.
 - Large quantities are produced, but the market cannot be reached easily.
 - When money is required quickly to meet expenses.
 - When storage and transportation will eat into the producer's time for production.
- A good middleman is:
 - A local man who is financially sound.
 - A businessman concerned about the producer.
 - A person who will help the producer produce what the market needs.
- A bad middleman will exploit the producer and will not give him a steady return
- Before helping find a middleman
 - study the market for the product;
 - trace the distribution system; and
 - find persons of financially sound backgrounds who will be able to communicate with the producers and the market.

What are we going to look at in this chapter?

- What accounting is.
- Three fundamental accounts statements

Balance Sheet

Profit & Loss Account

Cash Flow Statement

What is 'accounting'?

Accounting is recording and summarizing the financial (monetary) transactions of a business. The purpose of accounting is to measure the financial results of a business and to help the owner to take the right business decisions.

illustration

Revathi, a fisherv.'oman, has nevi'lv started a textile cut-piece' shop in her village. She has been doing good business for a month and is eager to know the fruits of her efforts for that month. She approaches Mohan, the local NGO field worker, and asks him to help her out in the exercise. Mohan agrees.

In the beginning, Revathi is not clear about what exactly she wants to know, but as they work together they identify the following important questions Revathi would like an answer to on a regular basis:

- What does she own?
At any given point of time, how much does Revathi owe others and what do others owe her?
- Is Revathi making any profit for herself from her efforts?
- If she is making a profit, where is it?

Revathi has got only a very rough record of her transactions. Mohan asks Revathi to show him all the things she has bought for the shop from the time she started her business. She shows Mohan the following:

Wooden rack, unsold cloth, fan, bulbs, electrical wire, switches, etc.

The values for these are ascertained from the purchase bills.

Mohan then asks Revathi to tell him how much cash she has got.

She opens the small metal box in which she keeps the cash and counts Rs.260.

Mohan now asks her to figure out how much she has to collect from her customers. Revathi finds it very difficult to compute the figure readily, as she has not kept a proper record of her customers' accounts. However, after a long time, a figure of Rs. 1,200 is arrived at.

Now Mohan and Revathi list out what the shop owns on that date as follows:

WHAT THE BUSINESS OWNS

	Rs.
Unsold	
Wooden rack	750
cloth	1,450
Fan, bulbs, wire etc.	890
Cash in the box	260
Money doe from customers	1,200
TOTAL	4,550

Mohan asks Revathi to tell him how much money she has borrowed and how much she owes the textile shop in the town from which she buys the cloth. They draw up the following list:

WHAT THE BUSINESS OWES

	Rs.
Loan from local bank	1,000
Money doe to supplier of cloth	250
TOTAL	1,250

Mohan tells Revathi that if she were to close down her business at that moment, sell all its possessions and collect the money from her customers, she will get Rs.4,550. But she would have to repay the bank loan and the supplier, and for this Rs.1,250 would be needed. The remaining Rs.3,300, thus, belongs to Revathi.

Mohan explains to Revathi that the statement that lists what a business owes and what it owns on a particular day is called the **Balance Sheet** and that the Balance Sheet is the statement that answers her first question. It is one of the three fundamental accounting statements that help in measuring the performance of a business.

Revathi thinks about this, asks Mohan . “Does the Rs.3,300/- represent the profit I earned in the business?”

Mohan answers. “Not entirely” and asks. “How much money did you originally invest in the business?”

Revathi replies, “Rs. 2,000.”

Mohan explains to Revathi that the difference between what the business owns and what the business owes, Rs.3,300, belongs to Revathi. But this is not entirely earned by the business. This amount includes Rs.2,000 originally put into the business. The remaining Rs.1,300 is the amount earned by the business. This is how it is calculated:

	Rs.
What is owned by the business	4,550
Less: What is owed by the business	1,250
Wealth belonging to owner	3,300
Less: Originally invested by the owner	2,000
Profit earned by the business	1,300

Revathi is thrilled by the knowledge that her efforts have earned a profit of Rs.1,300 in a month.

However, she soon begins to think it over and tells Mohan that something is wrong with the figures. She explains to him that on every rupee of cloth she bought, she had added 25 paise and sold at Rs.1.25. As she had sold Rs.12,500 worth of cloth she should have made Rs.2,500 profit. “How is it I have ended up with only Rs. 1,300?”

On the other hand, she said, she had purchased cloth worth Rs.11,450 so far and had sold cloth for Rs.12,500. Her profit then should be the difference between the value of cloth purchased and that sold, *i.e.* $\text{Rs.12,500} - \text{Rs.11,450} = \text{Rs.1,050}$.

Mohan points out to Revathi that she had forgotten to deduct the expenses she had incurred in earning the profit of Rs.2,500. If she wanted to know in detail how she had earned the profit of Rs. 1,300, and not Rs.2,500, they should gather more information on the expenses incurred by the shop.

Regarding her notion of profit being the difference between the sale of cloth and purchase of cloth, she had made a small mistake, he said. She had forgotten the unsold cloth, the purchase price of which, by her own reckoning, was Rs.1,450. In order to compute the correct profit she should compare the value of cloth sold with the purchase value of cloth sold and NOT the value of ALL cloth purchased. To arrive at the purchase value of cloth sold, value of unsold cloth should be deducted from the value of cloth purchased.

He explains it to her in numbers in this fashion:

	Rs.
Value of cloth purchased	11,450
Less: Value of unsold cloth	1,450
Purchase value of cloth sold	10,000
Less: Cloth sold	12,500
PROFIT	2,500

This profit does not consider the expenses she has incurred. It is **called** the **Gross Profit**.

To find out how the Gross Profit became Rs. 1,300, they put together out the following information about her expenses:

	Rs.
Transport of cloth from town to shop	190
Shop rent	100
Shop electricity charges	20
Shop inauguration expenses	350
Other shop expenses	240
Revathi's salary	300
TOTAL	1,200

They then computed the profit as follows:

Basic (Gross) Profit	2500
Less: Expenses:	1200
PROFIT	1,300

The profit after expenses are deducted **from** Gross Profit is called **Net Profit**.

Mohan: You see, you indeed made a Gross Profit of Rs.2,500. but after meeting expenses, Rs.1,300 is remaining. This is the final or **Net Profit**.

This statement, which explains whether a business has made a profit or loss, and how, is known as the **Profit and Loss Account**. It is the second fundamental accounting statement which measures the profitability of a business.

Revathi: But where is my profit?

Mohan: To find an answer to this question we must prepare another statement called the **Cash Flow Statement**. This statement explains from what sources the shop got money and how the money was spent.

They list out the cash flows as follows:

SOURCES OF CASH:

Revathi's savings	2,000
Bank loan	1,000
Money due to supplier	250
Profit	1,300
TOTAL	4,550

How the cash was used

Purchase of rack	750
Fan, bulbs, wires etc.	890
In the form of unsold cloth	1450
To be collected from customers	1200
TOTAL	4,290
Balance (available in the cash box)	260
GRAND TOTAL	4550

Mohan: Your profit together with money from other sources has been spent by purchasing the rack and electrical fittings. The remaining is in the form of unsold cloth and dues from customers.

Revathi: Thank you very much. I seem to have a better picture of where I stand. I would like to know how I am doing from time to time, but this exercise appears to be quite difficult and time-consuming.

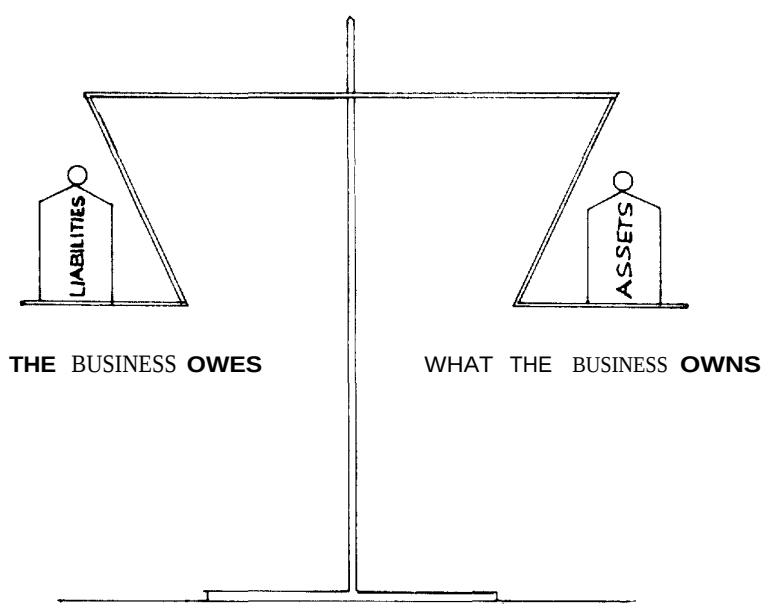
Mohan: Not at all. Provided you keep some basic records. I will one of these days teach you how to maintain these records. As for wanting to know how your business is faring, that is essential. Otherwise you may be losing money without knowing it and may, to overcome day-to-day problems, resort to frequent borrowings. Then one fine day, you will find you are buried in debts.

Fundamental accounting statements

We can see from this illustration that there are three fundamental accounting statements that measure the performance of a business and help the owner to take crucial business decisions. They are:

- **Balance Sheet:** A statement of what a business owes and what it owns, a statement of the wealth of the business.
- **Profit & Loss Account:** A statement which shows the profit of the business.
- **Cash Flow Statement:** A statement which explains from where the business raised money and how it was used.

BALANCE SHEET



ASSETS AND LIABILITIES **BALANCE** *EACH OTHER*

HENCE THE

This is a statement of what an enterprise owns and what it owes as on a particular date. What the enterprise owns is called its assets and what it owes is called its liabilities. The total of all liabilities, including the owner's own funds, should be equal to the total of all assets, *i.e.* they should balance each other. Hence the name **balance** sheet.

All capital transactions of a business will appear in the Balance Sheet. Refer to Appendix I for a discussion on capital and revenue transactions.

A few examples of assets and liabilities are:

<i>Assets</i>	<i>Liabilities</i>
Land	Credit taken (money you owe for supplies)
Car	Loans taken
Stock	Your investment, as owner
Credit given/money owed to you for supplies	

If assets are more than the 'outside liabilities' *i.e.* other than what is due to the owner, the surplus is the wealth of the enterprise. Thus, the Balance Sheet is the statement of wealth of the enterprise. This wealth belongs to the owner.

Extending the same logic, if the outside liabilities are more than the assets, then it represents the amount the owner would have to pay to the business and, therefore, the owner's debt to the business is shown as an asset in the balance sheet.

If a business is making profits, and the profits are retained in the business (*i.e.* not withdrawn by the owner), the profits will be reflected in the balance sheet as an increase of assets over outside liabilities. That is, the wealth has increased.

If the business is making losses, the wealth decreases.

EXERCISE

Given below is a list of items. Classify the items as Assets /Liabilities.

<i>Assets</i>	<i>Liabilities</i>
Land and building	
Bank loan	
Cycle	
Cash in hand	
Money due to suppliers	
Security deposit given	
Money due from customers	

EXERCISE

The following are the balance sheets of a business on two different dates. Find out if the business has made a profit or loss during the interim period and how much. The owner had drawn Rs.9,000 from the business as the premium for the money he has invested.

	Jan. 1, '92 Rs.	Dec. 31, '92 Rs.
Assets		
Shed	10,000	10,000
Stock	7,500	5,000
Due from customers	5,000	1,000
Cash on hand	250	450
	22,750	16,450
Liabilities		
Money invested by owner	10,000	2,000
Money due to suppliers	4,000	5,000
Loans	8,750	9,450
	22,750	16,450

Profit and Loss Account

A **Profit and Loss Account** is a statement which explains how the changes in the wealth of an enterprise have come about between two Balance Sheet dates. The period between these two dates is called the **accounting period**.

If income is more than expenses, then the enterprise has made a profit. Otherwise it has made a loss. If profit is made, the wealth will increase, otherwise it will decrease.

While the Balance Sheet is drawn up as of a particular day, the **Profit and Loss Account** is drawn up for the accounting period and reflects all the revenue transactions that have taken place during the accounting period. Refer to Appendix I for a detailed discussion of 'Capital and Revenue Transactions'.

Illustration

Prepare a Profit and Loss Account and Balance Sheet from this data:

	Rs.
Money invested in business by the owner	5,000
Purchases	12,000
Sales	18,000
Stock on hand at the end of the year	200
Expenses for the year (incl. salary)	4,700
Loan taken	5,000
Loan repaid	1,000
Money receivable from customers	900
Interest paid on loan	600
Payable to suppliers	750
Cash on hand	50
Profit already withdrawn	500
Cash at hand	

PROFIT & LOSS ACCOUNT

NOTES

<i>Expenses</i>		<i>Income</i>	
	Rs.		Rs.
Purchases	12,000	Sales	18,000
Less: Unsold stock	200		
	11,800		
Expenses	4,700		
Interest paid on loan	600		
Profit	900		
	18,000		18,000

BALANCE SHEET

<i>Liabilities</i>		<i>Assets</i>	
	Rs.		Rs.
Due to owner:			
Money invested	5,000	Stock on hand	200
		Due from customers	900
Add: Profit	900		
	5,900	Cash at bank	9,000
Less: Profit already withdrawn	500	Cash on hand	50
	5,400		
Loan taken	5,000		
Less: Repaid	1,000		
	4,000		
Due to suppliers	750		
	10,150		10,150

EXERCISE

Prepare a Profit & Loss Account and Balance Sheet with this data:

	Rs.
Sales	75,000
Purchases	50,000
Stock at the end of the year	1,500
Purchase of shop furniture	2,500
Shop rental advance given	1,000
Shop rent	1,200
Electricity charges	240
Owner's salary	12,000
Transport from market to shop	500
Money invested in business by owner	10,000
Diverse expenses	300
Profit already withdrawn	3,600
Payable to suppliers for purchases	1,400
Depreciation	250
Cash on hand	819
Cash at bank	12,000

Cash Flow Statement

A Cash Flow Statement is the third fundamental accounting statement. This explains how changes in the position of assets and liabilities have come about between Balance Sheets on two dates, other than by trading activities. That is. it explains the changes in wealth other than by trading activity.

All receipts and payments, other than those relating to the trade, are considered here. Trade-related transactions are excluded since they are already reflected in the Profit and Loss Account; only the net result of that statement, *i.e.* profit or loss, is considered here. It shows what the sources of cash were and how the cash was used.

Illustration

Consider the balance sheet of Shanrnukha, a sweets vendor, as on 31.3.91 and 31.3.92.

	31.3.91 Rs.	31.3.92 Rs.
Liabilities		
Capital	5,000	12,000
Loans	5,500	
Pending payments for purchases	3,000	4,000
TOTAL	13,500	16,000
 Assets		
Racks and table in shop	1,000	1,500
Money due from customers	3,500	2,800
Stock of sweets	1,500	1,600
Cash in bank	750	900
Loans given	6,500	6,900
Cash on hand	250	2,300
	13,500	16,000

The Profit and Loss Account for the year ended 31.3.1992 is as follows:

NOTES

	31.3.92
	Rs.
Income	
Sales	50,125
TOTAL	50,125
Expenses	
Purchases	37,500
Add: Stock at the beginning of the year	1,500
	39,000
Less: Stock at the close of the year	1,600
Cost of sweets sold	37,400
Rent	2,400
Shanmukha's salary	3,600
Other expenses	1,800
Profit	4,925
TOTAL	50,125

Additional **Information:** Shanmukha made additional investment of Rs.5,000/- during the year. He also drew Rs.2,925 as profit-to-owner.

