June 2009

ECO-01 Business Organisation

Section-A

1. Attempt any four of the following:

(a) State the main features of partnership form of organisation.

Ans: The main features of partnership form of organisation are:

i) PIurality of persons; To form a partnership firm, there should-be at least two persons.. The maximum limit on the number of persons is ten for banking business and twenty for other types of business.

ii) Contractual relationship: Partnership is created by an agreement between persons called 'partners'. In other words, a person can become a partner only on the basis of a contract. This contract could be oral, written or implied.

iii) Unlimited liability: In respect of business debts, each partner has unlimited liability. This means that if the assets of the firms are not sufficient to meet the obligations of the firm, the partners have to pay from their private assets. The creditors can even realise the whole of their dues from one of the partners. Thus, all the partners are jointly and severally liable for all business debts and obligations.

iv) Good faith and honesty: A partnership agreement exists on good faith among the partners. The partners must be honest to each other and trust each other. They must disclose every information about the business and present true accounts to one another.

v) Restriction on transfer of share: A partner cannot transfer his share to an outsider without the consent of all the other partners.

vi) Existence of business: The purpose of the agreement among the partners is to do some lawful business and share profits. If the purpose is something other than business, it should not be treated as partnership.

vii) Profit sharing: There must be an agreement among the partners to share the profits and losses of the business of the partnership firm. This is one of the basic elements of partnership. If two or more persons jointly own some property and share its income, it is not regarded as partnership.

viii) Principal-agent relationship: The business of the firm may be carried on by all or one or more partners acting for all the partners. Every partner is entitled to take part in the operations of the firm.

(b) Enumerate the documents to be filed for the registration of a company. Explain briefly the nature and purpose of any one of these documents.

Ans: Documents to be filed for the registration of a company are :

- Memorandum of Association
- Articles of .Association

Memorandum of Association: It is the most important document of a company as it lays down the constitution of the company and states the relationship of the company with the outside world.

It is a public document and each person who deals with the company is supposed to know the provisions contained in the memorandum. The purpose of memorandum is to enable the shareholder, creditors and those who deal with the company to know what is its permitted range of activities. If a company is engaged in any trade or business which is outside the provisions of the Memorandum of Association, such acts are regarded ultra vires of the company and therefore, void and inoperative.

The Memorandum of Association contains the following particulars under different clauses.

i) Name of the company

ii) Name of the state in which the registered office is to be located.

iii) Objects clause-The nature of business activities which the company will undertake is to be stated in this clause.

iv) A declaration that the liability of' the members will be limited to the face value of shares subscribed.

v) Capital clause-The total amount of capital with which the company is proposed to be registered and its divisions into different shares of a fixed amount are to be stated under this clause.

vi) A declaration by signatories to the Memorandum that they are desirous of being formed into a company and agree to take the number of shares mentioned against their names.

(c)Distinguish between insurable risks and non-insurable risks.

Ans: Those risks which can be covered up by some type of insurance policy are called insurable risk. Whereas those risks which cannot be covered up by some type of insurance policy are called non-insurable risk.

Insurable risks are risks in which the insurance provider can calculate potential future losses or claims. Non-insurable risks are risks which insurance companies cannot insure because the potential losses or claims cannot be calculated.

The risk should be accidental or random in nature. The loss causing factor should not be within the control of the insured in the case of insurable risk. Risks due to war (except cargo at sea) and certain risks such as radio activity arising from nuclear fusion are non-insurable risk.

(d) Explain any five factors determining capital structure.

Ans: Factors determing capital structure are:

i) Nature of the business

ii) Characteristics of the company

iii) Management control

iv) Cost of finance

v) Effect of debt financing on the earnings per equity share

vi) Expected earning in relation to interest charges

vii) Availability of cash (cash flow)

viii) Flexibility of capital structure

i) Nature of the business: If a company is engaged in business activities in which sales are subject to wide fluctuations, it is desirable to have a smaller proportion of borrowed funds. Companies manufacturing televisions, refrigerators, machine tools and capital goods are normally subject to fluctuations in sales from time to time. On the other hand, companies dealing in essential consumer goods of daily use dr products having inelastic demand generally have stable earnings, and thus may depend to a greater extent on borrowed capital. Competitiveness among companies is also another aspect of business which may affect the level of earnings.

