

**COURSE
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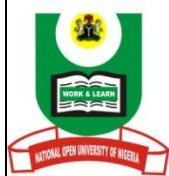
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ADVANCING MANAGING SMALL ENTERPRISES (ENT809)

INTRODUCTION

The course Advancing Managing Small Enterprises (ENT809) is a core course which carries two (2) credit units. It is prepared and made available to all Postgraduate students in Entrepreneurship Programme, in the Faculty of Management Sciences/Department of Entrepreneurial Studies. This course is a useful material to you in your academic pursuit as well as in your workplace as managers and administrators.

WHAT YOU WILL LEARN IN THIS COURSE

The course is made up of sixteen (16) units, covering areas such as:

- Description of Small Business and Entrepreneurship
- Pathways to owning a Small Business and characteristics of Small Business enterprises
- Approaches to innovation in small businesses
- Differences between traditional and entrepreneurial businesses
- Basic concepts of Management
- Strategic management and corporate entrepreneurship
- Management principles and management functions
- Marketing strategy and planning – definition of planning, importance of planning forms/kinds of planning and illustrate the flow of planning

decision in a small business organisation master plan, role of marketing in small business organisation,

- Differentiating strategy, marketing strategy, strategic marketing and managerial marketing.
- Nature of the Marketing Mix- Price, Product, Place and Promotion
- Risk taking in Business
- Market analysis in selection of market posture, coordination and control of business activities strategy revision and continuity psychological barriers to marketing strategy planning
- Communication skills in business
- Sources of information – definition internal and external source of information (Federal government and its agencies, state and local government as external sources of information
- Elements of an information system, advantages and procedures involved in developing records retention programme, uses of some information tools such as manuals, reports and forms,
- Ratio analysis and the limitations of ratio as a tool; budgeting and breakeven analysis – definition, budgeting process problems of budgeting preparation, kinds of budgets and the importance of budgets administration;
- Illustrate how Break-Even chart is constructed, changes associated with the chart as any of the variables change.

The Course Guide is meant to provide you with the necessary information about the course, the nature of the materials you will be using and how to make the best use of them towards ensuring adequate success in your programme as well as the practice of small business management in the society. Also included in this course guide is information on how to make use of your time and information on how to

tackle the tutor-marked assignment (TMA). There will be tutorial sessions during which your facilitator will take you through your difficult areas and at the same time have meaningful interaction with your fellow learners.

COURSE AIMS

The main aim of this course is to equip you with adequate information on the concept and nature of small scale business enterprises, its characteristics, managing small scale enterprises, and its roles in an economy. The course also aims at making you have a greater understanding of the small business management.

OBJECTIVES

At the end of this unit, you should be able to:

- Describe Small Businesses and Entrepreneurship
- Explain the pathways to owning a Small Business and characteristics of Small Business enterprises
- State the approaches to innovation in small businesses
- Differentiate between traditional and entrepreneurial businesses
- Understand the basic concepts of Management
- Elaborate on strategic management and corporate entrepreneurship
- Apply the management principles and management functions in business
- Discuss the marketing strategy and planning – definition of planning, importance of planning forms/kinds of planning and illustrate the flow of planning decision in a small business organisation master plan, role of marketing in small business organisation,

- Differentiating strategy, marketing strategy, strategic marketing and managerial marketing.
- Understand the Marketing Mix- Price, Product, Place, Promotion, People, Process etc.,
- Outline risk taking in Business
- Explain market analysis in selection of market posture, coordination and control of business activities strategy revision and continuity psychological barriers to marketing strategy planning
- Expatiate the communication skills in business
- Discuss the sources of information – definition internal and external source of information (Federal government and its agencies, state and local government as external sources of information
- Comprehend the elements of an information system, advantages and procedures involved in developing records retention programme, uses of some information tools such as manuals, reports and forms,
- Develop the ratio analysis and the limitations of ratio as a tool; budgeting and breakeven analysis – definition, budgeting process problems of budgeting preparation, kinds of budgets and the importance of budgets administration;
- Illustrate how Break-Even chart is constructed, changes associated with the chart as any of the variables change.

Course Materials

Major components of the course are:

- Course Guide
- Study Units
- Textbooks
- Assignment Guide

STUDY UNITS

There are three modules of 16 units in this course, which should be studied carefully.

MODULE 1

- Unit 1 Description of Small Businesses and Entrepreneurship
- Unit 2 Pathways to Own a Small Business
- Unit 3 The Feasibility Study Plan
- Unit 4 Managing Small Scale Businesses
- Unit 5 Management of SMEs

MODULE 2

- Unit 6; Strategic Management and Entrepreneurship
- Unit 7; Strategic Marketing and Marketing Strategy
- Unit 8; Strategic Marketing Planning Process
- Unit 9; Marketing Mix: Pricing Policies
- Unit 10: Marketing Mix: Products
- Unit 11: Marketing Mix: Place (Channels of distribution)

MODULE 3

- Unit 12: Essential Information on Buying and Selling
- Unit 13: Sources of Information and Effective Communication
- Unit 14: Elements of an Information System
- Unit 15: Budgeting and Ratio Analysis
- Unit 16: Break-Even Analysis and Chart

ASSIGNMENT

There are many assignments in this course and you are expected to do all of them by following the schedule prescribed for them in terms of when to attempt them and submit same for grading by your Tutor.

TUTOR-MARKED ASSIGNMENTS

You are expected to submit all the TMAs to your Tutor for grading on or before the stated deadline. If for any reason you cannot complete your assignment on time, contact your tutor before the assignment is due, to discuss the possibility of extension. Extension may not be granted after the deadline, unless on exceptional cases. The TMAs usually constitute 30% of the total score for the course.

FINAL EXAMINATION AND GRADING

At the end of the course, you will write the final examination. It will attract the remaining 70%. This makes the total final score to be 100%.

SUMMARY

This course Advancing Managing Small Enterprises (ENT809) will expose you to issues involved in small business management and entrepreneurship. On the successful completion of the course, you will have been armed with materials, expertise and skills necessary for efficient and effective management of a small business enterprise in relation to the cooperative society.

MAIN



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- Unit 3 : The Feasibility Study Plan
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MODULE 2

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- Unit 7: Strategic Marketing and Marketing Strategy
- Unit 8: Marketing Mix: Pricing Policies and Strategies
- Unit 9: Marketing Mix; Products
- Unit 10: Marketing Mix: Channels of Distribution
- Unit 11: Marketing Mix: Promotion and Personal selling

MODULE 3

- Unit 12: Essential Information on Buying and Selling
- Unit 13: Sources of Information and Effective Communication
- Unit 14: Elements of an Information System

- Unit 15: Budgeting and Ratio Analysis
- Unit 16: Break-Even Analysis and Chart

UNIT 1 DESCRIPTION OF SMALL BUSINESSES AND ENTREPRENEURSHIP

CONTENT

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3.0 Main Content

3.1 Description of Small Businesses

3.2 Distinction between traditional and entrepreneurial small businesses

3.3 Innovation in Micro, small and medium enterprises

3.4. Entrepreneurship intensity

4.0 Conclusion

5.0 Summary

6.0 Tutor-marked assignment

7.0 References/Further Reading

1.0 Introduction

In this unit, our focus is on clear understanding of micro, small and medium enterprises as well as distinguish them as either entrepreneurial or traditional. This distinction will properly guide our thoughts especially in introducing innovation into the small businesses. There is a need to comprehend the extent an innovation will reach to be able to affect the economy of a nation. Hence, this unit will lead us into all these contents.

2.0 Objectives

At the end of this unit, you should be able to;

- Describe Nano, Micro, Small and Medium Enterprises (NMSMEs)
- Differentiate between Traditional and Entrepreneurial firms
- Understand Innovation in Small Business Enterprises
- Measure the intensity of entrepreneurship in a small business.

3.0 Main Content

3.1 Micro, Small and Medium Scale Enterprises

These businesses are normally privately-owned companies, partnerships, or sole proprietorships. Small businesses are common in many countries, depending on the economic

system in operation. Typical examples include convenience stores, other small shops such as a bakery or confectionaries, hairdressers, tradesmen, solicitors, lawyers, accountants, restaurants, guest houses, photographers, small-scale manufacturers etc. Small businesses are usually independent. The small businesses, often located in private homes, are called micro businesses operated with few (or no) employees other than the owners. Micro, Small and medium businesses have no standard definition globally. Different bodies have different definitions, but the usual proxies are number of employees, annual sales/turnover, working capital, profitability, and total assets in particular.

Specific to our context, in the past in Nigeria, there used to be various definitions. For instance, the Central Bank of Nigeria (CBN), The Small and Medium Industries and Equity Investment Scheme (SMIEIS) and even certain industries had their definitions. By 2015, there was a national policy on classification of MSMEs in Nigeria that gave a unified outlook which becomes the standard in Nigeria. Small and Medium Development Agency of Nigeria (SMEDAN) National policy on MSMEs (2015) and National Survey of Micro, Small and Medium Enterprises (2017) postulated the Micro, Small and Medium Enterprises MSMEs. However, the National Policy was reviewed to maximize its employment generation, wealth creation, poverty reduction and contributions to economic growth. By 2021, this policy was launched. The new classification of the MSMEs in Nigeria as laid out in the revised National Micro, Small and Medium Scale Enterprise Policy (2021-2025) is as follows:

Table 1: MSMEs Description

S/N	Enterprise/ category	Employment size	Turnover(Nm)
1	Nano/Homestead	1-2	Less than 3
2	Micro	3-9	3-25
3	Small	10-49	25+ but less than 100
4	Medium	50-199	100+ but less than 1000

Source: Review of National Policy on MSMEs in Nigeria (2021)

Any ones beyond these figures are large scale organizations. This is the current and national standard for MSMEs in Nigeria. It is subject to review every five years to facilitate an exciting NMSMEs subsector as main players in national economic growth and employment drive.

There has been argument that business people may not be accurate with the assets declaration and valuation. SMEDAN (2017) asserted that where there is a conflict of criteria in classification,

employment based/ number of employees will take pre-eminence. It is easier to know the number of staff at the finger tips than total assets. Second, the matter of insecurity in the nation makes everyone a suspect. The fear of robbery and abduction may make it difficult for a business owner to divulge the actual value of his total assets. Third, many MSMEs owners try to evade tax, thus, they avoid releasing the true assets figure. Lastly, the economic depression and high inflationary trend in the country inflates the asset worth, making the owner to appear to be what he is not. Against this backdrop, focusing on number of employees to classify the MSMEs seems a better idea. Moreover, when discussing the relative terms of small and large businesses in this module, both micro and small businesses may sometimes be referred to as small firms or small businesses.

3.1.1 Wrong opinions about entrepreneurship and small businesses

There are different views ignorantly held as entrepreneurship that makes the understanding to be unclear. It is not possible to call pawpaw fruit as coconut fruit and get coconut oil extract benefit. If the perception is wrong, the result will be wrong. Suffice to say, that everybody is in business of buying and selling. Someone may sell product like medicine, clothes etc. while some persons like medical doctor, teacher, security etc. sell services. You will see that not everyone in business is an entrepreneur. Let us have more clarifications.