CASH FLOW STATEMENT FOR THE YEAR ENDED 31.3.1992

	Rs.
Sources of cash	
Profit	4,925
Increase in creditors	1,000
Decrease in money due from customers	700
Money additionally invested by Shanmukha	5,000
TOTAL	11,625
	Rs.
How the cash was used	
Repayment of loan	5,500
Additional racks purchased	500
Increase in stocks	100
Additional loans given	400
Increase in bank balance	150
Increase in cash balance	2,050
Profit already drawn by Shanmukha	2,925
TOTAL	11,625

Wealth of the enterprise

	31.3.9/ Rs.	31.3.92 Rs.
Assets	13,500	16,000
Less: Outside liabilities (other than due to owner)	8,500	4,000
Wealth	5,000	12,000

Change in wealth between the two balance sheets is
Rs.12,000 - Rs.5,000 = Rs.7,000

Increase in wealth is explained as follows:

	Rs.	Rs.
Profits from trading	4,925	
Less: Profit withdrawn by Shanmukha	2,925	
		2,000
Additional money invested by Shanmukha		5,000
TOTAL		7,000

While long-term sources can be used both for long-term and short-term applications, short-term sources should not be used for **long-term puposes.**

Any asset intended and expected to be sold or realized in cash within a year is considered as short-term, *e.g stocks or money due from customers*. Any asset which is not intended to be sold and whose life extends beyond one year is defined as long-term *e.g. land, building, tools, etc.*

Similarly. any loan repayable within a year is short-term and one not repayable within a year is long-term.

A few examples of long-term and short-term sources and applications are:

SOURCES

	<i>term</i>
<i>Money iinvested by owner</i>	<i>Money due to suppliers</i>
<i>Profits from business</i>	<i>Loan repayable within a year</i>
<i>Loans with repayment period exceeding one year</i>	<i>Sale of stocks</i>
<i>Sale ot Fixed Assets like arid, building. etc.</i>	<i>Collections from customers</i>



<i>Long-term</i>	<i>Short-term</i>
Purchase of fixed assets	Repayment of short-term loans
Profits withdrawn	Stocks
Repayment of long-term loans	Credit given to customers
Shop rental advance	
Security deposit for electricity	

As will be explained in the chapter on ‘Working Capital’, it is dangerous to use working capital funds for purchasing long-term assets and repaying long-term liabilities. Such improper use of working capital leads to sickness of the business due to lack of cash to running it day-to-day.

Such misuse can be easily detected from the Cash Flow Statement if it is prepared in a slightly modified form.

CASH FLOW OF SHANMUKHA

	<i>Long-term Rs.</i>	<i>Short-term Rs.</i>
Sources of cash		
Profit	4,925	
Money additionally invested by Shanmukha	5,000	
Increase in purchase bills to be paid		1,000
Decrease in money receivable from customers		700
	9,925	1,700
Uses of cash		
	<i>Long—term Rs.</i>	<i>Short-term Rs.</i>
Repayment of loans (assuming long-term)	5,500	
Additional racks purchased	500	
Additional loan given (assuming long-term)	400	
Profits withdrawn	2,925	
Increase in stock		100
Increase in bank balance		150
Increase in cash balance		2,050
Surplus/(Shortage)	600	(600)
	9,925	1,700

The modified cash flow statement shows that Shanmukha has applied only long-term sources of cash for long-term uses leaving a surplus of Rs.600/-. This he has utilized to meet the shortage in short-term sources.

THINGS TO REMEMBER

- Accounting is measuring how the business is doing in financial terms. Accounting helps the owner to take the right business decisions.
- A Balance Sheet is a fundamental accounting statement that shows what a business owns and what it owes on a particular day *i.e.* it is a statement of wealth.
- A Profit and Loss Account is another fundamental accounting statement. This statement shows whether a business has made a profit or loss in a given period of time and how much the profit or loss is. It explains the change in wealth due to trading activities of the business between Balance Sheets on two different dates.
- A Cash Flow Statement is the third accounting statement and explains the change in wealth due to transactions other than those related to trading. It shows, besides profits, from where the business raised money and how this money was spent in a given period.
- It is essential for a business to find out where it stands and in what direction it is going by compiling these three statements at regular intervals. Otherwise the business may be making losses without the owner ever knowing it. Losses will not be apparent for quite some time, as money will be flowing into and out of the business, giving a healthy feeling, which is false. By the time it is found out that the business is making losses, it will be too late.

What are we going to look at in this chapter?

- What bookkeeping is.
- How bookkeeping helps a business.
- Basic records relevant to a microenterprise

Cash Book

— Ledger

- How these books are maintained.

What is 'bookkeeping'?

Bookkeeping is the maintaining of a record of business transactions.

How does bookkeeping help a business?

Bookkeeping helps in the preparation of fundamental accounting statements.

The owner will be able to find out at any time what he has to collect from a particular customer and what is owed to suppliers. This will help him to manage his cash flow better.

It is easy for the traders, middlemen and moneylenders to exploit fishermen and small business people as they know that these people do not keep any accounts. If small business people maintain accounts it will dissuade others from taking advantage of them.

In order to prepare the Profit and Loss Account and Balance Sheet, basic information on sales, purchases, expenses etc. are required. To ensure this information is readily available, a few records have to be maintained. Among them, the following are relevant to a microenterprise:

Cash Book

Ledger

Cash Book

The **Cash Book** records all cash transactions. It records the transactions in the order they take place. A simple Cash Book contains columns to enter the following information:

- Date of transaction.
- Name of account and description of the transaction.
- Cash receipts.
- Cash payments.

CASH BOOK

Date	Name of accounts & description	Receipts Rs.	Payments Rs.
Total			

Cash on hand, at the beginning of the year/day, is entered as a receipt. Similarly, the balance at the end of the day is entered in payments, so that total receipts and payments agree. This procedure is followed again on the next day.

The process of totalling up the receipts, payments, calculating the balance and taking it to the next period is called balancing. Balancing the cash book should, ideally, be done every day.

Ledger

A **Ledger** records all transactions relating to a particular person or account, *e.g. all the transactions of Beenu, a customer of the business, will be recorded in one place.* This helps in finding out, readily, how much the business owes to or has to get from a particular person, in this case Beenu.

A ledger has columns to record the following:

- Date of transactions
- Nature of transaction *e.g. cash, sale's, purchases. etc.*
- Amount due to business (Debit)
- Amount due by business (Credit)

LEDGER

Date Rs.	Nature of transaction & description	Debit Rs.	Credit Rs.
Total			

The amount due to or due by the business at the beginning of the period is entered in the respective columns. The frequency of a ledger being balanced depends on your requirements, but it should be balanced **at least once a month.**

For every business transaction, there are two accounts involved and entries will have to be made in two places.

Beenu receives Rs. 500 cash from Archana as a loan. This transaction can be broken down into two parts:

- Cash has been received; and
- The amount is owed to Archana by Beenu.

Therefore this transaction will be entered in two places:

- Cash book – entry in ‘Receipts’ column; and
- Ledger – entry in the Account of Archana in the ‘owed by us’ (credit) column,

CASH BOOK

<i>Date</i>	<i>Name of account & description</i>	<i>Receipts</i>	<i>Pavment.s</i>
	Archana (received loan)	500	00

LEDGER

Account of Archana

<i>Date</i>	<i>Name of account & description</i>	<i>Debit</i>	<i>Credit</i>
	Cash (received loan)		500 00

Rules of debit and credit

You would have observed that a transaction is recorded in two places. In one place, the amount is entered on the left hand side and in the other place on the right hand side. Thus, every transaction balances itself, *i.e.* the left is always equal to the right.

In the Cash Book, the left hand side is called Receipts and the right hand side is called **Payments**.

In the Ledger, the left hand side is called Debit and the right hand side Credit.

The rules of Debit and Credit are:

- If the account relates to tangible things, like furniture, machinery etc., the account should be debited (amount entered in **Debit** column) if the thing is bought and credited if it is sold.
- If the account relates to a living person, the account is debited if he receives cash or goods or things (amount owed to you) and credited if he gives cash or goods or things (amount owed by you).
- If the account relates to an income, *e.g. sales, interest received, etc.*, the income account is credited.
- If the account relates to an expense *e.g. purchases, rent, electricity etc.*, the expense account should be debited.

Accounting for cash sales and cash purchases

Cash sales

Enter amount in the 'Receipts' column in the Cash Book.

Enter amount in the 'Credit' (Income) column of 'Sales Account' in the Ledger.

Cash purchases

Enter amount in 'Payments' of Cash Book.

Enter amount in 'Debit' (expense) column of 'Purchase Account' in the Ledger.

EXERCISE

Venkatesh is running a poultry business. Write the Cash Book and Ledger for the following transactions he's made:

Venkatesh bought 20 chicks at Rs.3/- each on April 5, 1992.

He had cash Rs.200/- in his hand on April 1, the beginning of the year.

He sold five birds on April 10, at Rs.75/- each. He also sold 20 eggs at Rs.0.65 each on April 10.

He borrowed Rs. 500/- from Murugan on April 15. He repaid Murugan Rs.250/- on May 15. He also paid interest of Rs. 10/- to Murugan on May 15.

Credit sales and collection of money

When goods are sold on credit, the transaction will not appear in the Cash Book since cash is not received. This is a transaction which will be entered only in the Ledger:

- Enter amount in customer's account in 'Debit' (due to us) column.

- Enter amount in sales account in ‘Credit’ (income) column.

Later, when the customer pays cash:

- Enter amount in ‘Receipts’ in Cash Book.
- Enter amount in ‘Credit’ (due by us) in customer’s account in the Ledger.

Illustration

Venkatesh sold 10 birds at Rs.80/- each to Gita on credit on Mai’ 16.

Gita paid Venkatesh Rs.500/- on May 23.

LEDGER

Account of Gita

Date	Name of account & description	Debit	Credit
16.5.92	Sales (10 birds at Rs.80 each)	800.00	
23.5.92	Cash (received part amount against sale on 16.5.92)		500.00
31.5.92	Balance carried forward		300.00
	TOTAL	800.00	800.00
1.6.92	Balance brought forward	300.00	

CASH BOOK

Date	Name of account & description	Receipts	payments
23.5.92	Gita (against sale of 10 birds at Rs.80 each on 16.5.92)	500.00	
31.5.92	Balance carried forward		500.00
	TOTAL	500.00	500.00
1.6.92	Balance brought forward	500.00	

LEDGER

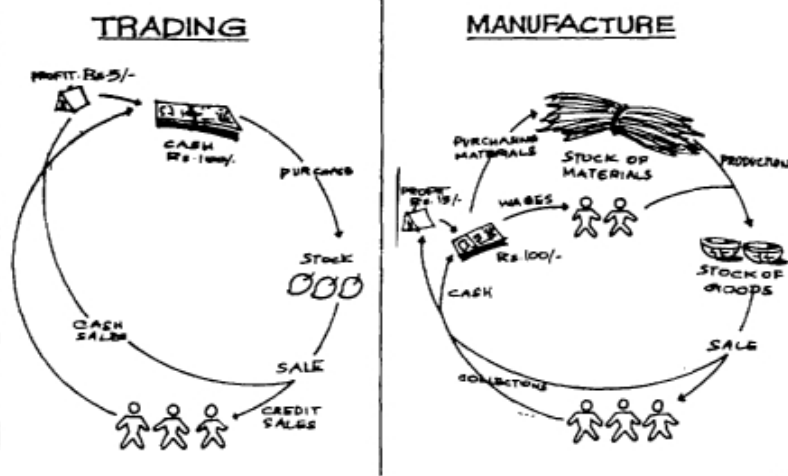
Account of Sales

Date	Name of account & description	Debit	Credit
16.5.92	(lita (sale of It) birds at Rs.80 each)		800.00
31.5.92	Balance carried forward	800.00	
	TOTAL	800.00	800.00
1.6.92	Balance brought forward		800.00

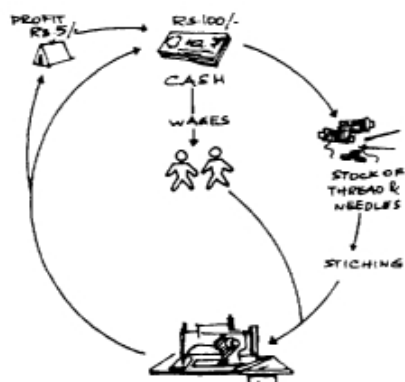
THINGS TO REMEMBER

- Maintaining basic records like a Cash Book and Ledger help:
 - In readily preparing such fundamental accounting statements as Profit and Loss Account, Balance Sheet and Cash Flow Statement.
 - The owner to know what he has to collect from his customers and what he has to pay to his suppliers, thus managing his cash flow better.
 - The owner to protect himself from being exploited by traders, middlemen and moneylenders.

WORKING CAPITAL CYCLE



SERVICES



Working capital

15

What are we going to look at in this chapter?

- What working capital is and how it is different from funds required to buy fixed assets.
- What a 'working capital cycle' is.
- How to estimate how much working capital is required for the business.
- What the sources are of financing working capital requirements.
- Working capital and liquidity of the business.
- Efficient use of working capital and measure of efficient use.
- Diversion of working capital for other purposes and consequences of such diversion.

What is 'working capital'?

Working capital is the money required for the day-to-day running of a business, *e.g. in the case of a vegetable shop, the money required for purchase of vegetables, transport from market to shop etc. In the case of tailor's shop, money required to buy thread, needles. payment of wages, etc.*

This is different from the money required for purchase of fixed assets like machinery, tools and equipment.

Working capital cycle

Cash is invested for purchase of goods, raw-materials, payment of wages and meeting other expenses in the process of producing and selling goods or rendering services. On the sale of goods or rendering of services, cash is got back, thus completing the cycle. Working capital is turned around in the business in regular cycles. In each cycle, the business is expected to generate, besides the money originally invested, an additional sum, called profit. The faster the cycle is completed, more efficient is the use of working capital and, consequently, the more the profit.

Ask participants to identify businesses they are familiar with and trace the working capital cycle with special emphasis on the duration of the various stages in the cycle.

Let us take the example of Elias and Samantha, each investing Rs.100 on fruit. Elias sells his fruit for Rs.120 in one day, while Samantha sells her fruit for Rs./30 in two days.

Here, we see that Elias will make a profit of $\text{Rs.120} - \text{Rs.100} = \text{Rs.20}$ per day.

Whereas Samantha would make a profit of $\text{Rs.130} - \text{Rs.100} = \text{Rs.30}$ in two days. *i.e.* Rs.15 per day.

Therefore, the business is more profitable for Elias who turns around his money in one day.

Components of working capital

Using the same examples, identify the components and estimate the money requirement for each of the components in the cycle.

The basic components of working capital are:

- Money required to maintain stock of raw materials and finished goods.
- Money required to extend credit to customers.
- Money required to pay wages and meet daily expenses.

In the case of a trading enterprise, the stock consists only of trading goods. Whereas, in the case of a manufacturing business, the stock will consist of:

- Raw materials.
- Semifinished goods.
- Finished goods.
- Minor materials required for production, like thread, paints etc.