ii) Characteristics of the company: The size of a company as well as its credit standing also determines the extent to which equity or debt capital should be raised. Small firms have to depend more on owners' funds as it is difficult for them to raise long-term loans. This is because investors consider lending to small firms to be more risky. In contrast, large companies must make use of different sources of raising funds as no single source can meet their total financial requirements. Normally investors prefer to lend money to large companies as they believe that their money is safe and the risk is less with big business firms. Similarly, firms which enjoy high credit standing among investors and lenders are in a better position to raise long-term finance from different sources.

iii) Availability of cash (cash flow): The ability of a business to discharge its fixed obligations depends essentially on the availability of liquid cash. Profits earned may be adequate to cover the fixed charges arising out of debt, but the firm may not have sufficient cash to pay as the income gets continually invested in the form of more inventory, book debts or even purchase of equipment, particularly, if it is a growing concern. Hence, besides profitability, it is necessary to estimate the cash flows before deciding on the proportion of debt in the capital structure.

iv) Cost of finance: Since interest paid on borrowings is chargeable to profits before tax calculation, the cost of debt financing is inevitably lower than the expected rate of earnings (i.e., profitability) on equity capital. Hence, it is always beneficial to raise part of the total financial requirement through long-term loans. With lower cost of debt financing, the overall (average) cost of financing is reduced, and the return on equity capital is higher. This is one of the important determinants of the capital structure.

v) Flexibility of capital structure: The capital structure decision is usually made by management keeping in view their ability to adjust the sources of funds. The scope of changing the capital structure in future happens to be a basic consideration. For instance, in case additional funds are needed, a firm which is already financed with heavy debt may be forced to issue equity shares with a higher cost of finance involved. Or, again if funds raised are to be refunded on account of declining business, a firm may be unable to do so if it earlier relied heavily on equity capital. Indeed, to preserve operating flexibility, it is desirable that every firm should have unused debt raising capacity for future use. On the other hand, there should be a judicious mix of debt and equity capital so that refund of debt is possible when necessary.

(e) Explain the concept of preference shares and its advantages as a method of raising long-term finance.

Ans: Preference shares commonly known as preferred stocks, are those shares that enable shareholders to receive dividends announced by the company before receiving to the equity shareholders. Preference shares are released to raise capital for the company, which is known as preference share capital. If the company is going through a loss and winding up, the last payments will be made to preference shareholders before paying to equity shareholders. A company may issue redeemable preference shares and have the flexibility of paying off the amount if necessary and replace it by some other type of capital.

Sonie investors subscribe to preference shares because of preferential rights as to the payment of dividend and the return of capital. But others do not prefer it due to the fixed return as well as some risk of non -payment of dividend. Also they do not derive any benefit by way of rise in market price of the shares as is the case with equity shares.

Issue of preference shares is another method of raising long -term capital. Advantages of preference shares are:

- Dividend is payable on preference shares at a fixed rate and is payable only if there are profits. Hence, there is no compulsory burden on the company's finances.
- Preference shareholders do not have voting right. So, they cannot take part in the management of the company and thus are not a threat' to the promoters.
- The company can declare higher rates of dividend for equity shareholders in good years because the rate of preference dividend is fixed.

(f) What is speculation? State its merits.

Ans: The word 'speculation' is derived from the Latin word 'speculare' which means 'to see from a distance or take a decision in anticipation of future happenings'. However, in the share market, it means dealing in securities keeping in view the present and future prices with the object of making profits from the difference of the two prices. e. The stock exchange provides an arrangement for the marketing of listed securities which are also called 'scrips'. The actual functioning of this market consists of buying and selling of these scrips. The buyers buy scrips with the object of selling them in future at a profit, or sell now in the expectation of buying at a lower price in future. They are known as speculators and their transactions are known as speculative transactions. Speculation is based on foresight. In speculation the intention is to gain from difference in prices. The risk of loss is assumed and anticipated in speculation. Speculation is a rational activity, based on reasoning. Speculation is a recognised activity.

(g) How are the advertisements harmful to society? Explain briefly.