Entrepreneurship is not vocational education, business studies, skills acquisition, technical work or craftwork. It is neither all about self-employment, proprietorship, petty trading, nor zealous trading. It is more than mere starting a business or buying and selling. It is not about titans or merchants in oil and gas, cargo and others without any value-addition. It is not about motivational speaking, training or seminar organization. It is not synonymous to small business owners or any Small and Medium Enterprises (SMEs) among others. Entrepreneurship is not a life-long title like chieftaincy or Doctor. To maintain being an entrepreneur, the entrepreneurial activities must be regular. As soon as a business or individual stops innovation, or stops being entrepreneurial, or its innovation has become common and taken over by others. Such business is no more entrepreneurship (Kuratko 2010) but has become a normal business. In summary, these perceptions can only be called entrepreneurship if there is a substantial value addition, introduction of novelty and uniqueness that is different from the norm known and done by everybody. Although, a skill acquisition may not be entrepreneurship but can be a stepping stone to entrepreneurial activities. The non-entrepreneurial businesses are owned by small business owners while the entrepreneurial ventures are owned by entrepreneurs.

3.2 Traditional businesses or Entrepreneurial businesses

Firms can be generally categorised into traditional and entrepreneurial (Megginson et al, 2003). Both create businesses for the general public, have the drive for profit and effective business model. However, on one hand, a traditional business is usually independently owned and operated but not prominent in its field and not involved in any **intense innovative** practice. On the other hand, a entrepreneurial business is involved in high level of innovation, desire for profit and growth (SBA, 2009). Any business that emphasized on continuous high-level innovation is entrepreneurial.

Consequently, Megginson et al. (2003) proposed that traditional small businesses create business with existing characteristics, contented with their size, ordinarily managing and maintaining the businesses, expecting normal sales, profit and growth with a degree of freedom and financial independence while entrepreneurial businesses create new and innovative firms, characterized by innovative strategic practices and/or products with the principal objective of profitability and grow company to new heights (Henrekson and Sanandaji, 2017; Adeyeye, 2018).

Certainly, micro and small businesses are outstanding vehicles to channel individuals' business initiatives and entrepreneurial behaviour and aspirations. Majority of the so-called entrepreneurial activities in Nigeria are mainly proprietorial activities, a way out of poverty, self-sustenance and personal consumption. This solves a partial economic problem of the proprietor being employed and a fractional part of the unemployment problem by offering employment to a few others (Adeyeye et al., 2019). Scase and Goffee (1982) drew attention to the fact that only a minority of small business owners can be considered 'entrepreneurs' in the classical sense. The small businesses are an expression of the individuals in charge, thus, firms that accommodate and convey the individual's high-level entrepreneurial activities to the marketplace are entrepreneurship as distinguished from traditional small firms (Carland et al., 1984, Adeyeye et al., 2018) that are proprietorship. The core of entrepreneurship is innovation. However, it should be noted that whether a traditional firm, or entrepreneurial firms, every MSMEs must be managed well to achieve the organizational goals and endeavour to be innovative to be competitive and also affect the economy of the nation.

3.3 Place of innovation in small businesses

Innovation literally means renovation or variation. It is the successful implementation of creativity within an organization. Innovation is deviating from the norm, and doing it in a new and different way to make life better for the populace. Hellriegel, Slocum and Jackson (2005) also described innovation as the process of creating and implementing a new idea, which can take different forms.

At the core of Schumpeter's theory of entrepreneurship is the concept of 'innovation', through which he initiated a strong connection between entrepreneurship, technological development and economic progress (Schumpeter, 1996). He identified five dimensions of innovation as new 'combinations of the factor of production' by an entrepreneur in reforming the pattern of production by any of the following:

- 1) *Introduction of new or improved products/services (Product innovation);*
- 2) *Introduction of new or improved methods of production (Process innovation such as mechanized or electrical equipment instead of a manual process);*
- 3) *Opening of new market (Market innovation);*
- 4) *Identification of new sources of supply of raw materials (Resource innovation e.g. biofuel); and*
- 5) *Creation of new ways of organizing businesses (Organizational innovation).*

Any form of entrepreneurship will automatically fall into any of these dimensions of innovation.

Wealth is created when such innovation results in new demand. Entrepreneurship is, therefore, the introduction of a new activity into the economy in order to improve the standard of living of the people and also earn an entrepreneurial profit. After identifying the dimension to which the innovation falls, there is need to consider the different approaches to innovation.

3.3.1 Approaches to Innovation in a small business

A firm that does not innovate will die (Kuratko, 2012) due to other competitors in the industry. A firm can be innovative after being categorized into Schumpeter's dimensions of innovation in four specific ways as discussed.

Invention or radical innovation / revolutionary innovation / discontinuous innovation / breakthrough innovation/ disruptive innovation: These terms are synonyms. It is the introduction of a new product that are usually a result of new technology. This product or service addresses a gap that has never been addressed before. An untried technology that is new to the world, and will change the customers' ways of dealing with the issue. Example is airplane.

Dynamically continuous innovation or synthesis: This is still part of Schumpeter's dimension on the introduction of an improved product/service. It is the improvement of the existing product/service by combining two or more features together as one. Example of such is a rechargeable fan.

Incremental innovation or continuous innovation / a step-at-a-time innovation/ extension: This is an improvement on an existing product by adding a feature to make it different from others. Example Coca cola bottling company production of 50cl soft drinks aside the 35cl.

Duplication or imitation: This is replicating or copying/ adapting/ mimicking the innovation of other forms. Example is Sony technology imitating Philips to produce refrigerator. Sometimes, such a

product can be introduced to the same market where the original exist or taken to another new market entirely.

The first two (that is, number i and ii) are highly entrepreneurial because of the high degree of innovativeness, risk-taking and proactiveness which can significantly affect the national economy positively. Whilst number iii and iv are low entrepreneurially and the impact on the economy might not be significant. Note, Innovation must be accepted in the marketplace before it can be called innovation.

3.4 Intensity of Entrepreneurship

This is the evaluation of the overall strength of entrepreneurship in a small business, the degree and frequency. In other words, the level and regularity, which equation is, **Degree X Frequency = Intensity**. For instance, moderate levels means the degree and frequency are periodical. This is very important in evaluating an individual, firm or industry as entrepreneurial. Before any innovation can be considered entrepreneurial, the intensity must be known. A change of the shape of bread is an extremely low innovation that cannot affect the Gross Domestic Income of a country. The impact is quite insignificant. For instance, Femtech companies with the various introduction of technological are entrepreneurial because of their breakthrough innovations and the frequency. It is only such entrepreneurial firms that can generate adequate wealth, create job, pay taxes and affect the individual's and national economy (Kuratko, Morris & Covin (2020) & Adeyeye (2018).

3.4.1 Degree of Entrepreneurship

Every organization, no matter how conventional, has an element of entrepreneurial behaviour. It is not enough to say, for a venture to be categorized as entrepreneurship, there must be innovation. For instance, a change in the shape of the soap mould is an innovation, and a change in the perfume added to a cream is innovation. How would you rate the degree of this innovation? How significant are the contribution of these changes to the GDI of a nation? It is insignificant and very low.

Thus, to assess the extent or degree of entrepreneurship of a particular product or service, these three combinations must be considered. The **innovativeness**, **risk-taking** and **proactiveness** which must be considered on the level of high, medium and low. Innovativeness is concerned with the type of innovation that is being engaged with. Is it a disruptive innovation or duplicate? **Risk-taking** is about the level of risk or uncertainty attached to the innovation. The calculated likelihood of loss or failure. Will it be easily accepted in the market? How long will it take people to accept the product or service? How about the payback period? These and others are the risks involved. Note that the higher the innovation, the higher the risk. Lastly, the level of **proactiveness**, which is action-oriented. This concerns the level of the activity or product in acting on the environment rather than reacting to the

environment. The ability to get to the market before other competitors, as one of the market pioneers or industry leaders. It is the desire that focuses on exploitation of the opportunity and taking responsibility on bringing innovation to reality. The combination of these three: **Innovativeness X Risk-taking X Proactiveness = the degree of entrepreneurship** of a firm. The degree can be low, moderate or high. Low level of entrepreneurship has no impact on the economy.

3.4.2 Frequency of Entrepreneurship

This expresses the regularity of entrepreneurship in a firm. The number of times entrepreneurial events takes place within a firm over a given period of time. A firm that does not innovate regularly is not an entrepreneurial firm. It is just a traditional business. Low frequency means less entrepreneurial initiatives. Thus, small businesses must desire to be innovative for profitability, sustainability and contribution to economic growth.

4.0 Conclusion

Nano, Micro, Small and Medium enterprises has been standardized in Nigeria, unlike the days various industries and parastatals had their definitions. Small businesses can either be traditional or entrepreneurial. It takes small business to become innovative to be entrepreneurial. Schumpeter's dimension of innovation was highlighted while the different approaches were expressed. However, the impact of a small business innovation on the economy can only be measured by its intensity, that is, the degree and frequency of innovation.

6.0 Tutor-Marked Assignment

- i. Are all small businesses entrepreneurship. Discuss.
- ii. Enumerate the different approaches to innovation?
- iii. How would you measure the intensity of innovation in a small business organisation?
- iv. What are the unique contribution of small businesses?

7.0 References/Further Reading

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UNIT 2 PATHWAYS TO OWN A SMALL BUSINESS ENTERPRISES

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- 2.0 Objectives
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1.0 INTRODUCTION

In the previous unit, we clearly described a small business organisation. This unit contains information related to the pathway in taking the right decision to own a business organisation.

2.0 OBJECTIVES

At the end of this unit, you will be able to:

- explain the motivations to own a small business
- identify the characteristics of small business
- Understand the steps in starting a business
- Know the forms of business ownership

3.0 MAIN CONTENT

3.2 Motivations to own a Small Business

Becoming the owner or an entrepreneur of a small business is a great decision to make. They are the promoters of small businesses whose motivations could be triggered by negative or positive reasons to start a small business. Some small businesses are started by people who are unemployed, dis-employed, mis-employed, under-employed or unhappy in the work place. Thus, personal, family or peer pressure to start a business and be self-employed comes up as the last resort. Some started on a full time basis while some on part-time to earn an extra income to support their needs and might never grow beyond the simple beginnings. Sometimes, the owners may be content with small-scale operations and not want to get any larger. Speaking in the language of entrepreneurship such people are referred to as ‘necessity-driven entrepreneurs or necessity –driven business owners’. They are described as “man-must-live” or “last resort” entrepreneurship. The motivation is negative in nature and sometimes referred to as “push

factor”. It is the entrepreneurship that an individual undertakes out of need, poverty, unemployment, under-employment, pressure from families and friends, or other social disasters, when all other options are absent or unsatisfactory among others (Adeyeye, et al. (2019). In anyway, such individual has solved the unemployment problem by getting self-employed and perhaps few others with them.

Still, others begun small businesses for the sheer challenge or innovativity involved while some have developed a product or service that can be produced and sold only in a new business set up. Historically, many such businesses have evolved into large corporations, providing employment opportunities for many other people. These are Opportunity-driven entrepreneurship, it is the opposite of necessity-driven entrepreneurship. It is the entrepreneurship that an individual chooses to dive into because of his traits, skills, interest, and knowledge or identified opportunity. It has positive influence by nature and sometimes referred to as “pull factor” (Adeyeye, Aliu, Oni, & Onimisi, 2019). Sometimes, such an individual may abandon the juicy and well-paid employment to face entrepreneurial activities in order to exploit a perceived business opportunity, independence or to fulfil life ambition.