In the case of a business rendering services, stock required will be limited, consisting of small items and spare parts, *e.g. thread, needles, buttons for a tailor's shop; oil, grease, water, kerosene for a mechanic's shop.*

Assessment of working capital requirement

The working capital requirement depends on the nature of the business and varies widely from business to business. It depends on the following factors:

- Stock required;
Time it takes to produce the goods (production cycle);
- Sales on credit and the credit period;
- Cash required for general operations (salary, electricity, sundry expenses); and
- Proportion of credit purchase to total purchases and the credit period.

Some production enterprises, *such as an oyster farm, a mango plantation or a rug-weaving workshop* may have long waiting periods before the first sale and long waiting periods between sales. During these periods, expenses like wages must be paid. Time becomes a major factor in the calculation of working capital.

Illustration

Parvathi runs a fish stall in a town. Her daily sales amount to Rs. 1,000 with 20% margin. Customers accounting for 20% of the sales pay after a month. She buys all her fish against cash. All unsold fish is eaten by Parvathi's family or given free to her sister for drying. She buys ice every day for Rs. 10. She pays herself a wage of 20 Rs/day. Other monthly expenses amount to Rs. 750. She works for 25 days in a month. Parvathi has set apart Rs. 2,000 for running the business, which, in her opinion, is quite adequate. However, she complains that she is always short of cash and has to borrow often.

Expenses and income of Parvathi's fish stall

Monthly sales	—	25 days x Rs. 1000	=	Rs. 25,000
Monthly purchases		25 days x Rs. 800	=	Rs. 20,000
Daily expenses		Rs.		
Parvathi's salary		20		
Ice		10		
TOTAL/month		30	x 25 =	Rs. 750
Other monthly expenses				750

Working capital requirement

	Rs.	
Money receivable		
from customers Rs. 20,000 x 20% (at cost)	4,000	
Cash required (for salary and ice for 7 days)	210	
Cash required (other expenses/month)	750	
	4,960	
Less: Credit available on purchase		
Working capital required	4,960	

It is assumed that a cash reserve to meet 7 days' requirement of ice and salary and other expenses for one month will be adequate.

From this illustration you can see that Parvathi's working capital requirement is Rs. 4,960, against which she has actually put aside only Rs. 2,000. Obviously, she is short of cash. In Parvathi's reckoning, she is buying fish for Rs. 800 a day and selling for Rs. 1000. Therefore an amount of Rs. 2,000 should be more than

sufficient. Here, however, what she is forgetting is the capital required for extending credit to her customers and this is what is causing her problems.

Funding

In the examples chosen by the participants, is any por-

by suppliers? How is the balance met?

The working capital required is partly met by credit extended by suppliers on purchases. The balance is met partly by the owner himself and the rest by borrowings, from banks or money-lenders. To take the example of Parvathi, she would have found Rs. 2,000 more than sufficient if she got her purchases on one month's credit.

An overdraft is the most suitable loan for funding working capital requirements, as it is a permanent loan and you can draw to the extent required upto a specified limit. Refer to Chapter 17 'Banking & Finance', for more details about overdrafts and other loans, how to raise loans etc.

Working capital and liquidity

The discussion should identify the following criteria for arriving at the correct quantity and mix of stocks, debtors and cash in order that the liquidity position of the business is sound:

- Payment terms stipulated by suppliers,
- How long it takes on an average for the stocks to be sold.
- What the daily cash and credit sales are,
- How long it takes on an average collect money from customers who have bought on credit.
- What the estimated daily expenses are both business and personal.

Supplier credit is an important source of funding working capital but you should be careful about meeting the payment commitments on time. The ability of the business to pay bills on time is called liquidity; this ensures credibility and is a permanent source of funding working capital.

To ensure that suppliers are paid on time, the business should hold sufficient cash, stocks and debts receivable which can be quickly converted into cash.

Inability of a business to pay suppliers on time, due to shortage of cash, is known as sickness. Prolonged sickness will lead to closure of a business.

The reasons for sickness could be that the business is continuously making losses and any amount of working capital made available is being eroded by losses or the business is profitable but sufficient working capital is not available.

Efficient use of working capital

While it is dangerous not to have sufficient working capital. too much of it leads to reduced profits. This is due to interest being paid on the loans taken to fund working capital. Therefore, a business should keep just sufficient working capital and use it most efficiently.

Measure of efficient use

The measure of efficient use of working capital is to see how many times it is turned over or how many cycles are completed in a

given period of time. The more the number of cycles, the greater the efficiency. Efficiency can, therefore, be improved by:

- Better management of stocks.
- Quicker sales.
- Better collection of debts.

Illustration

Kandan runs a provision s/lop. His sale during the year is Rs.120,000. Half his sale is on credit. Kandan keeps an average stock of Rs. 30,000 and the average owed by debtors is Rs. 10,000. Let us find out how many times his working capital is turned over in a year

WORKING CAPITAL		
		Rs.
Stock		30,000
Credit given		10,000
TOTAL		40,000
Sales for the year		120.000
Working capital turnover	Rs. 120,000	= 3 times
	Rs. 40,000	
Stock turnover	Rs. 120,000	= 4 times
	Rs. <u>30,000</u>	
Credit turnover =	Rs. 60,000 (credit sales)	= 6 times
	Rs. 10,000	

WHAT THE RESULTS SHOW

The results indicate that Kandan was able to rotate the money invested in stocks four times in a year, while the money used to sell on credit has been turned over six times, *i.e.* Kandan is more efficient in collecting the debts from customers than managing his stock.

The stock turnover of four times indicates that Kandan is keeping three months' sales requirement in stock. May be he is over-stocking.

CAUTION

The formula described above only tells you how many times the working capital is turned over in the business. Whether it is sufficient or not can be concluded only with a thorough knowledge of the business, how others in the same business are doing etc. For instance, in the above example it is possible that Kandan is simply stocking according to norms or that there is a supply problem and, hence, he has to stock more to avoid stock-outs. Conclusions should be drawn only after considering all aspects.

Diversion of working capital

Diversion means using working capital for purposes other than the day to-day running of the business. The following are common uses to which working capital is normally diverted:

- Purchase of fixed assets, *like machinery, equipment, land, building etc.*, for business or personal use.
- Investment in other businesses.
- Withdrawing large amounts of cash from the bank to meet personal / family commitments, *like celebrating daughter's marriage etc.*

1) diversion of money from the working capital system may result in even a highly profitable business becoming sick and could lead to its closure.

Diversion of working capital is a common problem, especially in small businesses. The reason for this is that the owners do not understand the dangers in diverting working capital and they do not have professional advice easily available to them to point out how important the proper use of working capital is.

DIVERSION OF WORKING CAPITAL



THINGS TO REMEMBER

- Working capital is the money required to **run a business** as distinct from money required to start a business. Without working capital, the business cannot run.
- The money invested for buying goods etc. comes back in the form of cash after completing a cycle during which it passes through several stages. After completion of every cycle, the money got back is more than what was originally invested. This additional money is the profit earned by the business. Thus, the working capital is turned round and round in the business, earning a profit in each cycle. The faster the cycle, the more the profits.
- In case the business is making a loss, the money got back after the completion of each cycle will be less than what was originally invested. If this is not detected, the business will be losing money in every cycle and, eventually, the cycle will stop as there will be no more money to run the business.
- The working capital needs of a business must be carefully assessed and adequately funded. Inadequate working capital funding could render even a profitable business sick.
- Working capital should be funded by a right mixture of:
 - Own money;
 - Supplier credit; and
 - Loans.
- The business should have sufficient cash, inventories and collectable debts to be able to pay the supplier on time. When the business is unable to do so, it is said to be sick. Even a profitable business could become sick if adequate working capital is not provided. Sickness will eventually lead to closure of the business.
- While sufficient working capital is essential to maintain healthy liquidity, too much of it means inefficient use. This results in reduced profits due to the cost of interest. The measure of efficient use is how many times the working capital is turned over in the business within a given period. If the number of cycles is more, efficiency is high; if less, efficiency is low.
- Working capital is the lifeblood of a business. It should be kept intact in the business and should not be diverted for other purposes.

Break-even analysis and best product mix

16

What are we going to look at in this chapter?

- What 'break-even analysis' is.
- Expenses : 'Fixed' and 'Variable' (their nature & behaviour).
- The concept of 'contribution'.
- Break-even analysis for a single-product business.
- Break-even analysis for a multiproduct business and identifying the best product mix under multiproduct situations.

What is 'break-even' in a business?

Break-even is when the gross, or basic, profit earned is just sufficient to meet the 'fixed expenses'. The basic profit is the difference between the selling price and the 'variable expenses'. It is a no profit-no loss situation.

Classification of recurring expenses

Recurring expenses (also called 'Revenue Expenses' or 'Operating Costs') incurred in the day-to-day running of a business, can be further classified into two groups:

- 'Variable expenses'
- 'Fixed expenses'.

Variable expenses are the expenses which can be identified as being the direct cost of a product or service. They include cost of raw materials purchases, labour and other direct expenses in the case of a manufacturing business. They are therefore also called direct expenses. These expenses, per **unit produced**, remain the same irrespective of whether 1000 units are produced or 10 units are produced. Therefore the total variable expenses increase or decrease with the level or volume of business, but their **cost per unit remains constant**. Since the total expenses vary with the volume of business, these expenses are called variable expenses. *e.g. A fruit vendor purchases 100 mangoes for Rs. 500. The cost of one mango = Rs. 5 and 5 mangoes = Rs.25.*

The cost of each mango sold, therefore, remains the same whether one mango is sold or five mangoes are sold.

ONE MANGO



Rs. 5/-

FIVE MANGOES



Rs. 25/-

Fixed expenses are those expenses in a business which remain constant. These can also be called **capacity costs** or **indirect costs**, as they will increase only if the production capacity is increased and are not effected by short-run changes in volume. These expenses are incurred more due to passage of time rather than volume of business and, therefore, are also called **period costs**. For example, rent for a place has to be paid every month irrespective of whether business is carried on or not.

While the total fixed expenses remain constant, fixed expenses **per unit** of goods sold decrease as the volumes increase and increase as the volumes decrease.



FIXED EXPENSES

SHOP RENT, ELECTRICITY,
SALARIES.



CAPACITY COSTS

CAPACITY OF CYCLE IS 5 KGS,
AND HIRE CHARGES RS. 5/-. IF
CAPACITY TO INCREASE TO 10 KGS,
REQUIRE ADDITIONAL CYCLE.
HIRE CHARGES WILL DOUBLE.



PERIOD COSTS

AS TIME PASSES
EXPENSES ARE
INCURRED.

In the example the **vendor** will be able to $\frac{65}{2} \times 30$ kg 30 days
 = 195 kgs. Therefore his profit will be $195 \times 172 \times 0.50$
Rs. 13.34 a month

NOTE'S

EXERCISE

Meenakshi produces four types of baskets — A,B,C,D. Weaving the baskets needs skills and there are NO skilled assistants in the locality. Meenakshi can effectively work for about 250 hours in a month. Particulars of the four types of baskets are as follows:

	Baskets	A	B	C	D
Selling price		38	26	18	10
Variable expenses		33	22	15	
Time taken to weave the basket	(mts)	60	90	100	150

Assuming that Meenakshi has only Rs.1,000 to invest. find out the best product mix and the average contribution for this mix. If the fixed expenses are Rs.500 .. bow many baskets should Meenakshi sell to break even?

Break-even is a situation in ‘which the business earns just sufficient contribution to meet the fixed expenses. It is a **no profit - no loss** situation.

Break-even analysis is a tool that helps in assessing the viability of a business idea and sets the minimum, or ‘threshold’, level of business.

For example, if Prem were to find that he cannot sell a minimum of 5 kg of fish, then he should not consider selling fish.

EXERCISE

Indra produces ‘floats’ for fishing nets. Her capacity is 10,000 units a month. Fixed expenses are constant at 5,000 Rsl/month. The selling price of a float is Rs.5.25 and variable expenses are Rs.4.00 for a float.

How many floats should Indra produce to break-even?

Break-even in the case of a multiproduct situation

The break-even analysis as explained above will hold good for an enterprise dealing with a single product. *Consider an enterprise producing three products.* The fixed expenses are common for all the three products. To find the break-even for each product, the fixed expenses have to be allocated to the three products. But on what basis?

On the other hand, if you try to find out the break-even for the three products put together, you require an average contribution for the three products, as the contributions of each of the products could be different.

Illustration

The entire illustration may be enacted by setting up a shop and actually buying / selling the various vegetables etc. in the manner of the illustration. This will highlight the concepts of ‘contribution’, ‘break-even’ in a multiproduct situation, ‘best product mix’ and contribution per rupee of sale.

	Potatoes R	Onions R	Brinjals R
Cost price / kg	2.00	1.00	3.00
Selling price / kg	2.50	1.50	4.00
Contribution / kg	0.50	0.50	1.00
Average contribution	$\frac{0.50 + 0.50 + 1.00}{3} = \text{Rs.0.67}$		

In computing this average it is presumed that all three products are sold in equal proportions, i.e. one kg each. However, it appears that brinjals gives maximum contribution (1 Rs/kg) compared to the other two products (0.50 Rs/kg each). This being the case, why would you want to sell the three vegetables in equal quantities? You would naturally try to sell more brinjals to earn more profits.

Therefore *if the vendor decides to sell two kgs of brinjals for every kilo of potatoes and onions sold*, the average contribution will be as follows:

	<i>Qty. Sold (kgs)</i>	<i>Contribution/kg Rs.</i>	<i>Total contribution Rs.</i>
Brinjal	2.00	1.00	2.00
Potatoes	1.00	0.50	0.50
Onions	1.00	0.50	0.50
	4.00		3.00

Average contribution $\frac{\text{Rs. 3.00}}{4 \text{ kg}} = \text{Rs. 0.75}$

Thus we see that in a multiproduct business the average contribution changes with the change in the product mix.

Further inquiry into product mix leads us to the question, “Is there a best product mix?”

Continuing with this example we see that potatoes and onions make an equal contribution of 0.50 Rs/kg whereas brinjals make a higher contribution of 1.00 Rs/kg.

Now it appears that *if the vendor were to sell only brinjals*, he would make maximum profit. Let us suppose that the vendor has only Rs.10 to invest. Let us take a situation when he buys only potatoes, only onions or only brinjals.

	<i>On/v potatoes</i>	<i>Only onions</i>	<i>Only brinjals</i>
Kgs bought	Rs.10	Rs.10	Rs.10
=	Rs. 2	Rs. 1	Rs. 3
	= 5 kgs	= 10 kgs	= 3.33 kg
Selling price / kg	Rs. 2.50	Rs. 1.50	Rs. 4.00
Total sales	Rs. 12.50	Rs. 15.00	Rs. 13.32
Contribution/kg	Rs. 0.50	Rs. 0.50	Rs. 1.00
Total contribution	Rs. 2.50	Rs. 5.00	Rs 3.33

Here, we see that it is not brinjals but onions which give the maximum profit. Now how is this? This is because for every rupee of sale, the contribution of onions is the highest.

	<i>Potatoes Rs.</i>	<i>Onions Rs</i>	<i>Brinjals Rs.</i>
Selling price / kg	2.50	1.50	4.00
Contribution / kg	0.50	0.50	1.00
Contribution / rupee of sale	0.50	0.50	1.00
	= 0.20	= 0.33	= 0.25
	2.50	1.50	4.00

We see that instead of absolute contribution, what we have to see is **the contribution per rupee of sale.**

From this example, we would conclude that a person with Rs.10 to invest on one day on the three vegetables, should really invest only in onions to maximize his profit. This assumes, of course, that all 10 kgs of onions can be sold.