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

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

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

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

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

5. Some Advertisements are in Bad Taste: Another criticism against advertising is that some advertisements are in bad taste. These show something which in not approved by some people say advertisements showing women dancing when not required or running after a man because he is

wearing a particular suit or using a particular perfume are certainly not good. Some advertisements distort the relationship like employer employee and are quite offensive.

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

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

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

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

(h) Explain the nature and purpose of various types of warehouses.

Ans: There are three types of warehouses which provide facilities for proper storage of goods:

- Bonded warehouses: Bonded warehouses are those which are located in or near ports where imported goods are stored till importers fulfill all formalities and take delivery of them. When an importer is unable to take delivery of the goods by paying the required customs duty, the customs authorities permit the goods to be kept in a bonded warehouse, and allow delivery as and when the duty is paid. The bonded warehouses are licensed specially for storing imported cargo on which customs duty is yet to be paid. Goods stored in a bonded warehouse are said to be 'in a bond'. These warehouses are usually owned by Government, but can also be privately owned in which case they are subject to government supervision and control. Bonded warehouses enable importers to pay customs duty on the goods as and when it is convenient. The import duty is not required to be paid on the entire lot at the same time. Delivery of a part of the goods be taken on payment of the proportionate amount of duty. Besides, these warehouses also can provide services of branding, blending and packaging, thereby, facilitate reexport of the same. Moreover, buyers are allowed to inspect the goods there. Thus, importers can recover the amount of duty included in the price when the goods are delivered directly to the buyers.
- Public warehouses: Public warehouses are those which provide warehousing facilities to manufacturers, producers, as well as traders on payment of specified charges. These

warehouses are located at favourable sites on railway routes and highways and near ports. Public warehouses are privately owned by organisations, as well as by the central and state governments. Public warehouses run by dock authorities facilitate storing of goods which cannot be immediately shipped on reaching the port, or imported goods where importer is not able to take immediate possession. Mechanical handling of heavy goods is also possible at warehouses on railway routes and at ports. Small scale manufacturers and traders cannot afford to build warehouses of their own and can Transport and Warehousing make use of public warehouses located in different regions. The warehouses also provide the facilities of grading, blending and packaging. These warehouses also undertake loading and unloading of goods, and arrange delivery according to the owner's direction.

- Private Warehouses are owned by large manufacturers and wholesalers for storing goods of their own. The maintenance of these warehouses is the responsibility of the owners. These warehouses are not available to the traders and producers in general and hence have limited usefulness.

Section-B

Attempt any three of the following

2. Who is termed as an entrepreneur? Explain the role of entrepreneur in business promotion. (3+7)

Ans: An entrepreneur is one in whose mind the idea of doing business of a particular type first takes shape. An entrepreneur is one who creates something new, something different. He innovates and combines resources in the form of men, materials and money and brings them together to make the business venture profitable. entrepreneurship is the act of being an entrepreneur. The word entrepreneursthip is actually derived from the French term 'entrepreneur' which means to undertake, to pursue opportunities, to fulfil needs and wants of people through innovation and starting business.

He undertakes a venture, organises it, raises capital to finance it and assumes the whole or major part of the risk of business. Thus, 'entrepreneurship is the process of giving birth to a new business'. An entrepreneur must have imagination and also the ability to think creatively.

Risk bearing is another aspect of entrepreneurship that every entrepreneur has to cope with. One who is an entrepreneur must be a risk taker, not a risk-avoider.

Role of entrepreneur are:

i) Develops an idea and explores opportunities: The idea of forming n business unit is first formed in the creative mind of the entrepreneur. On the basis of the idea explores the prospects of starting Business Organisation a manufacturing enterprise.

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

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

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

v) Collects necessary capital: He makes available sufficient amount of capital for the initiation and continuation of the business. He gives personal guarantees to the financiers who contribute capital. Otherwise, he promises to invest capital himself or arrange the necessary amounts from friends and relatives.