However, as the economy improves, the necessity-driven entrepreneurship gives way and becomes opportunity-driven entrepreneurial activity. Global Entrepreneurship Monitor (2017) reported that Opportunity-driven entrepreneurs are more dominant in high-income countries while necessity-driven are more in low-income countries (See GEM annual report for statistics). One common ground is that both are improvement-driven and has created job in one way or the other.

In the Nigerian economy and in all other economies, small businesses litter the economic landscape, generating most new private employment opportunities for people and contribute significantly to economic development.

Characteristics of Small Business

The characteristics of a small business vary from one place to another but there are few similar features related to a small business. Some prominent features are highlighted:

Ownership structure

Ownership structure can be used to distinguish between a small business and a large one. A business owned by an individual, as a sole proprietorship or as partnership (two or more people combined to form a partnership) or family business can be categorised small. At a higher level, it can be run as a private limited liability (tagged as “Ltd” companies) concern with private

shareholders as foundation owners. Whilst at a much higher level, a private limited liability company could be converted into a public limited liability company (tagged as “Plc.” Companies) that could sell shares to the public. It is also possible to start as a public limited liability company if the requirements are met.

Size of Employees

Small scale businesses employ smaller teams of employees than companies that operate on a larger scale because most small businesses are labour-intensive. The smallest businesses are run entirely by single individuals or small teams. Therefore, the SMEDAN definition will be the basis of the definition for this module being the benchmark for Nigeria businesses. According to SMEDAN (2017), where there is a conflict of criteria in classification, employment based/ number of employees will take pre-eminence. However, when discussing the relative terms of small and large businesses in this module, the nano, micro and small firms may sometimes be referred to as small firms.

Revenue and Profitability

Small scale business revenue is generally lower than companies that operate on a large scale. Note that lower revenue does not necessarily translate into lower profitability. Established small businesses often own their facilities and equipment outright, in which, in addition to other factors, helps to keep costs lower than more leveraged businesses.

Market Area

Small scale business serves a much smaller area than corporations or large businesses. A small convenience store might serve a single community and due to its size, it cannot serve areas much larger than a local area. Growing beyond that might increase the scale of the business operation and push it into a new classification.

Location

A small scale business is mostly found in a limited area, along busy streets or major mode of transport. Also, the business is often located closer to material and supply sources and to markets, easing the burdens of transportation and time.

Limited Investment

In a small business enterprise, capital is supplied by an individual or a small group of individuals. It could be through informal sources like personal savings, rotation contributions, cooperative society, legacy and inheritance, loans or/ and gifts from family and friends, sales of personal properties etc or formal sources such as bank loans, grants etc.

Initial Capital Outlay

Initial capital outlay refers to the financial resources that are required to start up a business. If the initial capital outlay required to start a business is small, that fact alone may not lead us to conclude that a small business requires a small amount of money to start. The major distinguishing factors in any business units rest on the numbers of the contributors to the capital or how the capital was raised.

Type of Technology Employed

Small businesses employ relatively simple technology that is easy to acquire because of their size. This is so because of the huge capital outlays involved in the acquisition of modern technology. Some small businesses may not be able to afford complex and costly technology due to this capital constraint has previously mentioned. They could lease, rent or involved in instalment payment until they pay up and it becomes their property.

3.3 Steps to Starting a New Small Business

A potential entrepreneur or business owner must take a decision either to be a business owner or an entrepreneur. When the decision is made, the following steps should be put into consideration.

- i. Search for an area of need, a product or service. Entrepreneurship is a problem solving exercise. Opportunity could be discovered through internal and external search. This place will give examples of external search such as the use of suggestion box, focus group brainstorming, alternative choice users, newspapers, trade association reports, industrial visits, vocational training avenues, consumer services, personal contact, survey, interviews, online facilities and social media etc.
- ii. Identify the areas of need by asking this question, what can be identified as a need that you might want to meet in the life of the people to raise their standard of living? That gives you an entrepreneurial opportunity. An entrepreneurial opportunity is an unmet need or gap in the market undiscovered by no one except the entrepreneur. It can be described as any 'new' venture that makes a good return on investment within a

reasonable period of time. A business opportunity is an existing area of buyer-need in which a company or entrepreneur can perform profitably. Identify where it falls into in the lens of Schumpeter's theory, if you desire to be entrepreneurial.

- iii. Subsequently, ensure is it in the economic desirability list of the government. The economic desirability of a project is very prominent in the assessment of banks for grants, aids and loans. Economic desirability suggests that the project must fall within the investment priority list of the country. The sectors that has been perceived by the government that can add developmental value to the economy in areas like employment generation, development and utilization of local resources, standard and socio-economic status of the low-income earners and improvement of indigenous technology should be your choice. Therefore, it is a sort of calculated risk to identify a gap from the priority list of the government.

Conduct a SWOT analysis. The SWOT analysis is very instrumental in discovering opportunities. SWOT is the acronym of Strength, Weakness, Opportunities and Threats. The internal environment x-rays your strengths and weaknesses. The Strengths (include your entrepreneurial mindset, knowledge-based concepts, technical expertise, managerial experience, customer network, distribution system, new proven product) and Weaknesses (include technical obsolescence, poor product design, lack of working capital, lack of know-how or know-what experience etc.) are inside of you or the organisation. The external environment encompasses the opportunities (include low interest on loan, technical assistance, needs in market place, societal trends, unexpected occurrences, rising income of target market) and Threats (include inflationary rate, corruption, bureaucracy, government policy, smuggling, shortage of raw materials, plagiarism, poor infrastructure, exchange rate). A sound comprehension of this internal and external environment is crucial to strategic decision making

- iv. Start to set up the operational and financial plans by writing out your visions, missions, objectives, policies, methods, strategies, standards, initial capital etc.
- v. Evaluate the business opportunities to ascertain the decision. Evaluation would be done through the feasibility study. This singular action gives an entrepreneur an edge over others. It is not an act for accountant or management experts only, many individuals do it unknowingly. The bread seller unknowingly conducted the feasibility study by establishing her production and marketing strategy under a financial outlay. This means when she decided to dig into her savings to buy loaves of bread, chose a lucrative spot to stay and projected how much she intended to make for each day had done a bit of

feasibility study. Nevertheless, a **blue ocean** (an unsaturated market with less competition) must be preferred to a **red ocean** (highly saturated market that is highly competitive). Conduct a feasibility study.

- vi. Interview experienced people in business, attend business workshops and seminars to build experience and momentum for right decision.
- vii. Decide whether to start a new business, buy an existing business or a franchise. Decide which form of business ownership would be best.
- viii. Develop these plans and feasibility to a detailed business plan.
- ix. Move to implement the plans. Others may be having the same vision. Delay might be dangerous lest you have a **missing boat**. Missing boat is when there is delay in implementation for one reason or the other and other people gets there before you. It is a **sinking boat** when you impulsively start without adequate feasibility study and consequently, the venture collapses. Opportunity is time.

3.3.1 Support Service for Potential Business owners/entrepreneurs

Many businesses started but did not continue due to wrong decision taken.

- i. *Before implementing your plans, ask these questions and sincerely give answers.*
 - How much capital is required to start and sustain this business successfully?
 - What are the prospects of this business and my chances of achieving them?
 - How long will it take to recoup my initial investment?
 - How long will it take to arrive at an acceptable level of income?
 - How will I survive till that time?
 - Having done the risk assessment, am I willing to take that risk?
 - Can I make it alone or need the assistance of others like family or friends?
 - Will I enjoy doing this business?
- ii. *Buying an existing business instead of starting your business:*
 - a. There are certain advantages derived from buying an existing business instead of starting ones. Such benefits include availability of personnel, structure, location, market share, stakeholders' relationship and possibly goodwill.
 - b. However, the structures may be old, personnel may have poor records of commitment to duty, unfavourable location, obsolete inventory and poor relationship with financial institutions and other stake holders.

c. Before acquiring and existing business, find out by asking the following questions.

- ✓ Why is the business put out for sales?
- ✓ What are the intentions of the present owners after disposal?
- ✓ Are there environmental challenges?
- ✓ Is the business operating efficiently?
- ✓ How suitable are the physical structures for now, and later operations?
- ✓ What is the financial status of the firm?
- ✓ What is the estimated return on investment?
How much is needed for the investment?
- ✓ Is the price alright?
- ✓ Do you have the necessary know-how and know-what to move on?

Decide on which form of business ownership will best fit your choice.

3.4 FORMS OF BUSINESS OWNERSHIP

In these contemporary days, there are different forms of business units that an individual can fit in conveniently. Investing in personal business can be one of the most critical decisions to make. One can choose to invest in a commercial/economic enterprise or a social enterprise. The options are, to start one, buy an existing business or buy a franchise. The challenges are colossal, physically and emotionally. Many budding entrepreneurs cop out early into this decision-making process. An entrepreneur will comprehend these various forms to select the best option to organize the enterprise.

Sole – Proprietorship

This is an organization established, owned, financed and controlled by one person with the aim of making a profit. It is the oldest and easiest form of enterprise an entrepreneur could start with. He sources the capital solely and dotes into his personal assets or bootstraps to meet the needs of the venture. The management and survival depend on his capability, skills and acumen. He can employ others or involve his family members formally or informally. He has no legal obligations to the government than tax payment. He earns his success and profits alone and bears the failure and losses alone too.

These ventures are good for Nano, micro and small retail outlets like supermarkets, convenience stores, schools and training institutes, small factories, craftworks, professional services like laboratory services, computer engineering workshop etc. It has several advantages

such as the requirement of small capital, fitness into any environment, ease of establishment and management, ease in decision-making without any consultation especially when introducing an innovation or exhibiting an entrepreneurial behavior, with no confrontation or legalism. He enjoys his privacy, pays less tax and personally owns all the profits.

However, there are some disadvantages like not being a legal entity; with unlimited liability that could extend to his private belongings; inadequate capital and limited scope of expansion; inability to face competitors and lastly, lack of continuity as the death of the owner may lead to the death of the venture but generally small at the beginning. Succession is possible after death if the entrepreneur has involved the family members in the venture as it is maturing. Many have developed large scale of production and increase turnover through this sole proprietorship. It only takes being focused. However, sole proprietorship seems to be a good option for an entrepreneur or business owner self-employment.

Partnerships

Partnership according to act 1890 of United Kingdom is the relationship which subsists between persons contributing skills, money or money worth in carrying on business “in common with a view to profit”. The number of people combining to run a partnership is 2-20 but 2-10 in case of banking. There are five kinds of partners – General partner, Limited partner, Active partner, Sleeping partner and Quasi-partner.

General partner: This is the managing partner in a partnership. He has unlimited liability and binds the firm. Death or bankruptcy of this partner leads to the dissolution of the partnership.

Limited partner: This is a partner in a limited partnership whose liability is limited to the amount registered under the Limited Partnership Act 1907.

Active partner: An active partner participates actively in the business of the firm and binds the firm. Sometimes draws salary from the partnership for his service on agreement.

Sleeping and Dormant partner: This is a partner who subscribes capital, receives a share of the profits, but does not participate actively in the business operation. The law, however, does not recognize such a partner has being different from other partners.

Quasi-partner or Nominal partner: This is a person who has allowed his name to be used as a partner on the basis of his social status in order to enhance the goodwill and reputation of the firm.