Let us assume that the demand for onions is 4 kgs, that for brinjals is 1 kg and potatoes is 2 kgs.

Since the contribution per rupee of sale is maximum for onions, he should definitely buy 4 kgs of onions. This would leave him with a balance of $\text{Rs.}10 - \text{Rs.}4 = \text{Rs.}6$. The second highest contribution is from brinjals. He would therefore buy a kilo of brinjals. This would leave him with a balance amount of $(\text{Rs.}6 - \text{Rs.}3) = \text{Rs.}3$. With this he should buy potatoes, *i.e.* $\text{Rs.}3/\text{Rs.}2 = 1.5$ kgs. This is less than the total demand for potatoes.

Therefore, we find that the best product mix is not dependent only on the contribution/unit of rupee sales but also on the demand! supply and other constraints on the products.

Break-even

Once the best product mix has been determined, the average contribution per unit of sale can be determined. This will be the best contribution the business can get. The fixed expenses should be divided by this contribution to get the break-even sale.

Continuing with the example, the best average contribution when a person has only Rs.10/- to invest per day will be

	<i>Qty. sold (kgs.)</i>	<i>Contribution/kg (Rs.)</i>	<i>Total contribution (R.c.)</i>
Onions	4.00	0.50	2.0(1)
Brinjal	1.00	1.00	1.00
Potatoes	1.50	0.50	0.75
	6.50		3.75
Average contribution	$\frac{\text{Rs.}3.75}{6.5\text{kg}}$	$= \text{Rs.}0.58$	

If the fixed expenses of the vegetable vendor are Rs.100/- per month, the break-even quantity will be

$$= \frac{\text{Rs. } 100}{\text{Rs.}0.58} = 172\text{kgs}$$

i.e. the vendor should sell at least 172 kgs in a month in the proportion of ‘best mix’ to be able to just meet his fixed expenses. Contribution on any additional quantity sold will be his profit.

In the example, the vendor will be able to sell $6.5 \text{ kg} \times 30 \text{ days}$
 $= 195 \text{ kgs}$. Therefore his profit will be $195 - 172 \text{ kgs} \times 23 \times 0.58$
 $= \text{Rs.}13.34 \text{ a month}$.

EXERCISE

Meenakshi produces four types of baskets — A,B,C,D. Weaving the baskets needs skills and there are NO skilled assistants in the locality. Meenaksbi can effectively work for about 250 hours in a month. Particulars of the four types of baskets are as follows:

	Baskets	A	B	C	D.
Selling price		38	26	1\$	10
Variable expenses		33	22	15	8
Time taken to weave the basket					
	(mts)	60	90	100	150

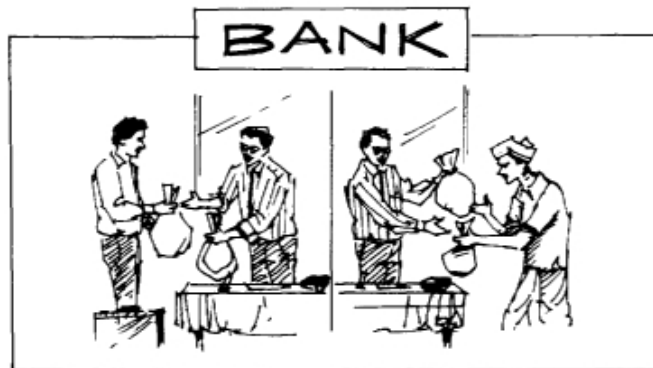
Assuming that Meenakshi has only Rs.1,000 to invest, find out the best product mix and the average contribution for this mix. If the fixed expenses are Rs.500/-, how many baskets should Meenakshi sell to break even?

THINGS TO REMEMBER

- Recurring expenses can be classified into
 - Variable expenses, and
 - Fixed expenses
- Variable expenses remain constant **per unit** sold or produced. Total variable expenses increase if sales increase and decrease if sales decrease.
- Total fixed expenses remain constant. Within this level, if the sales come down, the cost per unit sold goes up, and if sales go up, the cost **per unit** sold will come **down**.
- **The difference between the selling price and the variable cost of each unit is the basic (gross) profit earned by the business out of sale of a single unit of the goods.** This basic profit earned from the sale of every piece contributes towards meeting the fixed expenses and is known as contribution.
- Break-even is a situation when the total contribution is just sufficient to meet the fixed expense and there is neither a profit nor a loss in the business. Any additional contribution earned by the business is the final profit **which** the owner can enjoy.
- Break-even analysis helps in fixing the minimum level to be achieved by the business to be in a 'No profit - No loss' situation.
- Since the fixed expenses per unit come down as the volume of sales increase, one way of maximizing profits is to increase the volume of sales to the maximum.
- In a multiproduct business, you have to take the average contribution to find out the break-even point. Calculating this average calls for a standard mix, or proportion, in which the products will be sold. In deciding on the best product mix, you should not be misled by the absolute contribution of each product. The mix should be arrived at by ranking the products in the order of maximum contribution given per rupee of sale, within constraints like money available to invest, demand for the product etc.



SHOPS TRADE IN GOODS



BANKS TRADE IN MONEY

Banking & Finance

17

What are we going to look at in this chapter?

BANKING;

- What a bank is.
- Why anyone should deposit money in a bank.
- Types of deposits accepted by a bank.
- Why should a microenterprise operate a bank account?

FINANCE

- What finance is.
- Sources of finance.
- Evaluation of own and borrowed sources.
- Types of loans.
- Sources of loans.
- Security for loans
- Types of securities.
- Interest — Cost of Money.

BANKING

What is a 'bank'?

A **bank** is a business which receives money from those who do not have an immediate need for it (**depositors**) and lends it to those who need it (**borrowers**). The bank charges a fee (interest) on money it has lent, keeps a portion of the interest as its revenue and pays the balance to the depositors. Thus, a bank is a trader in money.

Banks, incidentally, also render certain services like regular making payment of bills on instructions from customers, providing lockers for safe-keeping of valuables etc.

Thus, banks play an important role in the growth of industry and trade.

Lead a discussion on what the participants think - a bank is

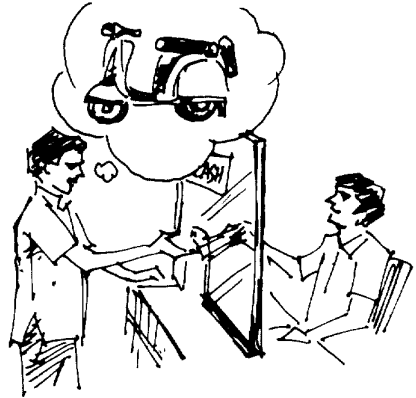
- It's functions.
- In what way banks have played a rôle in developing their local communities.

Need to deposit money in a bank

It is not safe to keep money in the form of cash. It can be stolen.



There is a temptation to spend on unnecessary things if you keep it in the form of cash.



The money will earn interest if it is deposited with a bank.



You can take it back when needed with minimum inconvenience.

Large sums can be paid or transferred from place to place, safely, by cheques or drafts without involving physical handling of cash.



Different kinds of deposits are accepted by banks.

Savings Deposits

For short-term personal savings. These deposits earn a lower rate of interest. Money can be taken out, but restrictions may be placed on the number of withdrawals in a given period. A Savings Account may or may not be operated by cheque.

Current Deposits

For business people and organizations. The account is expected to be operated frequently and, hence, the name 'Current Account'. This account is operated by cheque only. Very low or no interest on deposits, as the money is expected to be kept with the bank for short periods only.

Time Deposits

FIXED DEPOSITS

These are deposits of a fixed amount, paid into the bank in one lump sum for a fixed time. Hence the name 'Time Deposits'. Money cannot be withdrawn before the agreed period and, therefore a higher rate of interest is paid. In case of an urgent need, money can be withdrawn by closing the account or taking a loan against the deposit.

Ask participants to name the various deposit schemes they are aware of or have invested in. Emphasize small savings.

RECURRING DEPOSITS

This is a slight variation of the time deposit. Unlike a fixed deposit, where the entire sum is deposited in one lumpsum at the beginning, here the depositor deposits an equal amount in periodic intervals (weekly, fortnightly or monthly) as agreed upon for a fixed period (say 1 year, 2 years, 3 years). This scheme is ideal for people with recurring small incomes.



Why is it important for a business to open and operate a bank account?

NOTES

Banks are the **normal source of loans for a business**. Banks exist to lend money and make a profit out of the interest charged on the money lent. They are, therefore, on the look out for customers to whom they can lend.

But they will lend only to those whom they know well, whom they trust and who have the capacity to repay the loan together with interest. It is important for any business that the bank considers it favourably for loans. Therefore the business should gain the familiarity, trust and confidence of the bank. This can be done by operating a current account with a bank. The current account would help the manager to assess the business by studying the deposits and withdrawals.

The prosperity of a bank depends on the prosperity of its customers. Therefore, it is likely that the manager of the bank might take an interest in the business and act as an adviser.

FINANCE

What is 'finance'?

Every business requires money to
set it up, and
to run it (working capital).

Finance means obtaining access to various sources of money to fulfil the needs of a business.

Sources of finance

The three main sources of finance are:

- Own money (equity capital).
- Loans (borrowed money).
- Grants/Subsidies (given by Government/Development Agencies/Funding NGOs).

Ask participants to talk about how microenterprises in their areas are normally financed and the various credit schemes they are aware of

Own money vs. Borrowed money

Own money is less risks, because the owner is not answerable to anyone even if he loses the money in the business.

Interest need not be paid on own money. Initially, when the business is struggling to establish itself, interest could be a heavy **burden**. Many profitable businesses have failed on account of erosion of capital due to interest on loans.

However, it is generally not possible to finance a business entirely out of 'own money'. Therefore, a loan becomes a necessity.

Assessing the need for a loan

Owners of small businesses invariably blame nonavailability of loans for all their problems. Experience shows that, in the majority of cases, the real problem is something else. *such as inefficient stock management or poor collection of debts*. Therefore, whenever a small business seeks loan or complains of lack of money, the consultant should study all aspects of the business thoroughly to assess whether the money sought is really required.

Even if money is really required, the following options should be examined before considering a loan:

Is there any old, nonmoving or slow-moving stock that can be disposed of by offering it at a low price for **immediate** cash instead of expecting a good price and waiting for it.

Are there any debts remaining uncollected due to disputes etc. that can be settled by agreeing to take a little less than what is due?

— **Are** there any surplus assets **that** are idle that **could** be sold?

The objective in all these cases is to release the money locked up in unproductive assets within the business and, thus avoid taking loans as far as possible.

CASE STUDY

Rajan's shop did little or no business towards the end of each month.

The reason was clear; half-way through the month, the stocks of sugar, salt and kerosene almost always ran out. But, there were large quantities of dresses and other such goods to last 6 months or a year. Customers, Rajan explained, preferred to buy these things from the same shop where they bought their staple necessities.

Rajan said he had not got enough money to buy sufficient stocks of sugar, salt and kerosene for the whole month. Many of his customers bought goods on credit, and they could not pay until the end of the

month. But he could not pay cash for his supplies until the end of the

(Case study adapted from *Consultancy for Small Businesses* by Malcolm Harper.)

The trainer should lead a discussion of the case. The discussion should identify that it is not a loan that Rajan requires but advice on stock control i.e. Rajan should be advised to dispose of the slow moving stocks by discount sales and utilize the money obtained to keep adequate

of sugar, kerosene,

Term Loan

This loan is to be repaid within a specified term (repayment period) in instalments. The repayment period could be as short as a few months or several years, depending on the source and agreement between the parties.

Interest is usually charged on the principal outstanding after deducting instalments (**diminishing balance method**). The method of charging interest again depends on the source. Private money-lenders usually calculate interest for the entire period on the money initially lent (**flat rate method**).

For example, a trader borrows Rs.3 000 at a simple rate of interest of 20%. The loan has to be repaid in three equal annual instalments of Rs.1 000 each together with interest

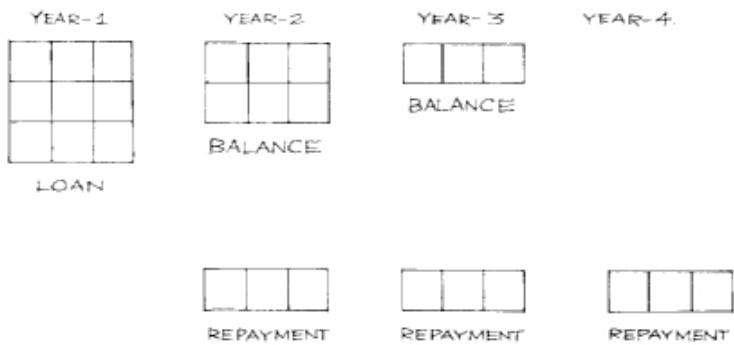
Under the diminishing balance method, the trader will pay an interest of Rs.600 for the first year, being 20% of Rs.3,000 outstanding at the beginning of the first year, Rs.400 for the second year being 20% of Rs.2,000, the loan outstanding at the beginning of second year after repaying the first instalment and Rs.200 for the third year being 20% of Rs.1,000 outstanding at the beginning of the third year after repaying the second instalment. Thus, the trader will pay a total sum of Rs.1,200 as interest during the loan period of three years.

Under the flat rate method the trader will pay a sum of Rs.600 each year for all the three years. being 20% of the Rs.3,000 originally lent to him. This means that the loan repaid in instalments is not reduced from the sum originally lent for the purpose of calculating interest. The trader will pay a total sum of Rs. 1,800 as interest for the loan period of three years.

It is evident from the above that the diminishing balance method of charging interest is favourable to the borrower, but private money-lenders normally do not agree to do this.

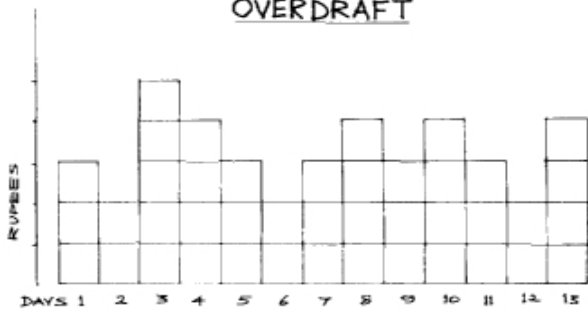
A term loan is suitable for purchase of fixed assets, like machinery, equipment etc., provided the **repayment period** is fairly long – say. three to five years. The reason being, fixed assets require a lot of money to be invested at the time of purchase, while the benefits are received over a long period of time. Term loan with a long repayment period helps the enterprise pay off the loan in easy instalments over a period of time the repayment coming from the money earned by the machinery.

TERM LOAN



TERM LOAN IS REPAYED IN INSTALMENTS

OVERDRAFT



FLUCTUATING BUT PERMANENT LOAN

This is another method of financing fixed assets. Under this method, the buyer pays a portion of the price at the time of purchase and takes the article home. The balance, together with interest, is paid over an agreed period of time. In the event of the buyer not paying the instalments regularly, the seller has the option to take possession of the article.

This method helps people to acquire and enjoy articles like cycles, radios, televisions and other durables with limited initial investment. If the entire price had to be paid at the time of purchase, many consumer durables would be outside the reach of a majority of people.

The benefit to the seller by adopting this method is that he can increase his sales, especially at times, when the purchasing power of people is low.