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

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

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

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

The role of an entrepreneur is that of an initiator and promoter. In a sense, the role of an entrepreneur is also that of an expert having knowledge of product, market conditions and of the practical aspects of running a business. He should not be simply an imaginative thinker but also have the ability to judge what kind of business will click. His role is indeed crucial for the eventual success of a business. When an enterprise has been launched and it turns out to be profitable, the entrepreneur may decide to leave it, give up his ownership tights, and hand it over to others to run it. The basic responsibilities of an entrepreneur include the ability to seize an opportunity, to innovate, explore the, prospects of profitable business, and then to complete legal formalities, raise, funds and finally manage the business are the basic responsibilities 'of the entrepreneur. He has to face many obstacles, many problems and difficulties in the course of promoting business. He has to take decisions which may have long-run implications. An entrepreneur has thus to undertake many things. But the most important of these are: (i) innovation, and (ii) risk bearing.

3. What do you understand by the term ‘development bank’? Describe the functions of any three major development banks in India.

1. Ans: Development Banks: After independence a large number of financial institutions have been established in India with the primary objective of providing long-term financial assistance to industrial enterprises. Some of these institutions have been set up on the initiative of the Central Government, while others have been set up in different states on the initiative of the

concerned State Governments. Thus there are all-India institutions like Industrial Finance Corporation of India (IFCI), Industrial Credit and Investment Corporation of India (ICICT), Industrial Development Bank of India (IDBI), and Industrial Reconstruction Corporation of India (IRCI). They mainly provide long-term finance for large companies. On the other hand, at the state level there are State Financial Corporations (SFCs) and Industrial Development Corporations (SIDCs). These state level institutions mainly provide long-term finance to relatively smaller companies. These institutions (both national level and state level) are known as 'Development Banks' because their main objective is to provide financial assistance to industrial enterprises for investment projects, expansion or modernisation n of plants in accordance with the priorities laid down in the Five Year Plans. Financial institutions which provide long and medium-term finance to entrepreneurs and organisations so that funds are invested in industrial , ventures which are in conformity with national development plans. The objective of these banks is to serve public interest rather than earning profits. Development banks primarily aim to accelerate the rate of growth. It helps industrialization specific and economic development in general. A development bank does not accept deposits from the public like commercial banks and other financial institutions who entirely depend upon saving mobilization.

Any two major development banks in India are:

Industrial Finance Corporation of India (IFCI): This was set up in 1948 under the Industrial Finance Corporation Act, 1948. Its primary objective is to provide long-term and medium-te'rm finance to large-scale industrial concerns particularly when bank loans were not suitable or funds could not be raised from the capital . market by issue of shares. The IFCI deals only with industrial enterprises registered as limited companies or cooperative societies. Non-manufacturing concerns, private limited companies, partnership or sole traders cannot get assistance from this institution. It considers loan applications for amounts in excess of Rs. 30 lakh. It provides financial assistance for long-term investment in new industries or expansion or diversification of existing activities, or moderqisation and renovation of plant and equipment. The IFCI can grant loans or subscribe to debe'ntures issued by companies repayable in not more than 25 years. It can also guarantee loans raised from other sources or debentures issued to the public. Further, companies can secure loans in foreign currency from the IFCI or get such loans guaranteed by the Corporation. IFCI takes up the underwriting of the public issue of shares and debentures by companies.

Industrial Development Bank of India (IDBI): This was set up by Government of India in 1964 and is a subsidiary of the Reserve Bank of India. It seeks to cover the gaps left by the various institutions in the field of industrial finance. The IDBI can provide financial assistance to all types of industrial enterprises which are registered under the Companies Act or any other law. There is no restriction on the types of finance and the amount of funds that may be available from this institution. It has the unique role of not only providing financial assistance directly to industrial units, but also to refinance loans granted by other financial institutions. Further, it is required to coordinate the functions of all development banks, scheduled commercial banks and state cooperative banks as regards industrial financing. Thus, the functions of the IDBI include the following: i) It refinances (a) term-loans to industrial concerns granted by IFCI and other financial institutions repayable between 3 and 25 years; (b) loans repayable between 3 and I0 years given by scheduled banks or state cooperative banks; (c) export credit granted by specified financial institutions maturing between 6 months and 10 years. ii) It subscribes directly to the issue of shares and debentures made by industrial concerns. iii) It grants loans and advances to companies repayable between 8 to 10 years. iv) It guarantees loans raised by industrial concerns from the capital market or scheduled banks. v) It accepts, discounts and rediscounts commercial bills of exchange and promissory notes of industrial enterprises. vi) It undertakes underwriting of the public issue of shares and debentures made by companies. vii) To meet the financial requirements of large enterprises, the IDBI also arranges joint financing by two or more financial institutions, particularly when the amount and the risk involved happen to be too heavy for any single institution to bear alone.