The partners contribute the capital and are jointly liable for profits and losses. Partnership liability is unlimited. The partners will agree on the rules and regulations for the day-to-day running of the business in what is referred to as ‘*the article of partnership or partnership deed or agreement*’.

The contents of the article include the following:

(i) names of the partners; (ii) name and nature of business; (iii) capital contributed by each partner; (iv) ratio for sharing profits or losses; (v) whether salary will be paid and to whom; (vi) factors leading to dissolution. Where the partners have no article of partnership, the Act of 1890 comes to operation. The content includes - equal contribution of capital, no interest on capital but 5% interest on extra contributed capital, no interest on drawings, salaries are not allowed for active partner and so on.

Partnerships can be found carrying on retail and wholesale activities usually undertaken by sole proprietors. They are found in professional activities also and are normally referred to as 'firms'. Where expensive capital equipment is not required, they can quite well undertake some forms of manufacturing ventures. However, selecting a partner is like selecting a life partner, hence, the need for extra carefulness. Where the firm's name is not the real names of the partners it becomes pertinent to register with the Corporate Affairs Commission of Nigeria (CAC). However, an entrepreneur needs to be careful about the set of people involved in the partnership. He must share his vision and seek their consent in writing in order to execute his mission. He might need the people in one way or the other but the flagbearer must make himself distinct. Two people cannot walk and work together without agreement. A partnership has the following advantages - pool of resources resulting to huge capital; joint and better decisions making since two good heads are better than one; opportunity for specialization through division of labour ; sharing of liabilities and others. The disadvantages include unlimited liability; not being a legal entity; exit of one of the partners or the introduction of a new partner can terminate the partnership business.

Co-operative Society

A co-operative society is a form of voluntary self-help business organization in which individuals, sole proprietors, traders or producers united to foster their group and individual business interest. In other words, it is a self-help organization formed by consumer or producers to provide service for its members who supply all its finances and administration. It is a business venture with the primary aim of promoting the economic interest of its members. It is a form of business where members pull their financial resources in order to embark on a business venture. A minimum membership of 6 in industrial co-operative societies and 10 in others.

The first successful co-operative society was by Rochdale Pioneers in England in 1844. Nigeria's first successful co-operative was producers' cooperative society formed in 1922. It is usually characterized by open membership to people of similar interest, democratically

controlled and limited payment of interest on capital invested; members are the primary beneficiaries and continuous education and development are made available to them.

There are five classes of cooperatives vis-à-vis Consumer Co-operative Society (deals with the retail sales of certain consumer products); Producers' or Farmers' Co-operative Society; Producers' / Industrial Co-operative Society (deals with marketing of their products nationally or internationally), Thrift, Credit and Loan Co-operatives (to develop saving habits and borrowing instead of going to bank) and Multi-purpose Co-operative society (combines more than one cooperative society activities and the most common form in this contemporary time). Nowadays, banks, Non-Governmental Organizations (NGOs), Agricultural Development Fund (ADF) and some international bodies are investing, training, giving loans and encouraging co-operatives to stand and make progress. Specific examples of co-operative society activities include Co-operative Press Ltd; Co-operative Transit Ltd; Association of Nigeria Exporter Ltd; Co-operative Agricultural Farm Ltd. It actually helps in buying viability out of insignificant resources by their pool of resources together and above all, members can fully participate in the management.

The renowned Sony electronics developed through a sort of co-operative efforts of 21 insignificant engineers and technicians that earned a name for their nation, Japan. Cooperative society encourages savings and investment, increases standard of living, prevents hoarding, fights inflation and deflation, saves advertisement cost but has the disadvantage of weak management, illiteracy, indiscriminate enrolment of members, and mismanagement of funds, poor returns on investment as well as members negligent or default in loan repayment. Co-operative is people-oriented rather than capital-oriented. It can be more associated with social entrepreneurship than commercial entrepreneurship as it helps in solving the challenge of market failure.

The Limited Liability Company

A limited liability company is a business owned by a number of people, operated as a legal person on behalf of its owners, with the usual motive of profit and the provision that the owners are liable to the company, only to the value of share capital the individual holds.

A company is the association of a group of persons associated together to undertake some form of business activities in order to profit thereby. They are called Joint Stock Company or registered company. This is a typical business of the contemporary time because of its uniqueness in terms of its ability to raise capital through shares, which people can take up in varying amounts and the company's profits being divided as 'dividends' among the

shareholders in proportion to the number of shares held. Moreover, the shareholders liabilities are limited to the nominal value of shares holding and cannot be extended to their personal belongings like sole proprietorship and partnership. There are two main kinds- Private and Public Limited Liability companies.

Private Limited Liability Company

The membership ranges between 2 and 50. It is an extension of a sole proprietor and a better alternative to partnership in terms of sourcing capital and limiting its liability. Nevertheless, it cannot make a public offer of its shares or issue debentures but rather invite relatives and friends to join. They are often seen with the tag 'Ltd' at the end of the company's name. Registration with the Company Allied Commission is highly imperative. It is not compelled to publish its account. It thrives more as family business. Family business is one of the trends in entrepreneurship. It is a business that trusts in a strong internal network. It involves coaching and encouraging next generation of owners, with family politics in a business context, and arrangement for succession. It is one of the best ways of employment creation, as family members get employed immediately after graduation or even engage in on-the-job learning/studies.

Public Limited Liability Company

A company can be statutorily defined as a legal entity with a distinct name and a perpetual succession. The membership is 7 to infinity. Shares are advertised to the public for subscription. A share is a unit of the capital which by purchasing makes an individual one of the owners often called a shareholder. A company is floated by promoters (that later will become board of directors). They take all essential steps until it is registered and given a Certificate of Incorporation which confers a legal status on a company. A Certificate of Trading will consequently be given as authority to commence business and exercise borrowing power. This is done after raising minimum required capital and directors have paid for their shares, etc. The names of such companies bear Public Limited Company (Plc.). There are two main operational documents: The Memorandum of Association and Article of Association.

The Memorandum of Association on one hand, regulates the powers of the company and its relations to the world. The content includes: The name of the company; location of the registered office; objectives of the company; the proposed amount of the registered or authorized capital and a statement indicating the liability of the shareholders of the company. The Article of Association, on the other hand, regulates the internal operations of the company.

The content of the Article of Association includes the rights of each member; mode of appointment of directors; sharing of dividends; when and how the general meetings are to be held; method of auditing, rights and powers of directors, etc.

Another document is the Prospectus. It is a document through which invitation is extended to the general public for subscriptions. It contains every detail about the company to enable a prospective shareholder take decision. The first activity of a company is to issue shares through Stock exchange market. There are two major types of shares- ordinary shares and preference shares.

Ordinary shares are called equity shares/capital. They do not receive any fixed rate of dividend but take whatever remains after the claims of others. Ordinary shareholders are permitted to cast their vote at the annual general meeting. Preference shareholders are primary receivers that take a fixed rate of dividend once profits are declared before any other claims. They do not vote at the annual general meeting since they are not classified as joint-owners of the company but has mere investors. Preference share is perceived as a debt capital. Certain advantages that can be derived from Limited Liability Company are as follows. It can sue and be sued without any interference with the owners of the company. In case of liquidation the loss is limited to the capital contributed by the shareholders. There is large capital advantage, unlimited capacity for expansion and assurance of continuity. Transfer of capital is possible and employees may be shareholders.

Nevertheless, it is not easy to establish because of its high requirements and needed capital, it is not flexible and lacks privacy. It is the most dangerous form of business ownership for an entrepreneur because the management is not in his hand. He lost the hold on it as soon as the shares are advertised. The Board of directors who do not have the entrepreneurial vision may hijack the venture, make him irrelevant and possibly kick him out.

Franchise

Franchise “is the agreement granting the right to do business and specifying the terms and conditions under which the business will be conducted (Meggison et al. 2004:77).” Franchising is one of the recognized ways an entrepreneur or a business owner can start a business. It is the marketing system based on legal arrangements that allows one party- the franchisee-to conduct business with another party- franchiser. It is may be costly but saves the stress of a starting one. This form is often used in a corporate organisation. It is a license to operate an individually owned business as though it was part of a chain of outlets or stores. It is also a situation where an existing organization becomes a parent venture (franchiser) granting other company or

individual (franchisee) the right to use its trademarks name to produce and sell its goods or services. The franchiser provides the franchisee with a complete assortment of materials and services for a fee and percentage of sales; trains, monitors and controls the franchisee to ensure conformity to agreed standard. Examples of such are McDonalds, Mr. Biggs, and tantalizers' etc. Financial assistance, technical assistance in site selection, accounting and operations management, guaranteed supplies and protected markets are consequent benefits. There are three basic types of franchise:

- i. Distributorships, which grant the right to sell their parent company's product such as auto dealerships (Ford, Toyota, GM, Mercedes etc.)
- ii. Trademark or brand name licensing, which gives the licensee the right to use the parent company's trademark or brand in conjunction with the operation of their own business.e.g. beverage (coca cola) and sport franchises.
- iii. Business format franchise is the type most people are familiar with. Business format franchisers offer to their franchisees the license or right to sell its goods or services and/ or use its business technique. The franchisees usually pay an initial fee to acquire this right and thereafter pay a percentage of their gross sales to the franchisor throughout the term of their franchise contract. In return for these payments, franchisees gain privileges, including the right to sell a proven and recognized product or service to use franchisor's business practices and to receive initial training and ongoing support.

Additional responsibilities can and usually do include:

- i) Requirements to meet a variety of quality controls for products and services sold.
- ii) Restriction on what they can sell or how they can operate using the company's name.
- iii) Specifications for their business location and site appearance.
- iv) Prohibitions on the operation of any similar businesses during or after the term of the franchise agreement.

Franchisees usually have an advantage over their non - franchisee competitors, since they have the rights to use the franchisers brand names, trademarks, copyrights, trade secrets and patents, uniform logos, storefronts, and interiors, proven records/goodwill, training and guidance, assistance in securing funding. Major challenge in franchising is the franchise fees, undue control and unfulfilled promises. The entrepreneur needs to discuss with the franchisor on various innovation that could boost the venture. When this is properly done, it is to the benefit of both the franchisor and franchisee.

Social Entrepreneurship

It is another form of entrepreneurship. It is a way of reducing poverty through the power of an enterprise. It is entrepreneurship that emanated out of passion for the disadvantaged and suffering masses. Entrepreneurship for social and not commercial ventures, emphasizes that life is not all about money but on impacting lives. It involves bringing innovation into social ventures. Such enterprise can be undertaken by private, public, individuals, or group. Often, Non-Governmental Organizations (NGOs) are supposed to be drivers of the initiatives but not all NGOs are social entrepreneurship. Such enterprises fill the gap that both the economic and political institutions have not been able to satisfy. They deal with the provision of social amenities such as infrastructure, humanitarian services, health, gender, and education and so on. It is the use of commercial initiatives to solve societal social problems. It is the employment of creativity and innovation to solve unmet social needs of the people. It is a business with primarily social objectives whose surpluses are mainly invested for the social purpose. It could be completely not-for-profit or for-profit or hybrid (both) for sustainability and growth but not to maximize profit for stakeholders sharing. Social enterprise in Nigeria are more of profit making while some are hybrid. This is because the economic entrepreneurship is saturated, there is a need to shift to the social side to meet the unemployment need by creating social enterprises

4.0 Conclusion

When an individual is motivated by necessity or opportunity, taking the right and appropriate decision is crucial to owning a business. The pathways to own a business are discussed, to start a new business, to buy an existing business or buy a franchise. Support service are made available to guide in the right direction.