Overdraft account

An overdraft is a fluctuating loan account. Under this scheme the borrower is allowed to draw money up to a specified limit even though there is no money in the account. The interest is calculated for every day the amount is overdrawn. This kind of a loan is normally given only by banks. An overdraft facility is usually given for a year, and reviewed annually. It is not expected to be repaid in instalments as in the case of a term loan. Thus, it is more or less a permanent loan.

The money required for the day-to-day running of a business (working capital) must be retained intact in the business. Since it is a permanent requirement, this should be financed either by a term loan with a very long repayment period or an overdraft.

Chit funds

This is a group savings scheme. Under this scheme, a certain number of members form a group and agree to contribute a certain sum of money at regular intervals for a definite period. At each interval, the money collected from the members will be taken by one of them, either by auction or by lot. The length of the subscription period will be equal to the number of members so that every member will get a chance to get the pooled money.

Let us assume 20 fishermen join together to run a chit fund. If the monthly subscription is Rs.100, the money pooled every month will be 20 members x Rs.100 each = Rs.2,000. This sum of Rs.2,000 will be taken by one of the members. Since every member must get a chance, the period of the chit will be 20 months.

Ask participants to identify

bought any article under hire purchase, ask them to mention what, and the conditions they had to fulfil

Highlight the dangers of:

Giving in to the temptation of the goods which are not within your reach.

- Inability to pay instalments due to fall in income.

Who gets the pooled money?

This is normally decided by auction or by lot. Those members who have an urgent requirement, bid in the auction, forego a certain sum, and take the balance. The bidder who is willing to forego the maximum will be entitled to take the chit amount. The amount foregone will be equally split and distributed among the members as dividend.

In some schemes, the member entitled to the prize may be determined by lot.

Chit funds are very popular in India. The scheme is called by different names in different parts of the country.

Some join the scheme to save money and others to bid for the chit. The attraction for those who wish to save is that the dividend received is more than the normal interest **AND** they have an option to bid and take a substantial sum (more than what they have saved) in case of an urgent need. For those who intend to bid for the prize, the amount foregone is normally less than what they would have to pay as interest. Further, unlike in borrowing, a member has a right to bid for and take the prize money and is, thus, assured of 'credit' if he is desperate.

Sources of loans

These are some sources of loans:

- **Government / Development Agencies/Funding NGOs** offer loans on very easy terms, but they are very difficult and time-consuming to obtain. Thus, they lose their significance as normal sources of loans.
- **Banks** offer term loans on easy instalments. They also give loans like overdrafts which private money-lenders do not give. The interest charged is reasonable and banks do not exert too much pressure if there is a small delay in repayment. Though difficult to get, banks offer better terms than private money-lenders.
- **Money-lenders** are the most easily accessible and ready sources of loans for small business. They usually live in the same villages and towns as the borrowers and they know the borrowers and their businesses intimately. They may also be involved in the same trade, as wholesalers. They exert immense influence over the borrowers. Their terms and collection methods are severe. Despite these adverse factors, they play a key role in small business activity.
- **Pawnbrokers** are found in every community. They offer short-term loans at high interest rates, but they are easily accessible. They require at least 100% security in the form of jewellery, watches, brass containers etc.

Draw attention to pawn shops operating in the participants' localities etc. What do they lend against? At what rates of interest?

- **Friends and relatives** offer personal loans, with or without interest. This is extremely common. No paperwork is normally done nor security given. Social control within the community is considered sufficient security.

Security

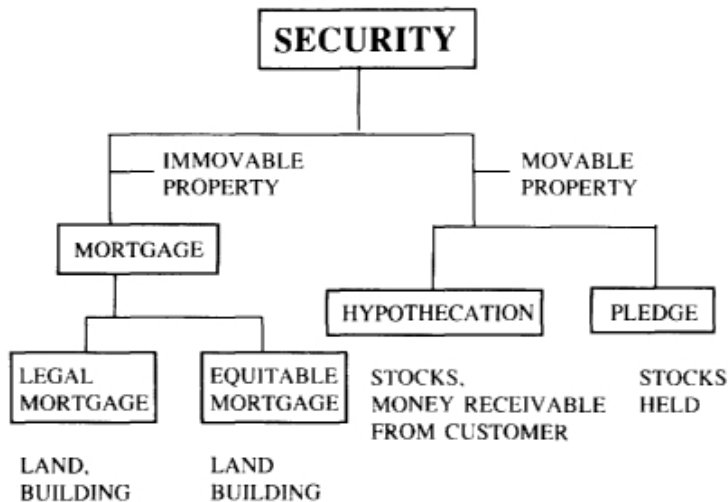
Before giving a loan, a lender will normally insist on some 'security'.

Security means any valuable property given by the borrower to the lender, which the lender can sell, in the event the loan is not repaid.

A few examples are:

- Gold.
- Land & Building.
- Stocks,

Let us look at some ways in which lenders treat security.



Hypothecation

Movable property, like a car, is given to the **lender without physically delivering the property**. The property is kept and used by **the borrower, but the right to the property belongs to the lender**. Often boats, lorries, autorickshaws and even street stalls are hypothecated to a bank.

Pledge

Movable property, like stocks, gold or any article or thing, is physically handed over to the lender (such as a pawnbroker). **The lender keeps the article with him till the borrower pays back the loan**. In the event of the borrower not repaying the loan, the lender can sell the article pledged to recover his money.

Mortgage

When an immovable property like land or building is given as security for a loan it is **called a mortgage**.

There are two types of mortgages. They are:

- Legal mortgage, and
- Equitable mortgage

In legal mortgage, the fact that the property has been mortgaged is noted in records maintained by Government. So it is difficult for the borrower to sell the mortgaged property, without the knowledge of the lender. However, such mortgaging is expensive as it requires duty to be paid to the Government.

In equitable mortgage, the borrower hands over the documents of ownership of the property to the lender. This is less cumbersome and inexpensive. However, it is more risky for the lender.

Interest (cost of money): Is it affordable?

Cassim needs Rs.100 every morning to buy hot snacks for the tray he carries around at the bus-stand in Nagercoil. He will be able to sell the snacks for Rs.120 by the end of the day and make a gross profit of Rs.20. He borrows Rs.100 from the village money-lender every morning and every evening he returns Rs.103. He is now considering giving a week's credit to his regular customers bus drivers and clerks in the offices.

Cassim is paying interest at the phenomenal rate of 3% per day or 1095% per annum. His net profit after interest is 17 Rs/day. By giving credit, he will be able to repay the moneylender only after seven days. The interest for seven days works out to $Rs.3 \times 7 \text{ days} = Rs.21$. He has made only Rs.20, but he has to pay Rs.21. He would, therefore, consider the rate of interest unaffordable for his business — unless he is able to sell the snacks for a higher price.

Similarly, the rate of interest would become unaffordable if his profit margins become lower.

As you can see, the affordability of the rate of interest really depends on

- How fast the borrowed money is turned over in the business (one day *versus* one week as in the illustration above).
- The profit margin.

THINGS TO REMEMBER

- **Banks take money from those who do not have an immediate use for it and lend it to those who have an immediate need.**
- **It is very important for a microenterprise to operate a bank account because:**
 - Banks lend money on easy terms,
 - They lend money only to reliable customers; and
 - Operating a bank account helps the manager to assess the business and consider extending a loan.
- **Own money is the safest source of finance, but it's availability is limited and a loan may be necessary.**
- **Before considering a loan, it should, be examined whether the money is really required. If 'yes', whether there are any sources for raising the money other than through a loan. A loan should be the last resort.**
- **A term loan is given in one stroke and recovered in instalments over a period of time. An overdraft is a fluctuating but, more or less, permanent loan.**
- **Whether the rate of interest on a loan is suitable or not depends on the profitability of the business.**
- **A term loan is suitable for purchasing fixed assets, an overdraft for meeting working capital requirements.**
- **Normally, the moneylender insists on the borrower giving some valuable property as security for the loan.**

Risk & Insurance

18

What are we going to look at in this chapter?

- What risk is.
- Two fundamental types of risks faced by business.
- What is meant by insurance.
- Types of insurance.
- Factors that govern buying Insurance.
- Life insurance.

RISK

What is 'risk'?

Risk means a possibility of loss, damage, destruction, injury or death.

A business involves taking many risks. Most of them are an integral part of the business process, *eg. a mistake in costing could result in an unprofitable contract, a sudden increase in raw material prices could also result in the contract becoming a loss.*

These are called **speculative** or **dynamic** risks. These risks are expected to be foreseen and provided for by the business in the normal course.

For example, Hemant agrees to make a product for Srinivas at 5 Rs/piece. He based the price on the basis of the costs in the market at that time:

Raw materials	=	Rs.1.50
Other variable costs	=	Rs.0.50
Fixed expenses	=	Rs.2.00
Profit	=	Rs.1.00

Instructor to give more examples of dynamic risks. He should also ask the trainees to come out with other examples of dynamic risks the business is likely to face.

The raw material costs have suddenly become Rs.2.50. Now Hemant's profits per unit have become nil and he does not find his agreement with Srinivas attractive.

A business is also exposed to risks like loss due to fire, floods, storm and other natural calamities, riots, war etc., all of which are beyond the control of the business. These risks are called **pure risks**.

What is 'insurance'?

Insurance is a system by which you protect yourself against risk by paying a small fee to a third person to bear the risk on your behalf. In other words, by paying a small price (**premium**) to an insurance company, a person protects himself from a huge potential loss.



Instructor to ask participants more about:

- Insurance companies operating in their areas.
- Different insurance schemes they are aware of.
- Their experience with accidents involving death, disability and the process of making and settling insurance claims.

Insurance companies insure enough people and businesses so that the amount they pay on account of actual losses is much less than what they claim from the same number of people who pay without claiming anything for losses. Like banks, insurance companies manage to pay for this cost and earn a profit out of the difference between premium payments and claims made on them.

Only pure risks can be insured. There is no insurance for normal business or speculative risks.

Types of insurance

Insurance protection is available for the following three types of pure risks:

Loss of property

- Fire.
- Floods.
- Accidents.
- Riots.
- War.



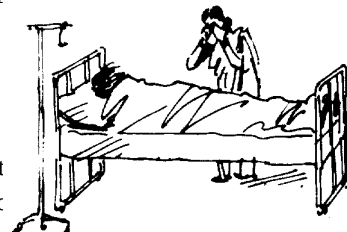
Liabilities

arising out of legal action due to defective quality, improper service etc.



Personal

- loss of income-generating capacity due to death or disability.



Two fundamental factors govern buying insurance. They are:

- Potential loss, and
- Cost-benefit comparison

Consider the following example:

A trader has to transport dry fish worth Rs.300 from one town to the other, every day, for 25 working days in a month. On each consignment she earns a profit of 10%, or a monthly profit of Rs.750 (Rs.300 × 10/100 × 25days). Her personal assets are worth Rs.1,000/-. Accident insurance for the material in transit is 1% of the value of the consignment.

If the trader does not take insurance, she is exposing herself to a potential loss of Rs.300 on each consignment.

Now consider a situation where the trader has to transport the entire 25 days' supply of dry fish at one time. The potential loss in the event of an accident, if she does not take insurance, is then Rs.7,500, which she cannot afford, considering her meagre personal assets.

In the first instance, the trader is sacrificing Rs.75 every month ($\text{Rs.300} \times 1/100 \times 25\text{days} = \text{Rs.75}$). Thus, she is paying 10% of her monthly profits every month and 25% of the potential loss itself, to protect herself from a small, possible loss of Rs.300. In the course of a year, no consignment having met with an accident, she would have paid Rs.900, three times what she is trying to protect.

On the other hand, the trader must definitely take insurance, in the second instance, as she cannot afford the potential loss of Rs.7500 at one shot. In the first instance she **may** decide **not** to take insurance.



Life insurance

Instructor to initiate discussion on the consequences of not paying premiums regularly. Discussion should stress the following:

- Lapse of policy
- Surrender value

Life insurance is a scheme whereby a person provides some financial support for his/her family in the event of the policy holder's sudden death through natural or accidental causes.

Under this scheme, a person takes insurance for a certain amount

— called the sum assured — and keeps paying a small sum at regular intervals. This periodical payment is called the **premium**.

The size of the premium depends on the sum assured, age of the person etc.. The premium is paid for a certain number of years, which is called the **policy term**.

In the event of the death of the person assured, **before the** expiry of the policy term, the family will get the full sum assured. If the policy holder lives right through the policy term, a part of the premiums paid will be returned together with some bonus. Thus, **life insurance serves as a savings scheme** besides providing insurance.

Life insurance is in no way connected with the management of small business. However, if the owner of a small business is aware of this possibility, he may take life insurance and provide financial security to his family in the event of his sudden death.

THINGS TO REMEMBER

- A business organization is exposed to two types of risks:
 - Loss due to sudden increase in prices, levy of new taxes etc., which are a part and parcel of business and arising out of it (dynamic or speculative risks); and
 - Loss due to events beyond the control of the business (pure risks).
- Only pure risks can be insured.
- A business can protect itself by paying small but regular sums (premiums) to insurance companies.
- Since cost of insurance itself could prove expensive, it should be taken only in cases where the potential loss is large and unaffordable to the owner.
- The owner of a small business can protect his family from financial problems in the event of his sudden death (whether natural or accidental) by taking life insurance.
- Unlike in the case of insurance of property, if a person taking out life insurance does not die, s/he will be refunded a part of the premiums paid together with a bonus.

APPENDIX

Accounting practices

To ensure that the balance sheet and the profit and loss account show a true picture of the state of the affairs of the business and to ensure that the accounting statements prepared by various business entities are comparable, it is essential to understand a few accounting concepts and follow certain accounting conventions. The important concepts and conventions are explained below.

Capital and Revenue

All business transactions can be classified under two categories — **Capital** (one time) and **Revenue** (recurring).

All trading transactions and transactions directly related to trading and whose benefit is derived within the accounting period are classified as revenue.

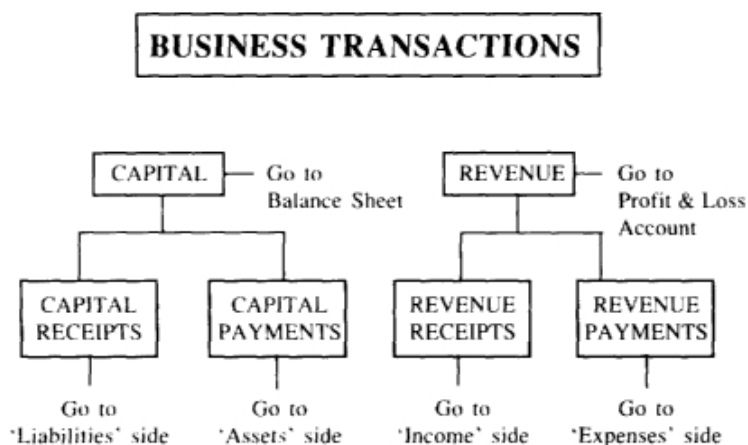
All receipts and payments whose benefits are not derived in one accounting period only but spread over many accounting periods are classified as capital.

If Viji buys 50 kg worth of raw materials, of which only Rs.20 worth of material is processed and sold, then the revenue cost is Rs.20 and capital cost = Rs.50 - Rs.20 = Rs.30/-.

Another way of defining these transactions is that all one-time expenditure is capital and all recurring expenditure is revenue.

All capital transactions find their place in the balance sheet. All capital receipts will be listed on the liabilities side and all capital payments on the assets side.

All revenue transactions will appear in the profit and loss account. All revenue receipts will be taken to income and all revenue payments will be taken to expenses.