4. Define stock exchange. Enumerate the factors affecting prices in a stock exchange. (3+7)

Ans: Stock exchange can be broken into two words- one is 'Stock' which means a part or fraction of the capital of a company, and the other is 'Exchange' which means a market for purchasing and selling. Stock exchange can be defined as a market or a place where different types of securities are bought and sold.

It not only deals in shares and debentures but also in various other types of securities issued by central, state and local governments as well as institutions like Unit Trust of India, Steel Authority of India, National Thermal Power Corporation, etc. Therefore, it is also called 'securities market' or 'securities exchange'.

This market is open only to members, most of whom are brokers acting as agents of the buyers and sellers of shares, debentures and bonds. The membership of the stock exchange is restricted to a certain number, and new members are admitted only when there are vacancies. Every member has to pay the prescribed membership fee.

Characteristics of stock exchange are:

1. Stock exchange is an organised market.
2. Securities (shares, debentures, bonds, etc.) issued by central, state and local governments, municipalities, port trusts, public utility concerns, joint stock companies and public corporations are bought and sold on the floor of a stock exchange.
3. In a stock exchange, transactions take place between members or their authorised agents on behalf of the investors.
4. In a stock exchange all transactions are regulated by the rules and bye-laws of the concerned stock exchange.

Factors affecting prices in a stock exchange are:

1. Interest rate: If there is a change in the rate of interest charged by banks on loans and overdrafts, there is a change in the speculative activities, and security prices also change as a consequence of it. Thus, if banks allow credit at lower interest rate, it may induce people to borrow money from banks and engage more in speculative activities to make profits. Hence, price of securities may go up as a result of speculative buying. However, if the interest on bank

credit goes up, borrowing will be reduced and demand for securities will be relatively lower. Hence prices of securities will tend to go down.

2. Activities of the financial institutions: When financial institutions start buying securities on a large scale, prices tend to move up because it leads to high expectation among the public about the prospects of the company and there is increased demand all around. Similarly, if there is large scale selling of securities by financial institutions, the price tends to go down.
3. Performance of the company: The prospects of a company as regards future profits and dividend payment are often reflected in the rising or falling prices of its shares. This is because the profit earning capacity and expected dividend rates influence the expectations of investors about the rate of return on investment and future rise in prices. If the prospects are good, there is increased demand for shares, and prices move up. On the contrary, if a company's performance in terms of profit earning and dividend payment allows an unsatisfactory trend, the price of its shares start declining due to reduced demand.
4. Business cycles: Business conditions are periodically found to be subject to prosperity and depression. Prices of securities continue to rise during prosperity as bull speculators are active and go on purchasing securities. However, when speculators are unable to meet their liabilities due to lack of adequate funds, they are forced to bargain for sale as a result of which prices rapidly decline and cause a state of depression in the market.
5. Changes in Board of Directors: Sometimes, security prices change as a result of changes in the Board of Directors of particular companies. The death or resignation of a well known director may cause doubt or apprehension about the future prospects of the company concerned. In that situation, generally, there would be an adverse effect on the price of shares of that company.
6. 6 sympathetic fluctuation: The prices of securities traded in more than one stock exchange often change due to changes in another exchange. If the prices of some I securities fall in one stock exchange due to some particular reason, it leads to a decline in the prices of the same securities in other exchanges too. This happens due to immediate communication among speculators.
7. Political events: Changes in the composition of government, changes in international relations, conflicts and political upheavals and wars between nations are always found to cause changes in the securities prices. This is because conditions of business and industry are generally affected by political events.
8. Changes in government policy: The changes in government policy with regard to taxation, import-export, price controls, licensing, etc. also influence the prices of securities, For example, if government decides to exempt dividends from income tax, the share prices will go up. If, on the other hand, government decides to raise income tax rates on company profits, the prices may fall. In fact, these days the policy changes by the government have become a major cause for an upswing or a downswing in prices of shares.
9. Miscellaneous factors: Various factors which may not be directly related with stock exchanges also affect prices of securities due to the psychological reaction of speculators. For example, unexpected changes in weather conditions, inadequate or excessive rainfall (which affects agricultural output), may bring about changes in the prices of shares of companies manufacturing fertilisers, edible oils, cotton textiles, etc. Similarly, lockout for a prolonged period may cause prices of shares to decline or illness of a powerful head of government may cause fall in security prices.