5.0 Summary

This unit vividly described the pathways to owning a small business. Something positive or negative must motivate a person into business or entrepreneurship. It could be of necessity or opportunity. Whichever, all are improvement-driven and will affect the economy one way or the other. The common characteristics of small businesses were highlighted. The forms of business ownership that the business owners/entrepreneurs can venture into as well as steps to take while deciding to establish a business were discussed.

6.0 Tutor Marked Assessment

- i. Distinguish between the necessity driven and opportunity driven entrepreneurship.
- ii. Explain an entrepreneurial opportunity?
- iii. What do you understand by economic desirability list? Of what importance is it in the choice of venture?

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UNIT 3 FEASIBILITY STUDY REPORT

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 - 3.5.1 New Entry or market pioneering or first movers
- 4.0 Conclusion
- 5.0 Summary
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1.0 Introduction

This unit is a continuation of module 2 and focuses on step six on steps to starting a new business. The need to conduct a feasibility study and the way to go about it. Also, the way to generate and exploit new entry strategy will be considered.

2.0 Objectives

- By the end of this unit, the students should be able to
- Understand the need for intentionality to be entrepreneurial
 - define a feasibility study
 - understand the importance of feasibility study
 - conduct and write a feasibility study report
 - Generate and exploit the new entry strategy

3.0 Main Content

3.1 Intention to be entrepreneurial in action

The choice to be entrepreneurial is not accidental but deliberate. The intention to pursue certain opportunities, offer a new product or service, enter a new market etc. must be intentional. The personal intention to carry out an activity captures the motivational factors that stimulates a

behaviour and the strong commitment to try to pursue entrepreneurial outcomes. As a rule of the thumb, the stronger the intention to engage in a behaviour, the more likely should be the success. Therefore, the perception of feasibility must begin from within the individual, the prospective entrepreneur's self-efficacy. The personal conviction that he can successfully implement entrepreneurial process. Self-efficacy affects the individual's level of initiatives, persistence, resilience and performance. People with high self-efficacy think and behave differently from those with low self-efficacy. Aside, the individual must add perceived desirability, that is, the extent to which the entrepreneurial course of action is desirable. It is about the individual's attitude toward the entrepreneurial outcome, the extent to which the prospective entrepreneur has a favourable or unfavourable evaluation of the potential entrepreneurial outcomes which include personal rewards. The higher the perceived desirability and feasibility, the stronger the intention to act entrepreneurially.

Therefore, individuals should choose the course to be entrepreneurial in their ventures as they conduct the feasibility study.

3.1.1 New-New/New-Old Methods

Newness in entrepreneurship is different from the general "new". Not a new in terms of new cloth or shoe that has just been bought in the market or tear leather vehicle. It is about new to the world or environment or region etc. The best way to approach a new business venture is to initiate a unique product that is not in the market today but would be in great demand if it were, which the new-new approach is. Whilst the new –old 'piggy-backs' on existing innovation of someone else by significantly improving on its current position or completely take it to a place where they have not known the product before.

Most new products or services are product of Research and Developments (R&D) efforts. Hence, R&D is part of entrepreneurial departments. It must be noted that unique ideas are not only from large companies. Research has revealed that most innovations come from small businesses, thus, large organisation seek to buy the innovations or the firms completely or collaborate with or resort to 'open innovations' strategy to benefit from them. In fact, large organisation go to the extent of buying over the innovator as a 'champion' for their organisation. The rate at which new things enter the market has created expectations in the heart of the public to be on the lookout for daily continuous improvement on personal and household goods. This throw a ball into the court of small businesses. In the previous unit, the examples of external

search for opportunities were cited. Here, the examples for internal search for opportunities will be given.

One of the simplest ways is to make a list of frustrating experiences or hazards encountered at a period. For instance, household chores or tasks that are difficult to do, items that are tough for storage, objects falling out of hand, situation that is problematic to fix, and activities that consumes a lot of time unnecessarily. Certain innovations alleviate this problem. Most business ideas arise as products of solutions to people's knotty and nasty experiences. Small businesses will not need stress. There are various and countless opportunities in green products, alternative energy, health care, Nano technology, home automation, engineering education, agriculture etc. You must ensure you make it so unique that it will not be easy for competitors' imitation.

The new-old approach is riskier as competitors can easily copy it like you do. New-new or new-old, it is essential to conduct a feasibility study.

3.2 What is Feasibility study plan?

A feasibility study plan is an action aim at ascertaining the viability, possibility and worthwhileness of a business venture afterward a report is generated. It shows the detailed analysis of the requirements, opportunities and challenges of the venture. It is the stage of fact finding, aimed at determining profit potentials and returns on investment. It is a comprehensive and intelligent investigation into a proposed line of business which findings will enable the potential entrepreneur to make a prudent choice to go ahead, make an alteration or go for another option.

3.2.1 Importance of feasibility study report

A feasibility study report is very important for any business venture as a 'road map' that shows whether that business venture will be profitable or not. It gives a restrain to impulsive actions and follow-follow or band wagon effects. It gives an idea of what is expected, measuring the preparedness of what is at hand with the reality. It is the management function of planning and organizing a business to provide it with everything useful for performance (Kuratko & Hodgett, 2008). He who fails to plan, plans to fail. It makes people to know what they are expected to achieve and whether they are up to the task. It implies managerial innovation. It bridges the line between where you are and where you are going.

3.2.2 Conducting a feasibility study

In order to carry out a feasibility study, a prior attempt to under study an existing similar business, consult relevant books and cross- check areas that are not clear is essential. Do not rely on hearsay but ascertain requirements from two or three sources.

- List your findings and prepare a simple projected profit and loss account and balance sheet (to know the state of your business at glance).
- Base your analysis on the requirements of the business not on what resources are available to you lest you get stuck.
- List the necessary equipment, office or space, finance, staff and training requirements.
- Analyse your own skills and needs for further training and invest your knowledge and education.

3.3 Writing a feasibility report

The feasibility study report is a document that shows what kind of business that is to be done and how it is to be done (Izedomi, 2007). It gives comprehensive report of the, commercial analysis, technical, economic, and financial information for final investment decision to convert available resources to a particular investment idea. This survey will enhance the decision-making process of the businessman either to drop that idea for another, make an amendment or optimistically and enthusiastically continue with the venture. Many people feel that it is a difficult task, no, as an entrepreneurial scholar you should be able to write it for yourself and even consult for others. The professional touch will be needed for an error free and balance finishing.

This study will adopt Dr. D.F Kuratko model.

Title Page

Name of Proposed Company

Names and Titles of proposed founding team members (If there are)

Relevant contact information (Address, phone number, e-mail)

Table of Contents (All pages must be numbered, and all the contents are listed)

- I. Executive Summary
- II. The Business Concept
- III. Industry/Market Analysis
- IV. Management Team
- V. Product/Service Development Plan
- VI. Financial Plan

- VII. Time plan
- VIII. Bibliography/Appendices

3.3.1 Detailed Explanations on the feasibility Plan Report

I. Executive Summary

(A brief overview of the most important highlights from each section. A clear description of the venture, whatever proprietary aspects it may possess, the target market, the amount of financing needed and the type that may be requested)

II. The Business Concept

(Articulate a compelling story to show this is an excellent concept. This section will convince people that you know what you want to do. describe whether it is retail, wholesale, production or service. Identify the current stage of development for the venture (concept, start-up, initial operations, or expansion; the target customer, value proposition in terms of benefits for the customer and potential growths opportunities)

III. Industry/Market Analysis

(Explain the industry of focus and the trends; discuss the target market analysis, specific market niche has produced. Identify the market size, its growth potential, plan for market penetration based on research. Describe the customer profile, who they are specifically and the benefit they will derive. Include competitors and how and why yours will exceed the competition.)

IV. Management Team

(List the founding team members and key personnel to guide the proposed company. Their qualifications, experience, skills and network that matches the critical tasks. An organogram will be good. Finally, outline any gaps in management team and the means to address it)

V. Product/Service Development analysis

(Provide the unique feature and what makes it distinct. Explain the current status and include a clear timeline of the completion of key tasks. Identify the intellectual property involved and proprietary protection inexistence. State if there is any prototype testing and at what stage)

VI. Financial Plan

(Summarise the critical assumptions upon which financial information is based.
Present a pro forma income statement and pro forma cash flow statement with
breakeven analysis)

VII. Time plan

(Use a graphic representation of the dates and related task completion until
actual concept launch.)

Bibliography

(Provide key endnotes, footnotes, sources or extra information)

Appendices

(Necessary pictures and documents like site plans and others that add credibility
to the assertions)

The feasibility plan report covers these key areas: technical, market, financial, organisational and competitiveness. Those are the key things. Write, refine, rewrite until you have a complete document that gives initial direction to your ventures and can subsequently be converted to a business plan to obtain a loan. A business plan is a guide or blueprint for a successful business and can be drawn for an on-going enterprise or a new one. A business plan is a document that can mar or make you, make a hero of you, fail you or fund you, raise or ruin you. It must speak for itself. It will negotiate with national and international financiers. It is the voice of your company to investors

3.4 Differences between a feasibility plan and business plan

A business plan is different from a feasibility study.

- i. A feasibility study is for the assist in taking an informed internal decision while business plan is used for an informed external decision making in relationship with stakeholders.
- ii. Feasibility study is used to evaluate the potentials of the venture to be undertaken and its worthiness while business plan is used to attract investors and obtain external financing.
- iii. The writing of feasibility study is before the venture commences; therefore, it precedes the writing of business plan.
- iv. Feasibility study may not be as detailed as business plan, but it is like a forerunner, making it easy to write a business plan.

After being satisfied with the feasibility study, the next question is, when can the entrepreneur to enter the market?

3.5 Generating and Exploiting New Entry Strategy

One of the crucial entrepreneurial behaviours is new entry. New entry can be perceived in three ways. First, offering a new product/service into an existing and established market. Second, offering an established product/service into a new market and third, creating a new organization regardless of whether the product or market is new to both competitors and customers (Histrich et al. 2009). The newness could constitute more uncertainty over new product/ service and greater strain on resources for successful exploit, but the end is fantastic.

In order to generate new entry opportunity, resources are fundamental building blocks for venture operations and performance. Major resources include fixed, financial and human capital that are converted to production process. Resources are generated in bundles, that is, various combinations of resources. For these combinations to enhance a firms superior performance it must be *valuable, Rare, inimitable and non-substitutable*.

Valuable in terms of the resource that will enable the firm to pursue new opportunities, neutralize threats and offer products and services that customers will value greatly. *Rare* because it is not commonly found everywhere. *Inimitable* because to duplicate the combination of the resources will be difficult or costly. *Non-substitutable*, that is, without a perfect substitution.

Knowledge is one of the key sources of generating bundle of resources. It could be tacit knowledge obtained through intuition, experience, observation, talent, skills etc. It could also be from explicit knowledge acquired formally from books, school, internet etc. Market knowledge, technology knowledge, prior knowledge and information search will help the entrepreneur to attract more knowledge that will enhance the decision for new entry strategy, whether to or to not.