A few examples of capital and revenue transactions are:

CAPITAL

Receipts:

Cash invested by the owner
Loan taken from bank
Sale of fixed assets

Payments:

Purchase of land
Purchase of boat
Net purchased
Tools and equipment bought
Loan given
Repayment of loan taken
Money taken by owner
for home expenses

REVENUE

Receipts:

Sale of goods
Fees for services rendered
Interest received

Payments:

Repairs to fixed assets
Interest paid on loans
Purchase of goods
Rent
Salaries & wages
Other expenses

Matching

Let us look at an example to see how that transactions are matched to get a true picture of the business.

Illustration

Rajni produces baskets for a wholesale basket trader in the town. For the year ended March 31, 1992, Rajni sold 2,000 baskets to the wholesaler for Rs.40,000. Further, Rajni received an advance of Rs.500/- on March 31, '92 to make 50 baskets but has not yet produced them.

In this instance, Rajni should consider only Rs.40,000 for computing profits. The advance of Rs.500, though received towards supply of baskets, should be ignored. The reason being she has not yet earned the income as she has not supplied the baskets.

Continuing the example, Rajni employs two women to produce baskets at a salary of 150 Rs/month, each. She normally pays them their salary on the seventh of the next month.

To calculate the profits earned by Rajni. for the year ended on March 31, 1992. the Rs.300 salaries payable to the women for the month of March, should be accounted, though it has not been paid by 31.3.92. The reason is that this Rs.300 expense has been incurred in earning the sales revenue Rs.40,000

In matching transactions in accounting, it should be noted that:

- All incomes earned in an accounting period should be considered, whether money has been actually received or not.
- Income should not be accounted if it is not earned, even if money (advance) is received.
- All expenses incurred in earning the income should be accounted, even if they have not been paid.

- Expenses should be ignored if they do not relate to the particular accounting period or if they have not been used **in earning the income, even** if they are paid.

Treatment of stocks

If all the goods purchased by a trader are sold, if all the raw materials purchased by a manufacturer of goods are consumed within the accounting period, computing the profits of the business would be simple.

Illustration

Rosy is a vendor of dried Ribbonfish. She started her business in April '9/. The rough notebook maintained by Rosy reveals the following:

	Kgs	Rs.
Total purchases upto March 31, 1992	500	22,500
Total sales for the period	500	25,880

Profit made by Rosy for the year ended March 31, 1992

	Rs.
Sale of fish	25,880
Less: Purchases	22,500
Profit	3,380

However, in reality, some of the goods usually remain unsold at the end of an accounting period. As already explained, while computing profits only the cost of the goods sold should be deducted from sales. That is, the value of the unsold goods should be deducted from the purchases to arrive at the cost of goods sold. The following paragraphs illustrate and explain how these unsold goods (stock), should be treated and discuss the problems of giving a value to this stock.

Illustration

Let us continue with the example of Rosy's dried Ribbonfish business. Assuming that Rosy had Rs.40/- worth offish unsold on March 31, '92, the profits are computed as follows:

Profit made by Rosy for the year ended March 31, 1992

	Rs.	Rs.
Sate of fish		25,880
Purchases	22,500	
Less: Stock on hand	40	
		22,460
Profit		3,420

While computing the profits, the purchases are taken at Rs.22,460 and not Rs.22,500 since fish worth Rs.22,460 only were sold to earn the income of Rs.25,880.

While computing the profits for the following year, the stock on hand on 31.3.92 will be added to the purchases of that year since she would have sold this stock too, besides the purchases for that year, to earn the income.

Let us assume Rosy's purchases for the year ended on 31.3.'93 were Rs.45,000, sales Rs.51,750 and unsold fish on 31.3.93 were Rs.80. The profit earned will be calculated as follows:

	Rs.	Rs.
Sales for the year ended on 31.3.93		51,750
Purchases for the period	45,000	
Add : Unsold stock of previous year sold during the year (opening stock)	40	
	45,040	
Less: Unsold stock of the current year (Closing stock)	80	
Cost of fish sold during the year		44,960
Profit		6,790

Valuation of stock

So far we have learnt that the value of stock at the beginning and end of the accounting period should be adjusted from purchases for computing correct profits. **But how do you fix the value for these stocks?**

Let us assume that the unsold fish stocks of Rosy on 31.3.1992 were 5 kgs purchased at 8 Rs/kg.

Purchases for the year ended March 31, 1993 were as follows:

		Rs.
1000	kgs at 8.00 Rs/kg	8,000
1500	kgs at 8.50 Rs/kg	12,750
1000	kgs at 9.00 Rs/kg	9,000
1000	kgs at 9.50 Rs/kg	9,500
575	kgs at 10.00 Rs/kg	5,750
Total	5075 kgs	45,000

The unsold stock on 31.3.1993 (valued at Rs.80, as indicated above) was 8 kgs and would have been bought at 10.00 Rs/kg.

Under the circumstances, at what price should the stock on 31.3.1993 be valued? At cost? Selling price? If at cost, should it be on the prices prevailing at the beginning of the year? Or in the

middle of the year? Or at the end of the year? Or on the average of the prices for the year.

In order to find answers to these questions, we should be familiar with another accounting concept called **prudence**.

Prudence

This concept states that all anticipated losses should be accounted while computing profits. However, anticipated gains should be accounted **only** when such gains are realized. This rule is called **prudence** in the accounting language.

Let us assume the selling price of fish on 31.3.1993 was 12 Rs/kg. Therefore, we can reasonably assume that Rosy could sell the fish the next day at the same price and value the stock at 96 Rs/kg. (8 kg x 12 Rs/kg). However, going by the concept of prudence, the fish should be valued at cost Rs.10 (purchase price) which is less than the selling price, as the anticipated gain of Rs.2 (Rs.12 - Rs.10) has not been realized.

However, if the fish is likely to fetch only 8 Rs/kg, being old, then the stock should be valued at the expected selling price of Rs.8, being less than cost of 10 Rs/kg, *i.e.* 8 kgs x Rs.8 = Rs.64.

Thus, stock should be valued **at cost (purchase price) or likely selling price, whichever is lower**.

But at what purchase price? The price at the beginning of the year? The price prevailing at the end of the year? Or average price?

Valuation methods

FIRST IN FIRST OUT (FIFO)

In the example above, as dry fish is a semi-perishable commodity when dried traditionally and not packaged, Rosy will try to dispose of it at the earliest. So, what comes into her hands first will go out of her hands first. Therefore, we can safely assume that the unsold stock in her hand was bought last and it will be reasonable to value the stock at the latest purchase price, *i.e.* 10 Rs/kg.

LAST IN FIRST OUT (LIFO)

*Visualize a huge shed storing clam shells for a time cement works. The clam shells are collected in large quantities at a rate faster than they are used. Also visualize the long shed as having only one entrance. The shells will be stocked from the farthest end of the shed and then progress with towards the entrance. As shells are not perishable, there is **no** necessity to sell the shells collected first. Therefore, we can visualize the shells collected last and stored nearest to the entrance being disposed of first. So what gets into*

the warehouse last gets sold first. Therefore, the unsold stock can be assumed to have been collected earlier and an can be valued at the cost at which they were collected.

AVERAGE PRICE

Some value stock at the average price. The average purchase price of Rosy’s fish is:

		Qty. (kgs)	Rate (Rs.)	Amount (Rs.)
Opening stock		5	8.00	40
Purchase	1	1000	8.00	8000
	2	t500	8.50	12750
	3	1000	9.00	9000
	4	1000	9.50	9500
	5	575	10.00	5750
Total		5080		45040

Average purchase price =

Rs.45,040

=

8.87 Rs/kg

5,080 kgs

There is no definite rule for valuation of stock. The method most suitable to the particular business should be adopted.

But whatever method of valuation is adopted, it **should be fol-**
lowed consistently, from year to year. Change in method could give rise to profits/losses which would be misleading.

Depreciation

Rosy uses a basket to sell her fish. It is a special basket suitable for fish vending and was bought by her for Rs./00 in April 199/, when she started her business. The life of the basket is expected to he two years.

Now, while computing the profits of Rosy’s fish business for the year ended March 31, 1992, half the value of the basket is consumed in making the sale of Rs.25,880. Applying the accounting principles or matching transactions, Rs.50, half the price of the basket, should be reduced from the profit. This amount represents the estimated amount by which the value of the asset (the basket) has been reduced due to wear and tear. The amount thus reduced is called **Depreciation.**

All fixed assets and one-time costs get ‘consumed’ due to wear and tear. The value of the assets so consumed during an account- ing period is charged as an expense while computing the profits of that period. This spreads the investment costs out, at least on paper, and allows you to see if the business profits are enough in the accounting period to ‘pay’ for fixed assets actually ‘used’.

SECTION III: The Fieldworker Consultant

19. Role of the consultant
20. Observing a business

THE FIELDWORKER CONSULTANT

A consultant can play a very important role in promoting and enabling the development of microenterprises, which could be an important way of enhancing incomes by providing nonfishery livelihoods to fisherfolk.

The consultant can help fisherfolk in the proper selection of an enterprise, keeping viability and sustainability in mind. S/he can assist fisherfolk in the establishment and running of their businesses and, most importantly, help them to cope with problems as they arise.

In this manual we have so far tried to understand various aspects of selecting, setting up and running a business. In this section the focus is going to be on you, the consultant. This section will help you to understand your role as a consultant and help you to manage your task better.

After your training, you can be of help to the community, but do not expect to solve all their problems overnight. Start small, by undertaking activities which visibly help, and demonstrate your usefulness to the community. Learn as you go and from experience; do not hesitate to ask for help when you need it.

Role of the consultant

19

What are we going to look at in this chapter?

- Understanding your current role.
- Problems you are likely to encounter in the field.
- **Your objectives** as a consultant.
- Increasing the effectiveness of your role.
- The work you will have to undertake:
 - Motivating yourself and others.
 - Communicating.
 - Problem-solving.
- Individual action planning exercise

As a consultant, it is vital to be clear about your role, what you should do and what you should not, and the problems you are likely to face. You should plan your work and interact with entrepreneurs keeping these in mind.

Problems you are likely to encounter

You may have to deal with large numbers of small businesses.

- The businesses may be geographically spread out and difficult to reach.
- Your clients, the entrepreneurs, may not be very literate or numerate.
- They may speak different languages/dialects.
- There may be several types of businesses, each quite different from the other.
- Your clients, many of whom may be running small businesses, will be very busy as they have to do all the tasks themselves with very little help.
- Small businesses are more vulnerable as they have little space to manoeuvre. The clients depend greatly on their businesses, but they can be exploited by more powerful economic groups.
- They cannot, on their own, reach experts, development aid agencies and financial institutions for help.

What are you trying to do as a consultant?

Bring about changes in attitude and behaviour in order that your clients may perform better as managers not merely increase their knowledge.

To help your clients to analyze their own situations, needs and problems.

— Help your clients to make more profits.

Motivate your clients to be self-reliant.

Make a permanent difference to their management skills,

ACTIVITY

UNDERSTANDING YOUR CURRENT ROLE AS A CONSULTANT

Give a sheet of paper and a pencil to each participant. No participant should write his name on the sheet of paper.

Request the participants to write about their current work. The key points to be brought out by each participant are:

- What major objectives are to be achieved by his work.
- How he goes about achieving these objectives. He should in his response break down the key activities and what he expects them to achieve.
- What help he received in his work from
 - the people he is trying to help,
 - his organization, and experts within the organization, and
 - his colleagues
- Whether he could have performed better if he had support from:
 - The people he is trying to help;
 - His organization, and experts within the organization;
 - His colleagues
- What helped and what hindered his work
- What aspects of his work he has found most satisfying,
- What aspects of his work he has found most dissatisfying

The sheets of paper should be collected, shuffled and then distributed amongst the participants

Each participant is to read out the sheet he has.

Put up charts in the following format:

- | | |
|-------------------|---|
| 1) Objective | 2) Key activities:
Activity achievements |
| 3) Help/hindrance | 4) Most satisfying /
Most dissatisfying |

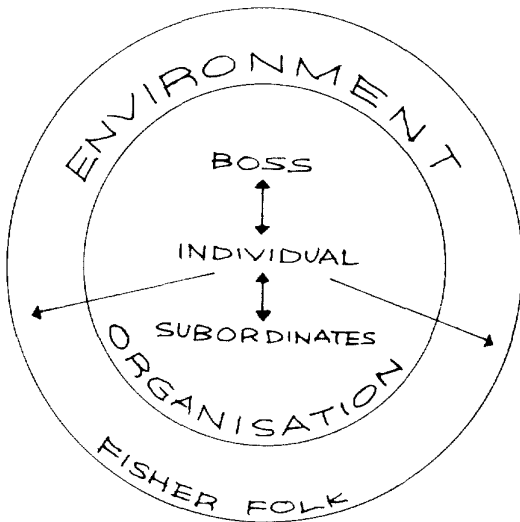
As each participant reads, only key points are to be noted on the charts.

The points should then be discussed and ways around problems found.

The objective of this exercise is to help participants focus clearly on their current role.

Ways to increase the effectiveness of your role as consultant

The performance of an individual in an organization is related to what he or she thinks the organization expects of him or her and how he or she perceives his or her own role. The more you work on improving your role, the more effective you will be.



At work, the consultant deals with the Organization: boss, co-workers and subordinates/assistants and those outside the organization, fisherfolk whom s/he works with. and other Organizations s/he has access to. To improve your role, you have to improve interaction with all involved, using the knowl-

edge, strengths, influence, technical competence and skills you have/can acquire. The more initiative you take in remaking your role, the more effective you will be.

Listed below are some aspects you should consider in helping to remake your role in order to increase your effectiveness. See which of these aspects you can use and how you can use them to remake your role. Always keep in mind all the people with whom you will have to interact.

Centrality

- First of all, you must understand that your role is very important. It is **Central** to improving the standard of living of the fisherfolk and you must be proud of it.

Integration

- You are capable of a lot. You have your own strengths. experience, training, skills and position. You can use each of these to help the fisherfolk. But first you must try and list all your strengths and see how you can use each.
- Write down at least one or two specific areas you could make a contribution in.

Initiative

- Don't wait for opportunities or someone to come to you. You should be the first to take the initiative, make the approach and show interest in helping others.
- The persons you approach will usually welcome you if they know you are genuinely interested in helping them.
- Don't be put off by their occasional hostility. Try and understand the reasons for such hostility and change your approach.
- Write down at least one such place where you can take the initiative.

Creativity

- Be creative. Do not close your mind to solutions. Look for solutions. Don't expect readymade solutions, or only one possible solution to your problem. **Try to look at a problem** from various angles, particularly **through the eyes of your client**.

Request the participants to consider these aspects and

Linking

the effectiveness of their roles. These should also be discussed in groups during the session

You

can use your position to bring together people in the community. You can help form partnerships. You can create a helping atmosphere in the community. You have

access to experts and organizations which can help from outside the community.

Influence

- You can work at influencing your organization/colleagues to provide help/support when you need it to be effective in your role. Think of situations where you can use your influence.

Growth

- When you don't know something, try and learn it. There are many sources of learning — do not give up. **When you learn new things, you grow. When you grow, you get more satisfaction, and confidence, in yourself.**

Confrontation

- Confront a problem — never avoid it. When a person brings a problem to you, help her or him in all ways to arrive at a solution, he will thereafter feel confident about coming back to you. Don't solve the problem for others. **Help them to solve it themselves.**

Motivation

A good consultant can, and should, motivate his or her clients to better performance and greater achievements. Knowledge and skills can be transferred and to do so is important and necessary. But people also need to be motivated to do what they should.