5. Explain briefly the features of an ideal advertising medium, and state the factors to be taken into consideration while choosing a suitable medium. (4+6)

Ans: Features of an ideal medium of advertising are:

1) Reach: The medium should be such as to reach the largest possible number of the target

audience.

2) Message: It should be possible to convey the message adequately through the medium.

3) Economy: The medium must be economical from the point of view of cost.

4) Flexible: It should provide flexibility of size, design, layout, colour, etc.

5) Scope of repetition: The medium should provide adequate scope for repeating the message, if necessary, at frequent intervals.

6) Effective: The use of the medium should result in achieving the goal of sales promotion.

The following factors influence the choice of media:

1) Character of the media:

The following aspects of the media are to be considered before choosing any particular medium.

a) The geographical coverage of the medium i.e., national, regional or local.

b) The, frequency and duration of exposure of the message to the audience.

c) Method of communication i.e., visual, oral, both visual and oral, etc.

d) Power of the ~medium to reach special categories of audience e.g., children, ladies, business executives, etc. This is also called audience selectivity.

e) Scheduling flexibility is another factor. Producing a TV advertisement takes more time than producing a newspaper advertisement. Similarly, withdrawal of advertisement with a short notice is not possible with some media.

f) Production quality of the media.

g) Degree of permanence or durability in the sense that how long the advertisement can remain before prospective customers eyes or within their grasp. A TV advertisement disappears within a few seconds whereas a hoarding continues delivering the same message to the passing public for a year or more.

2) Nature of the product to be advertised: Consumer goods need to be advertised with different types of appeal for effectiveness. Familiar goods of daily consumption do not require elaborate description, while industrial machinery may require technical details to be explained. The size of advertisement and the time of exposure required vary according to the

nature of the products. Again, advertisement for consumer goods can reach the largest possible number of people through mass media like newspapers, radio and television. But industrial goods may be more effectively advertised through trade and technical magazines. Advertisement of garments is best done in multi-colour printing in magazines.

3) Type of audience: Media habits of the target audience to be reached is one of the important factors to be considered while selecting the medium. If the target audience are illiterate, press medium (newspapers and magazines) is ineffective. Similarly, if the target customers are in villages where there are no TV sets, advertising by TV is a waste. The most effective medium to reach housewives in the urban areas may be the radio or television, and for- business executives it may be a professional magazine. Therefore, the characteristics of the target customers with respect to media are very important in selecting proper medium.

4) Coverage: How many and what percentage of the potential buyers can be approached through each possible medium are also determining factors in the choice of a medium. One medium may be able to reach more number of target customers than the other media. Therefore, n medium which can reach the maximum number of target customers should be preferred. For instance, if target audience are illiterate and do not have TV sets, short films in the cinema halls may be more effective. Similarly, the number of doctors who can be reached through direct mail is expected to be more than the number who can be reached through any other medium. To advertise sewing machines to the urban customers, women's magazines may be more appropriate as the appeal will reach many more ladies through this medium.

5) Cost: The most important factor determining the choice of a medium is the cost involved. Cost of a medium may be analysed in two ways: 1) absolute cost, and 2) cost related to audience size. Absolute cost is the actual charge for buying a certain amount of time or space in a medium. If the small firm had set aside a small amount for advertising, it cannot afford to use an expensive medium. For instance TV is a very expensive medium whereas newspaper advertising is relatively cheaper. However, what is important is not the absolute cost of using each medium but the size of the target, audience reached in relation to the cost. Relative cost is a comparative cost. It is the absolute cost related to the size of the audience served by the chosen medium.

6. What is meant by business risk? Explain the main causes due to which business risk may arise. (3+7)

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

Business risks arise due to a variety of causes, which are classified as follows:

(i) Natural causes: Every business firm is confronted by potential loss to its property and personnel through common perils such as fire, explosion, wind storm, flood, theft, business liability damage suits, earth quake and death or disability of its personnel. These perils may cause direct loss by damaging property or killing personnel. Losses may occur to business from the occurrence of some of these perils. Natural calamities like flood, earthquake, lightning, heavy rains, famine are beyond human control. They result in heavy loss of life, property and income.