3.5.1 New Entry/ market pioneering/ first movers

The entrepreneurs' decision to be proactive and be a first mover or first to the market is based on the uniqueness and the bundle of resources that offers them a competitive advantage. They are firm that brings new products or service to the market before other organizations (Muller et al. (2009). Being first can result into a number of initial advantages that can enhance growth and performance. There will be limited competitions for a time of grace or lead time, brand leadership, choice of best employees, high turnover, high profitability, prime position in the market, cost advantages, protect product uniqueness and secures access to important sources of supply and distribution. However, first movers do not always prosper and can be disadvantaged. Such include high instability of the environment surrounding the entry such as

customers' demand, changes in technology, retention, inability to educate customers' etc. These disadvantages can be reduced by creating a niche to serve in the market rather than general. Nevertheless, to enjoy the first mover advantage maximally, barriers can be erected to dissuade entry by potential competitors by building customers' loyalty and switching costs.

A choice to be a second mover or late entry is an option, if the entrepreneur cannot have a combination of resources to create a bundle.

4.0 Conclusion

There must be a deliberate decision to be entrepreneurial by developing a right attitude that believes in oneself for outstanding performance in the path to entrepreneurial outcomes. The feasibility study is very important since entrepreneurs are not impulsive actors. The simple way to write the report has been simplified for individual to be able to carry out the exercise. A choice of entry has to be taken, a market pioneer or late entrants with their pros and cons.

5.0 Summary

The importance of deliberately developing a high perceived self-efficacy and high perceived desirability to become entrepreneurial was emphasized. Also, the entrepreneurial methods of the new-new and new-old was clarified. The internal ways of sourcing innovation was explained. The feasibility plan was explained with its importance. The content of a feasibility study as well as detailed explanation on each sub-head was made clear. Finally, the difference between feasibility study and business plan were stated explicitly.

6.0 Tutor Marked Assessment

. Write short notes on the relationship between these pairs:

- i. Perceived self –efficacy and perceived desirability
- ii. New-new and New-old
- iii. Feasibility study and business plan.

7.0 References/Further Reading

Adeyeye, M. M. (2018) *A Fundamental Approach to Entrepreneurship, Small and Medium Scale Enterprises second Edition*. Ibadan: Evi-Coleman and Co. Publishing House.

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UNIT 4 MANAGING SMALL SCALE BUSINESSES

1.0 . Introduction

2.0 Objectives

3.0 Main Content

3.1 The nature of management

3.2 Management of micro enterprises

3.2.1 Tips for managing a micro business

3.3 Reasons for the survival of small businesses

3.3.1 Signs of problems in small businesses

3.3.2 Factors responsible for small businesses failure

3.4 Prospects of business enterprises development in Nigeria

3.5 Forms of Business Expansion

4.0 Conclusion

5.0 Summary

6.0 Tutor Marked Assessment

7.0 References/Further Reading

1.0 Introduction

This unit discusses some advances in managing small scale businesses. Statistics showed that 95% of small businesses fail in the first 5 years. This unit attempts to expose readers to this challenge to have more survivors through this study.

2.0 Objectives

By the end of this unit, scholars should be able to

- Understand the nature management.
- State the tips to manage a small business
- Identify signals that can lead to demise of small businesses
- Explain reasons for continual survival of a business
- Describe diverse forms of business expansion

3.0 Main Content

3.1 The Nature of ‘Management’

Management is the achievement of the organisational goals effectively and efficiently. This is a basic definition which needs to be expanded. Management is applicable to every kind of organization. Any organization that involves human and other resources calls for management.

(a) Management is important to any level in an organization. In other words, whatever position you find yourself in an organization, you will feel the presence of the management. Those that practice management by carrying out the functions of management are called managers. Managers make people to accomplish the organizational goals. They need to understand and appreciate it so that they can have in-depth of what they are doing.

(b) Managers are people employed to manage the organization by carrying out some specific functions. These functions are commonly referred to as managerial functions. We shall be looking at these managerial functions one after the other in subsequent units of this course. These functions are planning, organizing, staffing, leading, motivating, coordinating, directing and controlling among others.

(c) The aim of all managers whether a senior manager or a junior one is the same.

It is to make surplus, in other words, to make profit. Making surplus demands taking the right decisions, so that the resources available to an organization are used without wastage. All resources have values and the values are always expressed in monetary terms: Naira and Kobo.

Consequently, when making use of organizational resources, money is being spent to acquire revenue. The manager needs to find out whether the amount coming in is more than the amount being spent, then there is surplus. If contrary is the case, it means that the organization is making a loss.

In a non-profit organization, efficiency in the use of resources is also demanded. Remember, that management is practiced both in profit and non-profit making organizations. Even though profit/surplus is not supposed to be emphasized in a non-profit making organization, they should at least break-even.

(d) Managing is concerned with productivity. This demands creating something that is of value to the customers, but the higher the volume of production, the better for the organization, that is, economy of scale. The manager, therefore, always looks at the situations where he will produce more so that the unit cost will always be smaller.

(e) The success of any organisation depends on how well it is managed. The management of small, medium and large and some small organisation is quite different from Nano and micro. Thus, this unit will discuss the management of the small categories.

3.2 Management of Micro Enterprises

Management of micro business may be termed as the gainful use of resources, strategies and factors that are necessary to conduct business successfully. It is the utilization of management principles and functions for the available resources sharing and uses in the organization. Success in any business is dependent on the

management and marketing. A Nano and micro businesses are firms with less than 10 employees and are usually product of self-employment. They are not intense entrepreneurially since they are often contented with remaining small. They are often at the verge of collapsing or struggling for survival. However, micro firms have the potentials to grow if properly managed. Most entrepreneurial firms globally started micro and became corporate.

3.2.1 Tips for Managing a Micro-Business

Micro businesses cannot implement all the management functions at a stretch. Hence, the following recommendations are made for entrepreneurial micro firms to manage the business till maturity and enhance the growth.

1. Sacrificial beginning is very important, hence, there may be the necessity to reduce the cost of living to fund the business. For instance, move out of a large apartment to a smaller one, sell your big car for smaller one or none and so on for a while.
2. There may be need to bootstrap, that is, the use of existing resources to run the business. For instance, the business can be run completely from home. Peradventure, a place can be acquired as shop/office, obtain equipment like furniture, etc. from home or lease equipment instead of buying. If it is unavoidable to buy, it is advisable to buy used equipment instead of new.
3. Where extra hands are needed, involve the household members. You can also employ staff for shorter periods instead of permanent employment and at non-market rate. It is better to employ less hands to avoid under-utilization of staff.
4. Obtain loans from relatives instead of banks. Deliberately choose customers who pay quickly and endeavour to offer same conditions to all customers except to offer discounts to customers that are paying cash.
5. It is equally important in managing the micro-firms to be mindful of your drawings, seldom take products or cash from the firm, if done for self, family or friends, such should be accounted for and be paid for.

6. Avoid extravagant spending generally, including at occasions and ceremonies. It will drain your capital. Keep proper records of all your transactions.
7. Be physically present to supervise the venture, if unavoidably absent, have irregular routine checks getting there at an unsuspected time. Take regular inventory of your stock.
8. Do not rely on just one customer from a distant for the supply of your products, lest you end up being made a fool. Similarly, do not always depend on waybill, travel to ascertain price once in a while.
9. Moreover, keep your trade secret at the initial stage and avoid overtrading; use the opportunity to maximize the market before it gets saturated. and always seek to be innovative
10. Plough back your profits for growth and take advantage of credit purchase that are not burdensome.
11. Place yourself on monthly salary before growing to earn the entrepreneurial profit; maintain the business entity concept that separates the business from the owner despite not being a corporate body.
12. Attend workshop and training to acquire more knowledge and enhance your managerial skills.

These tips are essential for proper management. As the business grows from micro to small, somethings will be changed and the management functions and structure will be adopted. However, business is to be nurtured carefully and to discover any symptom that could lead to death for immediate attention.

3.3 Reasons for the Survival of Small Businesses

In spite of all odds, small scale enterprises keep surviving. The reasons include the following: There is:

- a) Small capital requirements with optimism of brighter future by the owner.
- b) The pride of ownership because independence has no option.
- c) Personal attention given to customers and business.

- d) Lack of strict rules, regulations and policies that could hamper the foreseen changing conditions of the market.
- e) High respect for customers as kings.
- f) Government assistance is received in form of loans, aids, provision of raw materials, infrastructures, etc.
- g) Absence of government interference and less bureaucracy.
- h) Sources of inventions and innovations are discovered through open innovations.
- i) Rendering of personalized services to customers in the face of stiff competitions from large organization.
- j) Privilege to serve as great substitute for large ones at weekends and public holiday's period.
- k) the believe in small profits and low prices that results in quick turnover making them not to pack-up and make life convenient for the poor masses.
- l) Flexibility in diversification by changing their business lines according to the needs of the customers.

Thus, they survive but there are signs to observe while running the business that could lead to problems if not nibbled on time.

3.3.1 Signs of Problems in Small Businesses

Small business activities like any other ventures have high potentials and prospects; nevertheless, it has its limitations and problems. In identifying the various problems there are some signals that are problem pointers which could be curtailed before they constitute into a serious problem. The following signals indicate there is a problem. Urgent attention should be given to avert it because a stitch on time saves nine.

- i) When the total revenue does not cover the total costs.

- ii) When there is deterioration of working capital i.e. current assets not being able to meet the current expenditure due to over investment in fixed assets, the absence of cash planning, long-term repayment or drawings.
- iii) When there is high liquidity ratio which indicates that the business is sponsored by creditors' funds (debts) with the inability to pay up.
- iv) When there are declining sales and/ or inconsistent growth in sales turnover.
- v) When the profit is declining instead of growing.
- vi) When there is decline in capacity utilization which is tantamount to a fall in production capacity.
- vii) When there is decline in the quality of products and poor supervision of the plant.
- viii) When there is high labour turnover or high exit of employees due to one reason or the other.
- ix) When there is a high rate of fraudulent practices by employees.
- x) When there is a desire for an alternative venture inside of you because of lack of interest, zeal and other logistic reasons.

When these indices converge and are prolonged in the enterprises, they hatch and manifest themselves as problems which could lead to complete business failure and collapse. These problems can be caused by one reason or the other.

3. 3.2 Factors Responsible for Business Failure

Business failure is the last step in the organisational lifecycle. The key factors that may lead to failure of micro and small enterprises can be classified into two: internal and external factors. The internal factors are cases that emanated from within and can be managed by the organization or the manager. Whilst the external factors cannot be controlled by the owner- manager or the organization.

Internal factors

The internal factors will be considered first and they include the following points.

i. Wrong choice of location: A good location may enable a struggling business to survive and prosper, whereas a wrong choice of location could spell disaster to even the best managed enterprise.

ii. Over expansion/ rapid expansion: This is one of the leading causes, it often happens when business owners confuse success with how fast they can expand their business and consequently leading to overtrading. It is best to focus on slow and steady growth. Many bankruptcies have been caused by rapidly expanding companies.

iii. Choosing a business with little or no prospect: Since you are not operating a charity organization, the essence of business is profitability. A profitable venture with great prospect is necessary to sustain an on-going organization. You need to ascertain there is a future for this business.

iv. Inadequate cash reserves; This involves the necessary funds needed for both the cash flow as well as the personal living expenses to survive before the business starts booming. If such funds are not enough then the prospects for success may be narrow.