First let us take a look at what we mean by **motivation**.

Each individual has ‘needs’ which are unique to him or her.

Each individual also has ‘needs’ which are unique to him or her. Needs can be classified, basically, as:

PHYSIOLOGICAL	- Hunger
	- Thirst
	- Shelter
SAFETY/SECURITY	- Danger
	- Threats
SOCIAL	- Friends
	- Love
SELF-ESTEEM	- Reputation
	- Self-respect
	- Confidence
SELF-FULFILMENT	- Realizing full potential
	- Being creative

A self-motivated consultant could do a lot to motivate the fisherfolk.

Instil in him/her self-confidence, a feeling of importance and that he/she can achieve something on his, her own. This can be done by:

- Treating people as individuals whom the consultants cares for.
- Setting realistic goals and challenging tasks.
- Giving constructive feedback on how someone is doing.
- Giving recognition and showing appreciation of achievements.
- Helping people solve their personal/work-related problems.

The need makes the person act or influences his or her action. The ‘need’ is the **MOTIVATING FORCE**.

As a consultant you have to learn how to motivate yourself and then motivate your clients. Experience is a great teacher. Learn from it.

Communication

As a consultant, the single most important skill you need is to be able to communicate with your clients: to listen to them and understand what they are saying (**as different from what you think they are saying, or what they should be saying**) and to let them know clearly what you would like them to know.

Communication comes naturally to some, hut most of us have to learn to communicate better.

These aspects of communication should he clearly understood:

- The importance of being simple and clear in communication.
- The importance of being a good listener.

- The importance of ensuring that the message communicated has been understood.
- The importance of the way you speak and how you physically convey your message, through:
 - Facial expression:
 - Body language: and
 - Tone of voice.
- The importance of communicating without delay.

Problem-solving

There are many ways of solving a problem.

Commonsense would suggest that problems can be solved using the basic steps outlined below.

I. DIAGNOSE THE PROBLEM

Quite often we make a mistake in diagnosing the problem. A problem is not always what it appears to be. Let us take an example.

Participants could be divided into two groups to diagnose the problem and present their findings with reasons.

Discussion to highlight how the actual problem of CREDIT MANAGEMENT was arrived at. Before diagnosing a problem, it is important to

- ask questions.
- collect information, and
- analyze information.

Here the consultant has talked to Abdul, seen him in operation and looked at the records kept by him.

Abdul runs a grocery store. His problem was that he never had sufficient money to buy stocks for his shop and, because of this, he was losing many customers. Talking to him for a period of time and spending a day with him revealed a totally different problem

altogether, Abdul considered himself a very good businessman who could attract a lot of customers. He had many more customers than his competitor. The competitor was, however, flourishing.

Abdul gave to his customers much credit, all of which he kept noting down, datewise, in a book. He would follow up with his customers and they would pay him; but they still continued to one hint. What do you think was his problem.'

2. THINK OF POSSIBLE SOLUTIONS

Abdul's problem is credit management. What could be the various possible solutions to his problem?

Abdul should

- Stop giving credit.
- Get out of the retail trade.
- Give credit only to selected customers — those who pay promptly.
- Have a better system of follow-up.
- Make collections the next day, at least a week or with fixed frequency.
- Keep records in the name of each person and constantly update it so that, at any point of time, he knows who owes him how much and from whom.
- Stop credit to alien people who do not pay.
- Use the last two listed solutions in combination.

Discussion to highlight that there is more than one solution to the problem.

Write down solutions, on chart paper as participants mention them.

Ensure the above solutions are definitely mentioned — not necessary in the same order.

This could be handled by letting the participants work in groups.

3. EVALUATE EACH SOLUTION

Evaluate each of the above solutions. By evaluation we mean judging what is most likely to happen when each of the solutions is adopted. *Take, for example, the solution that Abdul should stop credit. What do you think will happen?*

The participants to divide into two groups and each to discuss the various solutions and put it up on posters. One person from each group to describe how they arrived at the solution.

4. IMPLEMENT THE SOLUTION

The final step is the implementation of the solution.

This is the most sensitive part in the problem-solving cycle,

Abdul's customers are used to credit and suddenly stopping credit might result in his customers getting angry because they feel that Abdul has begun to mistrust them: a large proportion of them are likely to stop being his customers and go over to his competitor.

What do we mean by sensitive!

The sensitiveness lies in the fact that the solution has to be acceptable to Abdul and he has to be convinced that

- It is the right solution;
- Implementing it would be easy; and
- Implementing it would make his business flourish.

Abdul must also be convinced to accept interference from the consultant. Though he probably brought the problem to the consultant himself, he may not accept the consultant saying, "Look, Abdul, your problem is that your records are not properly maintained. Take a book in which you have one page for each customer and write down how much he owes you. Every Sunday, you must collect all that is owed you and stop further credit for anyone who does not pay you".

Abdul might implement the solution or he might nod his head and later think, "Oh, it is very well for Mr. C to talk like this. What does he think?! My records are not proper? I don't know how much each person owes me? I know every paisa each person owes me!

The discussion to be led by asking the following questions:

- What do you think is the problem in the implementation?
- If you were to be the barefoot consultant, how would you have handled it?

Participants to work in two groups. Each group to bring out

- 1) What the problem in implementation of the solution was, and
- 2) How they would have handled the situation and implemented it.

And Where does he think I have the time to write so inativ accounts and go after every person on Sunday? Does he know how much work I have on Sunday?" Abdul t is, thus very angr\ with the consultant for not helping hint properly and tot giving him solu- tions which arc not feasible. Now, if lie had arranged a loan. that would have been the right thing to do. Abdul is verdepresed and his business continues to get into more trouble.

ACTIVITY

The activity aid discus- sions that follow to highlight that problem-solving meth- ads wiH vary from person to person

Role Play

One person from Group A to he Abdul. One person from Group B to be Mr. C to implement Group B's solutionAnd Abdul to react. The process to be repeated, with Abdul this time being from Group B and Mr. C from Group A implementing Group A's solution.

	Consultant	Entrepreneur
DIRECTIVE	1. Tells: resolves, decides and issues instructions. 2. Tells and sells: resolves, decides, informs instructions with reasons.	Acts only on instructions. Acts m instructions with explanation.

There are people who want to be told what they should do next, there are others who want to be told why they have been asked to do some- thing. This is what we would call directive problem solving.

PRESCRIPTIVE	Tells and sells and tests: resolves, decides, informs, instructions with reasons and results expected. Reviews and changes recommendations.	Discusses solutions and gives recomm- endations based on testing.
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'there are people who want to he told why they have been asked to do something and would like to test and give their own recommendations before a solution is arrived at. This is what we would call prescriptive problem solving.

PARTICIPATIVE	Joint problem solving: discusses and defines problems. joint problem- solving process and joint. decisions are made.	loins in the problem-solving process.
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There are people who want to participate and are capable of thinking along with you and offering solutions. Solutions arrived at in this manner are more acceptable to such people. This is what we call the participa- tive problem solving method.

It is important for the consultant to realize the situation, be SENSI- TIVE to it and he able to judge which method is likely to be the most effective.

Time management

Time is something which we often take for granted. The busier you get, the more the pressure on your time. Therefore, you should **manage** time effectively in order to achieve goals.

Effective time management will help you to make better use of your time by giving you an overview and, as a result, 'control' over your time. This would lead to better results.

Effective time management would involve, first, listing all that you have to do under the following heads;

- Major tasks
(broken up into)
- Minor tasks
(further broken up into
- Practical activities.
- Other details required to complete each of your major tasks.

The instructor may give a few examples to convey the concept

Once this is done, an estimate of time required to complete each activity can then be made.

Now you could take up the individual activities one by one and ensure that the major task gets completed. It is not enough if this break-up alone is done. It would be essential to decide **when** you would undertake **each of the** activities.

A diary is the most useful tool for this. The diary should be used to plan how you are going to spend your year, month, week and day.

The most important of these is the day. Daily planning will help you achieve your weekly, monthly and yearly goals by ensuring that all the minor tasks and activities get done. Since you have arrived at the minor activities only by breaking up your major tasks, you would achieve your goals in the given timeframe. Thus, the way you spend each day will determine what you will achieve (during the year/your lifetime).

'The daily plan for the next day should be ready by the end of each

is plan should be implemented by taking the following steps'

Fill in your diary with your fixed appointments:

- (Get an overview of what time is remaining; then

Make a realistic 'to do' list of minor tasks. ^{from} your list of tasks. etc.

Each participant makes a presentation of his or her action plan to the group and discussion is mediated by the instructor to ensure that the lessons have been well assimilated

ACTIVITY

Individual Action Planning Exercise

Give each individual a sheet of paper and pencil.

Ask the participants to consider

- **Their work situations, i.e. the fisherfolk communities they work in; and**
- **What they have been exposed to in the programme.**

Based on the above, each participant should draw up an action plan.

Key facts to be indicated are:

- **Identification of communities/families/individuals who could start microenterprises. What options and what could be the consultant's role in making it happen: initiative, communicating, identifying etc.**
- **identification of existing microenterprises the consultant could help.**
- **Identification of ways in which the consultant could increase his/her own role.**
- **Timeframe in which the consultant can really make some impact.**
- **What additional support the consultant would need to make the above happen. How s/he can get the additional support.**

Observing a business

20

What are we going to look at in this chapter?

- Assessing the general condition of a business.
- Systematic recording of information.

As a consultant, one of the first tasks you must undertake is to assess the general condition of the business and ask questions in order that the causes of the problems the entrepreneur is facing are brought to light. In particular, you should consider the following aspects of management, and you should note down your answers to these questions, together with your ideas of how any deficiencies might be remedied. You need not, at this stage, try to persuade the entrepreneur to follow your suggestions, but you should try to discuss them with him.

- How well the cash is controlled, and how safe it is.
- Whether the owner knows how much cash is being received, and how much is being paid out.
- Whether the owners' withdrawals from the business are properly recorded.

Whether the customers buy goods on credit and, if so, whether the owner records this and can he tell at a glance how much each customer owes.

Whether the owner receives any credit from suppliers and, if so, does he know what he owes them at any time.

How the owner decides what goods to put into stock.

- **How** the owner decides what quantities of goods to buy.
- What the other problems or deficiencies are.

You must remember that information just for information's sake is useless and will only clutter your mind and not allow you to move forward to help the business. However, certain preliminary information about the business is essential. Since you will be interacting with so many businesses and people, it will be useful to maintain a systematic record of your work.

Apart from the basic information which you will collect about every business, you also should ask about problems the businesses, are facing and make recommendations on ways to overcome these problems. It is important that a summary of this dialogue and recommendations are recorded, datewise for effective monitoring. Otherwise you might have to start all over again and valuable time may be lost.

These records should, ideally be filed in separate folders for each business.

Your observations can be recorded in a particular format for every business you offer your services to, so that a basic record is created. These basic records may be:

- A statement of what the business owns and owes.
- An estimate of the profit/loss being made by the business.
- Any other information.

The specimen forms that follow are adapted from *Consultancy for Small Businesses* by Malcolm Harper (Intermediate Technology Publications Ltd., London).

Preliminary information

PLACE _____ VILLAGE/MARKET/TOWN

DATE OF FIRST SESSION _____

NAME AND ADDRESS OF BUSINESS _____

YEAR BUSINESS STARTED _____

TYPE OF BUSINESS _____

WHAT IS TI-IF MOST IMPORTANT PROBLEM IN YOUR BUSINESS?

WHAT ARE THE OTHER PROBLEMS, IF ANY _____

The consultant before filling in the forms should explain that **BETTER MANAGEMENT** may help the entrepreneur to get over his problems, that he is not giving loans, chasing debts or asking about taxes, but trying to help him manage his business better with some **ADVICE** and that he needs some information from him before he can do this.

WHAT THE BUSINESS OWNS AND WHAT IT OWES

What do you have in your business today. and how much is it worth'?

Is this building your property? (Yes/No) If yes' what is its value now'?

What is the value of all the furniture and equipment you have in your business, if you had to sell it today?

What is the value of all the goods in stock today'?

Do you give any credit at all? (Yes/No). If 'yes. how much is owed to you today, by all your customers. whether overdue or not? (Try to add up i/u' total from the record of debtors.)

Does the business have a bank account'? (Yes/No), If 'yes'. how much is in it? (Try to check the bank

Do you have any other money which can be used for the business when necessary?

How much CASH have you got here now which belongs to the business'? (Try to See the actual money.?

The total amount of money, or value of other things that you are using in your business today is, therefore
TOTAL 'ASSETS'

Let us try' to see where this came from.

Do you get any credit from your suppliers? (Yes/No, If so. how much do you owe them) altogether today? (Try to check from records.)

Do your customers ever pay in advance'? (Yes/No.) If so. how much have you got from them at the moment for goods not yet sold'? (Try to check from records.)

Have you received loans from any source'? If so. how much do you owe at the moment'?

How much money did you and your partners. if any. put into this business at the beginning'?

How much have you put into it since then'?

The total amount put into the business by you or 'lent' from other sources, is, therefore. TOTAL

The difference between this and the total value of what is in the business has come from profits (or losses) earned by the business.

The total value of everything in the business is as we worked out before:

Now let us see how much profit or loss you are making each month

What is the total value of your sales in an average month? (Try to check from cash records, debtors records, guesses of a day's sales, or your own observations.) SALES TOTAL

What does it cost you to buy the goods that you sell for this amount? (Check opening stock and goods bought less closing stock, or receipts, or average gross profit on sales.)

What do you yourself take out of the business in an average month in wages, salary, value of goods taken and not paid for, gifts to relatives and so on? (Check records.)

Do you employ any others in this business? How many? (If so, what do you pay them in total per month? _____)

What rent do you pay per month? _____

What do you spend on transport each month?

What do you spend on water, electricity, wrapping materials etc. each month for the business? (Be sure no expenses are forgotten.)

What do you spend on loan interest and repayments each month? _____

What is the MONTHLY cost of your licences? (Check licence fee/week.) _____

Your total expenses per month are therefore.
EXPENSES TOTAL

The difference between your total expenses and your sales is your profit/loss. PROFIT/LOSS

PUBLICATIONS OF THE BAY OF BENGAL PROGRAMME (BOBP)

The BOBP brings out the following types of publications:

Reports (BOBP/REP/...) which describe and analyze completed activities such as seminars, annual meetings of BOBP's Advisory Committee, and subprojects in member-countries for which BOBP inputs have ended.

Working Papers (BOBP/WP/...) which are progress reports that discuss the findings of ongoing work.

Manuals and Guides (BOBP/MAG/...) which are instructional documents for specific audiences.

Information Documents (BOBP/INF/...) which are bibliographies and descriptive documents on the fisheries of member-countries in the region.

Newsletters (*Bay of Bengal News*) which are issued quarterly and which contain illustrated articles and features in nontechnical style on BOBP work and related subjects.

Other publications which include books and other miscellaneous reports.

Those marked with an asterisk (*) are out of stock but photocopies can be supplied.

Reports (BOBP/REP/...)