(ii) Human causes: Human causes include unexpected events like carelessness, negligence or dishonesty of employees, stoppage of work due to power failure, strikes, riots, management inefficiency.

(iii) Economic causes: These include uncertainties caused due to economic fluctuations such as changes in demand for goods, competition, price, a collection of dues from customers, increased cost of raw materials and labour, government policies, market regulations, increasing interest rates, change of technology or method of production. Financial problems like rise in interest rate and higher taxation also come under economic causes as they raise the cost of operation of business unexpectedly.

(iv) Financial causes: All business firms borrow money and also extend credit to customers. There is always scope for loss from both credit received as well as credit extended. Bad debts due to insolvency of customers is a continuous problem in business. Similarly, creditors like banks and financial institutions may fail or cancel the loans due to bad business conditions. This can cause financial loss to the firm due to curtailed operations. Similarly, unexpected rise in interest rates on bank loans may reduce profits. Business firms investments in stocks and bonds always face risk.

(v) Production causes: Manufacturing enterprises face the problems such as production losses due to breakdown of machinery, defective products due to faulty machinery or poor quality of raw material, under utilisation of installed capacity, inventory buildup to levels much higher than current demand, improper plant layout, uneconomical plant capacity, etc. Such production risks may be minimized by careful planning.

(vi) Marketing Risks: Marketing activity includes all those business activities necessary to move goods from producers to consumers. The major functions include buying, selling, transportation and storage. Activities like standarization, market information and research are also other important functions of marketing activities. There is an element of risk in all these activities. For instance, you may not be able to sell your products at the prices you want. Due to market conditions, you may be forced to sell at lower prices and incur losses. Similarly, due to sudden spurt in the raw material prices, your cost of production may go up and you may incur losses. Goods may be stolen, damaged or destroyed in transit from perils for which the transporter is not - liable. Similarly, improper facilities for storage may cause unexpected losses. Normal perils such as fire, floods, storm, explosion, theft, etc., can cause extensive damage to goods in the storage. For instance, the fire due to electric short circuit may cause extensive damage to the goods in the storage.

Or

Discuss the merits and limitations of public corporation as a form of organisation for public enterprises.

Ans: Merits of public corporation are:

i) Initiative and flexibility (Autonomous set-up): As it is autonomous corporate body set up under an Act of Legislature, it manages its affairs independently with its own initiative and flexibility. There is great flexibility in terms of a public corporation’s operations. It experiments in new lines, exercises initiative in business affairs and enjoys the operational flexibility as in private enterprises.

ii) Avoids red-tapism: The evils of red-tapism and bureaucracy associated with departmental form of organisation are avoided. Business functions cannot be carried out efficiently in a government set-up, which is marked by rules, regulations and procedures. Compared with a departmental organisation a public corporation can take quick decisions and prompt actions on any matter affecting its business.

iii) Easy to raise capital: Public corporations are government owned statutory bodies. They can easily raise required capital on their own whenever needed by floating bonds at relatively lower rates of interest. Public also comes forward to subscribe to such bonds since they are safe.

iv) Protects public interest: Compared to a departmental organisation, a public corporation is relatively free from political interference, parliamentary enquiry and departmental checks and controls. Although it has a considerable degree of administrative autonomy, its policies are subject to parliamentary control. Thus, it ensures protection of public interests. Further, the Board of Directors of the public corporations consists of persons from various fields such as business experts and the representatives of special interests like labour, consumers, etc., who are nominated by the government. Thus, exploitation of any class at the cost of another is r'uled out.

v) Works with service motive: Public corporation avoids the defects of profiteering, exploitation, illegitimate speculation, etc., which are often associated with private enterprises. A public corporation works primarily with service motive and profit Forms of Organisation in earning is only a secondary consideration. Though it works efficiently to show good Public Enterprises results in the form of 'surplus,' such surplus must not be the result of exploitation. The surpluses generated by the public corporations are used for the good of the consumers and the community.

vi) Secures working efficiency: It secures greater working efficiency by providing better amenities and more attractive terms of service to its employees which in turn; reduces the labour problems.

vii) Secures benefits of large scale economies: Economies of large scale operations are realised by the virtue of increased size and scale of the business. Further, it is easy to reap considerable economies in management by affecting the integration of several companies under this form. For example, giant government undertakings organised as autonomous units such as, banking, insurance, transport, etc., can secure better management and staff with comparatively lesser costs.