V. Failure to clearly define and understand your market: This involves plunging into business without proper feasibility study to analyze issues. Issues like who your customers are, how to reach them, the nature of your product in relation to their needs, their buying patterns, the competitors, risk assessment etc. could lead to failure.

vi. Failure to set your product or service price correctly: Under-pricing of goods. For instance, someone who would wish to be the cheapest, at the

same time to be the best/ highest must clearly set or define your pricing and procurement strategies.

vii. Failure to adequately anticipate cash flow: For instance, at an early stage, the flows are limited and takes long to be realized. Over-extension of credit facilities from debtors and tight outflows will consequently affect prompt payment of suppliers and other things leading to failure. This should be properly be looked into

viii. Absence of productivity intelligence: Failure to anticipate or react to competition, technology, and other changes in the market place. It is dangerous to assume that what was done in the past will always work. Always change things based on the new market needs and time, check on competition activities, available technology and be open to new ideas and experiment. Those who fail to do this end up being challenged and sent out by proactive competitors.

ix. Over dependence on a single customer: The business must expand its customer base. If a business has one customer, there would be a serious fear of losing the customer including the implication of closing down. It is better to have a large customer base than having one big customer.

x. Poor management: Most owners do not have the require skills to successfully run the organization. More importantly there are no avenues for training to improve their skills. This happens due to lack of managerial know-how, knowledge and experience in the venture or I can do everything syndrome. Also, as the business grows beyond existing management, resources and skills may exceed certain individual's ability to manage and plan. All these account for poor management. Small business enterprises are characterized by poor record keeping and there are no institutional support facilities for them to have access to require information for effective planning and management purposes.

xi. Inadequate /ill - timed financing: It is important to have sufficient capital, it is, however, not enough to simply have sufficient financing. Business owners should avoid securing wrong type of financing, miscalculating the required amount or the cost of borrowing money. Majority have limited access to diverse sources of capital or even foreign exchange as institutional credit.

xii. Inadequate infrastructure: Facilities that are needed as support base to start, run a business successfully and to grow are grossly inadequate. In some cases, these facilities have to be provided by the owners of the enterprises.

xiii. Lack of raw materials: In some cases, needed raw materials are sourced externally. Hence the fate of such establishment is tied to the availability of foreign exchange, fluctuation in the exchange rate and strict government policy for accessing the foreign exchange.

xiv. Owners' subjective perception: The inability of the proprietor to be objective, lack of self-criticism and being conservative may to businesses failure. New businesses suffer more often because there are more dreamers than doers.

Xvi. Poor accounting system: Most small scale enterprises do not keep proper records and in some cases none is kept. It is therefore difficult to assess and evaluate their viability and package them for external credit facilities.

Others factors include poor inventory control; unethical businesses practices such as adulteration, dishonesty; inability to attract qualified and varied skills personnel; lack of personal attributes, leadership acumen and autocracy; lack of business connection and poor human relationship etc. are factors that the owner could control to avoid failure.

External factors

These are factors beyond the organization and the owner's control. Such factors include the listed but not limited to these.

- i. Competition with large companies
- ii. Inaccessibility to relevant modern technology
- iii. Natural disasters like war, draught, trade disruptions etc.
- iv. Unfavourable policy framework by the government, economic and political instability.
- v. Inability to secure funds or loans, long-term equity capital and build financial reserves.
- vi. Limitations in available extension services infrastructural supplies and power supply.
- vii. Constant changes in government policy destabilize or lead some small business enterprises folding up. Some of these policies are not only contradictory sometimes they are out rightly discouraging.
- viii. So many government policies in respect of small business enterprises are poorly implemented, which makes it possible to continually sustain and support small business enterprises

3.4 The Prospects of Business Enterprises Development to Nigeria Economy

Entrepreneurship is very cardinal to the economic growth and development of a nation. It is sometimes referred to as the engine growth of most economic world. There are great prospects for entrepreneurship in Nigeria with the look of things. The sky is the limit for an optimistic and persevering entrepreneur. There are many benefits accrued to such development as a nation as well as individuals, if holistically considered.

- a. It is a source of job creation for self and others, hence, reducing unemployment. In developing countries, it is the private sectors that employs average of 85% of the workforce while government employs range of 15%.
- b. It Promotes creativity, exploration and innovation among citizens.

- c. It stimulates economic competition and prevent monopolistic economic imbalance in the country.
- d. It is a means of revenue generation for the government and increasing the economic growth.
- e. It enables some individuals to earn extra income especially those who are already employed in one thing or the other.
- f. It leads to the development of more industries and local technologies as catalyst for technological development.
- g. It encourages self-reliance and effective domestic production for consumption and exportation.
- h. It reduces rural-urban migration by young graduates.
- i. It complements services rendered or products offered by large scale industries, for instance, big businesses can manufacture automobiles while small ones does the repair
- j. It has the power of penetration and transformation in the local areas.
- k. It assists in the development of indigenous entrepreneurial qualities, attitude and skills in others.
- l. It affords the opportunity to create wide dispersion of industries in the society and enhances regional economic balance.
- m. It rejuvenates adaptation to change by its flexibility.
- n. It grants development of new markets, promotion of modern technology in small-scale industries and healthy competition for higher quality product.
- o. It offers opportunity for the exploitation of untapped industrial opportunities.
- p. It helps in the promotion of indigenous technology.
- q. It assists in reducing of crimes in urban areas.
- r. It enhances regional economic balances.
- s. The preservation of healthy competition in the business world becomes a reality.
- t. There is reduction in human resource wastage.

- u. The discoveries of genius and making of entrepreneurs becomes possible.
- v. Planning to facilitate specialization in terms of particular areas for particular industry.
- w. Poverty reduction and better standard of living by generating foreign exchange through export and the national income per capita will shoot up positively.
- x. They provide training ground for establishment and management of a large firm, over time some of these firms grow and expand.
- y. They encourage and promote private sector initiatives and development.
- z. They act as industrial links between local producers of raw materials and industrial concerns

The economic atmosphere must promote private enterprises in Nigeria. For instance, many large markets are springing up in villages, towns and cities with foreign goods among the teeming population. This is the constitution of the army of consumers with demands according their age groups. The environment should be made more favourable for liberal foreign exchange and trade policies.

In view of the various opportunities highlighted Nano, Micro, Small and large business should desire for growth and expansion.

3.5 Forms of Business Expansion

Growth is one of the distinctive of an entrepreneurial venture. It must desire and pursue growth. A sole proprietor, a partnership etc. can grow through expansion. Expansion can only take place when a business is surviving and existing. This section considers various ways of business expansion.

Expansion of the scale of production

Expansion of the scale of production can take place to attract economy of scale in two ways - by natural growth (usually slow) or artificial growth.

The natural growth is when a sole proprietor wants to expand by ‘ploughing-back profits’, changing to partnership or private limited company.

Artificial growth is when two or more firms combining together. They can combine with other firms horizontally or vertically, temporarily or permanently. Where all member firms are at the same stage of production is referred to as *horizontal combination*. For instance, all cobblers coming together to rejuvenate shoe business. Firms coming together at different stages are referred to as *vertical combination*. For instance, a group of bakers coming together – one does all the mixtures, another bakes, another is in charge of the finished products, another does all the branding and packaging, and finally, another takes charge of distribution. This could be done rotationally or as agreed. Fixing of the selling price depends on the cost of production and the agreed percentage mark – up or margin. The Resale Price Act (1964) makes it illegal to fix minimum prices that the combination should not fall below for products.

Alliance

A business alliance occurs when two or more businesses come together to achieve a goal over a defined period of time. The entrepreneur or business owner should go into alliance with another entrepreneur or a businessman that his willing to compromise with the innovative vision. The business may be in direct competition by offering similar products or services to the same target audience. There must be proper documentation of terms of agreement in a legal form – A Memorandum of Understanding (MoU). The businesses are to maintain their separate entities; however common goals must be developed. It is quite cost advantageous as complementary services on each other’s business efforts are rendered within the alliance and possibility of introducing an innovation. There is increased effectiveness in product supply and boosted customer’s base. It saves

time, reduces cost on some capital expenditures and overheads like sales promotion, marketing expenses, duplication of staff etc. An example of such is a computer engineering firm forming an alliance with a cyber café.

Joint Venture

It is a business arrangement wherein two or more independent firms come together to form a legally independent undertaking, for a stipulated period, to fulfil a specific purpose such as accomplishing a task, activity or project. An entrepreneur can engage in this form of temporary partnership that is established for a definite reason with or without a specific firm name. They are co-venturer on a contractual agreement pulling their resources together to carry out an economic activity with a joint control.

Diversification by Small Businesses

This is form of business ownership that occurs when an entrepreneur ventures into a new product and a new market entirely. It could be *a horizontal diversification, vertical integration, concentric diversification or conglomerate diversification.*

Horizontal Diversification is when an entrepreneur takes over a business of the same type and with related technology.

Vertical Integration is when either a supplier or distributor's firm is taken over by an entrepreneur. It is sometimes called chain integration.

Concentric Diversification is a situation where an enterprise takes over another similar type with strong connection to one or other of its features.

Conglomerate Diversification is when an entrepreneur takes over another enterprise in a completely new product market situation. Most conglomerates developed by making a number of such additions to their kinds of business operations. Examples of such additives are health products, industrial chemicals, building materials, road construction products etc.

Cartel or Kartel (German): These are firms producing similar commodities (horizontal structurally) setting up a central selling- organization for the marketing of the product. The aim is to keep up the price of the commodity by restricting output. Member firms must not exceed the production quotas assigned to them.

Mergers: It is the amalgamation of two or more firms into a single undertaking. It may be a large, powerful firm absorbing smaller and weaker rival business. After a successful “take over” bid the smaller loses its identity and adopts the name of the large one. If both are large companies, a new name is formed or the two names are combined not to lose their goodwill.

Trusts: These are generally vertical in structure. It is an amalgamation in very large scale, formed by the transfer to a body of trustees of the share in the constituent companies. The shareholders receive trust certificate in exchange for their share certificate. They are like Non-Governmental Organizations (NGO) or social enterprises.

A Holding Company: A holding company is purely a financial institution which owns and obtains the control of a whole series of organizations referred to as subsidiaries by holding not less than 51% of its capital of shares. These subsidiaries now pursue similar policy with the holding company and still retain their original names and goodwill. They are not involved in the subsidiaries daily activities but manages, coordinates and share benefits. It is possible for one man or small group to dictate policy to a vast organization by having a controlling interest of minimum 51% capital in the holding company itself. Each constituent firm thus becomes a subsidiary company. A subsidiary company does not hold shares in its holding company. A collection of subsidiaries of a holding company

is known as group. For instance, U.A.C. (Nig. Ltd.) having G.B. Ollivant, Kingsway Stores, A.J. Sowards, Nigeria Breweries, U.T.C. Motors Ltd & Lever Brothers Nig. Ltd. are a typical example of pyramiding. Pyramiding is a system whereby holding companies are subsidiaries of another holding company referred to as parent company. It involves using the initial investment profits for an additional investment which is a pyramid of investments. This is one of the contemporary developments in Nigeria businesses. Examples of Nigerians' holding companies are Dangote Group of companies, Honeywell Group, Access Bank Group, Transcorp and UAC of Nigeria Plc. Entrepreneurs seeking expansion can establish their own subsidiary companies and become the group Managing Director or Chairman of a group of companies. The holding company and each of the subsidiaries must be individually registered as different limited liability companies.