- 32.* *Bank Credit for Artisanal Marine Fisherfolk of Orissa, India.* U. Tietze. (Madras, 1987.)
33. *Nonformal Primary Education for Children of Marine Fisherfolk in Orissa, India.* U. Tietze, N. Ray. (Madras, 1987.)
34. *The Coastal Set Bagnet Fishery of Bangladesh — Fishing Trials and Investigations.* S. E. Akerman. (Madras, 1986.)
35. *Brackishwater Shrimp Culture Demonstration in Bangladesh.* M. Karim. (Madras, 1986.)
36. *Hilsa Investigations in Bangladesh.* (Colombo, 1987.)
37. *High-Opening Bottom Trawling in Tamil Nadu, Gujarat and Orissa, India : A Summary of Effort and Impact.* (Madras, 1987.)
38. *Report of the Eleventh Meeting of the Advisory Committee, Bangkok, Thailand, 26-28 March, 1987.* (Madras, 1987.)
39. *Investigations on the Mackerel and Scad Resources of the Malacca Straits.* (Colombo, 1987.)
40. *Tuna in the Andaman Sea.* (Colombo, 1987.)
41. *Studies of the Tuna Resource in the EEZs of Sri Lanka and Maldives.* (Colombo, 1988.)
42. *Report of the Twelfth Meeting of the Advisory Committee.* Bhubaneswari, India, 12-15 January 1988. (Madras, 1988.)
43. *Report of the Thirteenth Meeting of the Advisory Committee.* Penang, Malaysia, 26-28 January 1988. (Madras, 1989.)
44. *Report of the Fourteenth Meeting of the Advisory Committee.* Medan, Indonesia, 22-25 January, 1990. (Madras, 1990.)
45. *Gracilaria Production and Utilization in the Bay of Bengal Region Report of a seminar held in Songkhla, Thailand, 23-27 October 1989.* (Madras, 1990.)
46. *Exploratory Fishing for Large Pelagic Species in the Maldives* R.C.Anderson, A.Waheed, (Madras, .1990.)
47. *Exploratory Fishing for Large Pelagic Species in Sri Lanka.* R Maldeniya, S. L. Suraweera. (Madras, 1991.)
48. *Report of the Fifteenth Meeting of the Advisory Committee.* Colombo, Sri Lanka, 28-30 January 1991. (Madras, 1991.)
49. *Introduction of New Small Fishing Craft in Kerala, India.* O. Gulbrandsen and M. R. Anderson. (Madras, 1992.)
50. *Report of the Sixteenth Meeting of the Advisory Committee.* Phuket, Thailand, 20-23 January 1992. (Madras, 1992.)
51. *Report of the Seminar on the Mud Crab Culture and Trade in the Bay of Bengal Region, November 5-8, Surat Thani, Thailand.* Ed by CA. Angell. (Madras, 1992.)
52. *Feeds for Artisanal Shrimp Culture in India — Their Development and Evaluation.* J F Wood et al. (Madras, 1992.)
53. *A Radio Programme for Fisherfolk in Sri Lanka.* R N Roy. (Madras, 1992.)
54. *Developing and Introducing a Beachlanding Craft on the East Coast of India.* V L C Pietersz. (Madras, 1993.)
55. *A Sri Lanka Credit Project to Provide Banking Services to Fisherfolk.* C. Fernando, D. Attanayake. (Madras, 1992.)
56. *A Study on Dolphin Catches in Sri Lanka.* L Joseph. (Madras, April 1993.)
57. *Introduction of New Outrigger Canoes in Indonesia.* G Pajot, O Gulbrandsen. (Madras, 1993.)
58. *Report of the Seventeenth Meeting of the Advisory Committee.* Dhaka, Bangladesh, 6-8 April 1993. (Madras, 1993.)
59. *Report on Development of Canoes in Sri Lanka.* G Pajot, O Gulbrandsen. (Madras, 1993.)
60. *Improving Fisherfolk Incomes through Group Formation and Enterprise Development in Indonesia.* R N Roy. (Madras, 1993.)
61. *Small Offshore Fishing Boats in Sri Lanka.* G Pajot. (Madras, 1993.)
63. *Small-scale Oyster Culture on the West Coast of Peninsular Malaysia.* D Nair, R Hall, C Angell. (Madras, 1993.)

Working Papers(BOBP WP/...)

49. *Pen Culture of Shrimp by Fisherfolk : The BOBP Experience in Killai, Tamil Nadu, India.* E. Drewes, G. Rajappan. (Madras, 1987.)

50. *Experiences with a Manually Operated Net-Braiding Machine in Bangladesh.* B.C. Gillgren, A. Kashem. (Madras, 1986.)
51. *Hauling Devices for Beachlanding Craft.* A. Overa. P.A. Hemminghyth. (Madras, 1986.)
52. *Experimental Culture of Seaweeds* (Gracilaria Sp.) in Penang, Malaysia. (Based on a report by M. Doty and J. Fisher). (Madras, 1987.)
53. *Atlas of Deep Water Demersal Fishery Resources in the Bay of Bengal.* T. Nishida, K. Sivasubramaniam. (Colombo, 1986.)
54. *Experiences with Fish Aggregating Devices in Sri Lanka.* K.T. Weerasooriya. (Madras, 1987.)
55. *Study of Income, Indebtedness and Savings among Fisherfolk of Orissa, India.* T. Mammo. (Madras, 1987.)
56. *Fishing Trials with Beachlanding Craft at Uppada, Andhra Pradesh, India.* L. Nyberg. (Madras, 1987.)
57. *Identifying Extension Activities for Fisherwomen in Vishakhapatnam District, Andhra Pradesh, India.* D. Tempelman. (Madras, 1987.)
58. *Shrimp Fisheries in the Bay of Bengal.* M. Van der Knaap. (Madras, 1989.)
59. *Fishery Statistics in the Bay of Bengal.* T. Nishida, (Madras, 1988.)
60. *Pen Culture of Shrimp in Chilaw, Sri Lanka.* D. Reyntjens. (Madras, 1989.)
61. *Development of Outrigger Canoes in Sri Lanka.* O. Gulbrandsen, (Madras, 1990.)
62. *Silvi-Pisciculture Project in Sunderbans, West Bengal : A Summary Report of BOBP's assistance.* C.L. Angell, J. Muir, (Madras, 1990.)
63. *Shrimp Seed Collectors of Bangladesh.* (Based on a study by UBINIG.) (Madras, 1990.)
64. *Reef Fish Resources Survey in the Maldives.* M. Van Der Knaap et al. (Madras, 1991.)
65. *Seaweed (Gracilaria Edulis) Farming in Vedalai and Chinnapalam, India.* I. Kalkman, I. Rajendran, C. L. Angell. (Madras, 1991.)
66. *Improving Marketing Conditions for Women Fish Vendors in Besant Nagar, Madras.* K. Menezes. (Madras, 1991.)
67. *Design and Trial of Ice Boxes for Use on Fishing Boats in Kakinada, India.* I.J. Clucas. (Madras, 1991.)
68. *The By-catch from Indian Shrimp Trawlers in the Bay of Bengal: The potential for its improved utilization.* A. Gordon. (Madras, 1991.)
69. *Agar and Alginate Production from Seaweed in India.* J. J. W. Coopen, P. Nambiar. (Madras; 1991.)
70. *The Kattumaram of Kothapatnam-Pallipalem, Andhra Pradesh, India — A survey of the fisheries and fisherfolk.* K. Sivasubramaniam. (Madras, 1991.)
71. *Manual Boat Hauling Devices in the Maldives.* (Madras, 1992.)
72. *Giant Clams in the Maldives-A stock assessment and study of their potential for culture.* J. R. Barker. (Madras, 1991.)
73. *Small-scale Culture of the Flat Oyster (Ostrea folium) in Pulau Langkawi, Kedah, Malaysia.* D. Nair, B. Lindeblad. (Madras, 1991.)
74. *A Study of the Performance of Selected Small Fishing Craft on the East Coast of India.* G. El Gendy. (Madras, 1992.)
75. *Fishing Trials with Beachlanding Craft at Thirumullaivasal, Tamil Nadu, India 1989-1992.* G. Pajot (Madras, 1992.)
76. *A View from the Beach — Understanding the status and needs of fisherfolk in the Meemu, Vaavu and Faafu Atolls of the Republic of Maldives.* The Extension and Projects Section of the Ministry of Fisheries and Agriculture, The Republic of Maldives. (Madras, 1991.)
77. *Development of Canoe Fisheries in Sumatera, Indonesia.* O. Gulbrandsen, G. Pajot. (Madras, 1992.)
78. *The Fisheries and Fisherfolk of Nias Island, Indonesia. A description of the fisheries and a socio-economic appraisal of the fisherfolk.* Based on reports by G. Pajot, P. Townsley. (Madras, 1991.)
79. *Review of the Beche De Mer (Sea Cucumber) Fishery in the Maldives.* L. Joseph. (Madras, 1992.)
80. *Reef Fish Resources Survey in the Maldives -Phase Two.* R. C. Anderson, Z. Waheed, A. Arif. (Madras, 1992.)
81. *Exploratory Fishing for Large Pelagic Species in South Indian Water.* J. Gallene, R. Hall. (Madras, 1992.)
82. *Cleaner Fishery Harbours in the Bay of Bengal.* Comp. by R. Ravi Kumar (Madras, 1992.)
83. *Survey of Fish Consumption in Madras.* Marketing and Research Group, Madras, India. (Madras, 1992.)
84. *Flyingfish Fishing on the Coromandel Coast.* G. Pajot, C. R. Prabhakaradu. (Madras, 1993.)
85. *The Processing and Marketing of Anchovy in the Kanniyakumari District of South India: Scope for Development.* T. W. Bostock, M. H. Kalavathy, R. Vijaynidhi. (Madras, 1992.)
86. *Nursery Rearing of Tiger Shrimp Post-larvae in West Bengal, India.* H. Nielsen, R. Hall. (Madras, 1993.)
87. *Market Study of Tiger Shrimp Fry in West Bengal, India.* M M Raj, R. Hall. (Madras, 1993.)
88. *The Shrimp Fry By-catch in West Bengal.* B K Banerjee, H. Singh. (Madras, 1993.)
89. *Studies of Interactive Marine Fisheries of Bangladesh.* Management and Development Project, Department of Fisheries, Chittagong, Bangladesh. (Madras, 1993.)
90. *Socioeconomic Conditions of Estuarine Set Bagnet Fisherfolk in Bangladesh.* K.T. Thomson, Sk. Md. Dilbar Jahan, Md. Syed Hussain. (Madras, 1993.)
91. *Further Exploratory Fishing for Large Pelagic Species in South Indian Waters.* G. Pajot. (Madras, 1993.)

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1. **Towards Shared Learning : Non-formal Adult Education for Marine Fisherfolk. Trainers' Manual.** Madras, June 1985.)
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3. **Fishery Statistics on the Microcomputer : A BASIC Version of Hasselblad's NORMSEP Program.** Madras, N. David, J. Hertel-Wulff. (Colombo, 1986.)
4. **Separating Mixtures of Normal Distributions : Basic program for Bhattacharya's Method and Their Application for Fish Population Analysis.** Madras, I. Goonetilleke, K. Sivasubramaniam. (Madras, 1987.)
5. **Bay of Bengal Fisheries Information System (BOBFINS): User's Manual.** Colombo, 1987.)
6. **A Manual on Rapid Appraisal Method for Coastal Communities.** Madras, P. Townsley. (Madras, 1993.)
7. **Guidelines for Extension Workers in Group Management, Savings Promotion and Selection of Enterprises.** Madras, P. Limawan. Directorate General of Fisheries, Ministry of Agriculture, Government of Indonesia, Jakarta and Bay of Bengal Programme. (In Indonesian). (Madras, 1992.)
8. **Extension Approaches to Coastal Fisherfolk Development in Bangladesh: Guidelines for Trainers and Field Level Fishery Extension Workers.** Madras, Department of Fisheries, Ministry of Fisheries and Livestock, Government of Bangladesh and Bay of Bengal Programme. (In Bangla). (Bangladesh, 1992.)
9. **Guidelines on Fisheries Extension in the Bay of Bengal Region.** Madras, I. Jungeling. (Madras, 1993.)
10. **Our Fish, Our Wealth.** A guide to fisherfolk on resources management. — In 'comic book' style (English/Tamil/Telugu). K. Chandrakant with K. Sivasubramaniam, R. Roy. (Madras, 1991.)
11. **How to Build a Timber Outrigger Canoe.** Madras, O. Gulbrandsen. (Madras, 1993.)
12. **A Manual for Operating a Small-scale Recirculation Freshwater Prawn Hatchery.** Madras, Chowdhury, H. Bhattacharjee, C. Angell. (Madras, 1993.)
13. **Building a Portable Propulsion System for Small Fishing Craft— The BOB Drive.** Madras, O. Gulbrandsen, M R Andersen. (Madras, 1993.)
14. **Guidelines for Fisheries Extension in the Coastal Provinces of Thailand.** Madras, Fisheries Extension Division, Department of Fisheries, Ministry of Agriculture and Cooperatives, Bangkok, Thailand and the Bay of Bengal Programme. (Thailand, 1993.)
15. **Guidelines for Cleaner Fishery Harbours.** Madras, R. Ravikumar. (Madras, 1993.)
16. **A Handbook of Oyster Culture.** Madras, Y.B.H. Nawawi. (In English/Malay). (Madras, 1993.)
17. **Management of Fisherfolk Microenterprises: A manual for training of trainers.** Madras, V. Muthu, P.S.A. Kunchitba Padam, Bhatnagar. (Madras, 1993.)
18. **Life on Our Reefs- A colouring book.** Madras, Ministry of Fisheries and Agriculture, Male, Republic of Maldives and the Bay of Bengal Programme. (Madras, 1993.)

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10. **Bibliography on Gracilaria— Production and Utilization in the Bay of Bengal.** Madras, 1990.)
11. **Marine Small-Scale Fisheries of West Bengal : An Introduction.** Madras, 1990.)
12. **The Fisherfolk of Puttalam, Chilaw, Galle and Matara- A study of the economic status of the fisherfolk of four fisheries districts in Sri Lanka.** Madras, 1991.)
13. **Bibliography on the Mud Crab Culture and Trade in the Bay of Bengal Region.** Madras, 1992.)

Newsletters (Bay of Bengal News)

Quarterly, from 1981

Other Publications

1. **Helping Fisherfolk to Help Themselves : A Study in People's Participation.** Madras, 1990.)
2. **The Shark Fisheries of the Maldives.** Madras, R C Andersen, H Ahmed. Ministry of Fisheries and Agriculture, Maldives. (Madras, 1993.)

NOTE: Apart from these publications, the BOBP has brought out several folders, leaflets, posters etc., as part of its extension activities. These include Post-Harvest Fisheries folders in English and in some South Indian languages on anchovy drying, insulated fish boxes, fish containers, ice boxes, the use of ice etc. Several unpublished reports connected with BOBP's activities over the years are also available in its Library.

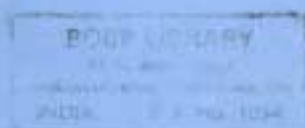
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Extension



For Fisheries Development

BAY OF BENGAL PROGRAMME

The Bay of Bengal Programme (BOBP) is a multiagency regional fisheries programme which covers seven countries around the Bay of Bengal — Bangladesh, India, Indonesia, Malaysia, Maldives, Sri Lanka and Thailand. The Programme plays a catalytic and consultative role: it develops, demonstrates and promotes new technologies, methodologies and ideas to help improve the conditions of small-scale fisherfolk communities in member countries. The BOBP is sponsored by the Governments of Denmark, Sweden and the United Kingdom, and also by UNDP (United Nations Development Programme). The main executing agency is the FAO (Food and Agriculture Organization of the United Nations).