Limitations of public corporation form of organisation :

i) Less autonomy: Compared to departmental form, public corporations enjoy more autonomy. But, in practice, the autonomy of public corporation is closely and systematically controlled by the government even in matters where they are supposed to have freedom. For example, the Food Corporation of India and the Electricity Boards in various States (these are statutory corporations) are of important to the government and to the public at large. But, the Central and State Governments often find it difficult to allow them the freedom which they are entitled to as per their Acts.

ii) Inflexibility: A public corporation is set up by a special Act of legislature. Any change in the objects and powers of the corporation requires an amendment in the Act by the legislature. This tends to make a corporation inflexible and insensitive to changing situations.
iii) Clash amongst divergent interests: As you know, the corporations are owned by the government and are managed by a Board of Directors appointed by the government. When the Board of Directors represent different interests there may be clash of interests. This in turn, may hamper the smooth functioning of the corporation. Sometimes, the directors may abuse their autonomy and authority by indulging in undesirable practices. This would defeat the social objectives of public corporation.
iv) Ignores commercial principles: Public corporations do not have to face any competition. They are neither guided by profit motive nor haunted by the fear of loss. . Therefore, there is a possibility of ignoring commercial principles in their working. This may ultimately lead to inefficiency and losses to the corporation. The losses, thus arising are met by the government through subsidies.
v) Excessive public accountabili6: You know that the public corporations work with the service motive rather than profit motive. This public accountability of the corporation sometimes acts as a stumbling block in the operational efficiency of the enterprise.

7. Discuss the various aspects of price policy of public utilities.

Ans: Price of a commodity is usually determined by two factors: 1) demand, and 2) supply. This does not apply in the case of all goods and services supplied by the public utility undertakings. There are other considerations which play a more important role in fixing the price. In the case of public utility concerns, price is not fixed on the basis of cost involved in the production or supply of such services i.e. cost of service principle. It is determined on the basis of the purchasing capacity of the consumers, which is called the principle of what the traffic will bear.

The goods and services provided by public utility concerns are essential services or goods. These products or services are used by the poor and the rich alike. The rich can pay higher price to avail of these services, while the poor may not be able to pay for it if prices are fixed on cost basis. Hence the government takes care of and safeguards the interests of the poor by regulating the prices of such goods and services so that the poorer people may also be able to use them. Consumer will pay a fair price. Determination of a fair price involves a number of considerations like cost of production, cost of supply, a reasonable rate of profit, paying capacity of the customers, changes in the general price level, and so on. Thus, price determination is not a simple matter. It is to be determined after due consideration and consultation with various interests. However, the following three broad aspects of the price policy of public utility undertakings can be kept in mind.

i) Promotional aspect: This aspect is concerned with the promotion of demand of the services provided by the public utility undertakings. Promotional aspect refers to increasing demand for the products or services. Promotion of demand is necessary to ensure full utilisation of the production capacity of the undertaking. This helps in spreading the overhead costs over large output. For example, transport services such as roadways and railways issue monthly tickets (Season tickets) as a concessional rate to a large number of regular passengers.

ii) Price discrimination: The demand for the products of a public utility undertaking is elastic in some markets and inelastic in other markets. For example, in the case of transport services, general public or tourists demand for bus service is elastic (they do not solely depend on public buses, they may also hire auto or taxi). The demand for bus among regular office-goers or students is inelastic (they mainly depend on public buses only. Here the undertakings have to charge less from the students and officegoers, and more from the tourists and the general public. In some cases, public utilities can demand lower price in one market and higher price in others, or may charge lower price from one category of consumers and higher price from the other category of consumer.

iii) Social considerations: Some of the public utility undertakings touch everyday life of the people and are "affected with public interests". In such cases the price of the product is not fixed purely on economic basis. Considerations of social welfare play an important role in the price fixation, Consumers with low incomes or poor people get the services at concessional or subsidised rates.