4.0 Conclusion

If businesses are properly managed, there will be more survivor. Management is applicable to every facet of life. Ignorance in managing micro business can affect the potentials of such organizations. The various ways an organisation can stop being small and make profits were duly discussed.

5.0 Summary

The term management was simply explained as a means of achieving the organisational goals effectively and efficiently. The management of a nano, micro-organisation is different from SMEs that are corporate. The tips were given. Signs that could show itself in businesses as indicators of problems were extensively discussed. The internal and external factors were discussed as ways to expand a growing business was expressed.

6.0 Tutor Marked Assessment

- i) Highlight five internal factors that can lead to failure and postulate solutions to them.

- ii) Identify five ways to manage a micro business.
- iii) What are some prospects in starting a small business?

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UNIT 5 MANAGEMENT OF SMEs

CONTENTS

1.0 Introduction

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3.0 Main Content

3.1 Conceptual understanding of management

3.2 Management Functions

3.3 Universal Principles of Management

3.4 Management versus Entrepreneurship

4.0 Conclusion

5.0 Summary

6.0 Tutor Marked Assessment

7.0 References/Further Reading

1.0 INTRODUCTION

In the previous unit, our discussion has been on nano and micro business also referred to as small business enterprises. In this unit, we will be talking about the management in small and medium enterprises.

2.0 OBJECTIVES

At the end of this unit, you will be able to:

- Possess a conceptual understanding of management
- explain the different management functions
- apply the management principles
- distinguish clearly between management and entrepreneurship

MAIN CONTENT

3.0 Conceptual understanding of Management.

Management is a universally acceptable and necessary concept irrespective of whether an organization exists to make profit. It takes place at all levels in an organization and every manager performs essentially the same function whether he belongs to top or middle- or first-line management. The difference lies in the magnitude of the task, the scope and degree of the authority.

Lawal (1993) noted that the word Management was derived from an Italian word "managgiare" meaning to train horses. It was originally used to indicate the

process of managing, training, or directing sporting and housekeeping activities. Later it was extended to the operations of government and business. Management and thus be defined as a process by which scarce resources are combined to 'achieve given objectives. This describes an activity which can be better referred to as managing. It refers to the people who carry out the activities, that is, the managers.

Put differently, Management is the achievement of organizational goals through people and other resources. The manager's job is to combine and coordinate human, material and technical resources in the best way to achieve these goals. Managers may not be directly involved in production; they do not produce a finished good, rather they direct the efforts and activities of other to achieving the organization 's set goals. Management, indeed, is the critical ingredient for the six Ms'(Manpower, Machinery, Money, Market, Methods and Materials,) these are the basic resources of any organization centered on the manufacturing processes as it is widely known today. Most production efforts especially that of consumer goods, was undertaken in the home. Different authors postulated different perspectives, but they point towards the same things.

For instance, Fredrick Winslow Taylor, said "Scientific management means knowing exactly what you want men to do and seeing that they do it in the best and the cheapest way." while Harlow Person asserted "Scientific management as characterizing that form of organisation and procedure in purposive collective effort which rests on principles or laws derived by the process of scientific investigation and analysis, instead of tradition or on policies determined empirically and casually by the process of trial and error." Also, Jones perceived "Scientific management as a body of rules, together with their appropriate expression in physical and administrative mechanism and specialized executives, to be operated in coordination as a system for the achievement of a new strictness in the control and process of production."

The term Management can often be used to mean a discipline, or an activity or in reference to corporate leadership. When used to mean a corporate leadership the term refers to a body or group of people who assumes joint responsibility of formulating, interpreting and implementing the broad objectives and/or policies of an organization.

The American Institute of Management defines management, "it is used to designate either a group of functions or the personnel who carry them out; to describe either an organisation 's official hierarchy or the activities of men who compose it; to provide antonym to either labour or ownership". Mary Parker Follett (1868-1933), defined management as "the art of getting things done through people" because they are willing to do it. She also described management as philosophy.

Furthermore, Drucker (1973) defined management as an objective function that ought to be grounded in the responsibility for performance. Whilst Lawrence Appley (1981) in his book titled "Management in Action" defined management as the art of getting things done through people". Also, Sekaran (1989) defined management as the functional process of accomplishing the goals of the organization through the help of others.

Sherlekar (2001) defined management as a social process, involving coordination of human and material resources, through the function of planning, organizing, staffing, leading and controlling in order to accomplish stated objectives. definitions are endless while some corroborated themselves; some contradicted one another. What appears to be indisputable is the fact that management is a process by which responsible people (managers) in an organization get things done through the effort of other people in grouped activities. This size of an organisation or number of employees does not determine who a manager is. Right from the very simple organization up till the more complex organization.

One can think of management functionally, as the action of measuring a quantity on a regular basis and of adjusting some initial plan; or as the actions taken to reach one's intended goal. This applies even in situations where planning does not take place. Stoner and Wankel (1988) described management as the process of planning, organizing, leading and controlling the efforts of organization members and of using all other organizational resources to achieve stated organizational goals. From this perspective, Frenchman Henri Fayol (1919) considered management as to forecast and plan, to command and organize and to co-ordinate and control. In this school of thought, Frenchman submitted that management is the act of seven functions:

1. Planning
2. Organizing
3. Leading
4. Controlling
5. Coordinating
6. Staffing
7. Motivating.

These becomes the universal management functions.

3.2. The management Functions

The first four are the basic management functions. These seven functions are applicable where the employees are a bit large and can operate on functional departmental levels. The functions will be elaborated.

Planning

Planning involves selecting mission and objectives as well as the actions to achieve them, which requires decision-making. Decision-making means choosing a course of action from among alternatives. No real plan exists until a decision - a commitment of human or material resources has been made. Planning is a design, an analysis or proposal that should include strategic planning, operational planning and financial planning. It is very basic to all management function. It is

deciding in advance what to do, when to do it, who to do it, which ways to do it, why doing it and how many resources are to be used. Ilesanmi (1997) stated that planning is a set of managerial activities designed to prepare the organization for the future and ensure that decisions regarding the use of people and resources to achieve organizational objectives are taken. Planning is particularly critical in the SMEs because of its extensive resources. A plan establishes the basic objectives of the firm, determines how these objectives can be attained, puts into consideration various aspects of the environment, and determines the number of resources necessary for successful implementation.

Decision-making enables the consideration of the planning premises, identify alternatives, make comparisons, and select the course of actions that will best lead to the achievement of the organisational goals and objective. There is need for regular appraisal to ensure there is no deviation except where there is need for a better choice of alternative.

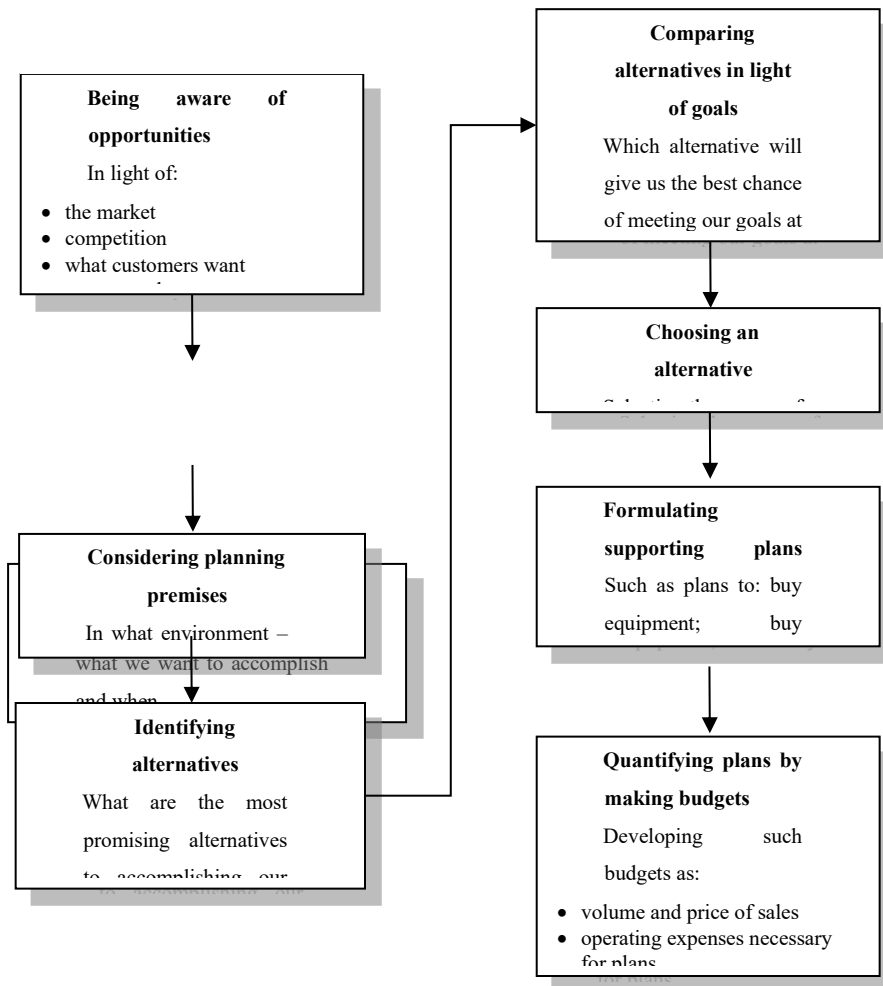


Figure 1: Steps in Planning

Mission: Missions are the basic purpose or function or tasks of an enterprise. It is the broadest aim that the organization chooses for itself. Its uniqueness distinguishes an organization from others of its type in the society. It is the major objectives to which the activities of the enterprise are directed.

Procedure for determining Organizational Mission

Mission is usually the offspring of a vision. Here are some guidelines in taking this decision. What is your vision? That is, what is your dream in terms of customers' satisfaction and their socio-economic status?

In answering the following questions posed by Drucker (1973)

- What is our Business? A business is defined by how the consumer is satisfied by the product, is it market or consumer oriented or production oriented?
- Who is the customer? The customers may not be users.

- What is the value of the customer? See value not as quality but as benefits or advantages derived by customers from the enterprise.
- What will our business be? The inculcation of these environmental developments into the objectives and strategies of organization.
- What should our business be? Access to new opportunities and new technological innovation is a way of redefining.

Objective answers will lead to the creation of a mission statement.

Mission Statements is a public statement on behalf of an organization which sets out *raison d'être* in terms of customer needs it intends to satisfy, the market within which it will meet them (Cole, 1997:16). It facilitates organized thinking within the organization, enhances focused communication with the subordinates and common sense of organizational purpose.

Example: British Airways

Our Mission

To be the best and most successful company in the airline industry

Goals are general targets to be accomplished.

Objectives: Objectives are the organization's operational or specific intentions of the various operational units of the organization targets usually tied to budget. Establishing objectives is to convert the mission directional cause into designated performance outcomes. Objectives are goals towards which activities are directed. Objectives must be stated in quantifiable levels and must contain deadline for accomplishment. Objective may be set in area as market share, innovation, productivity, profitability, work performance and social responsibility. Other areas could be survival, services to customers, employees' welfare, and growth etc. Objectives state accomplishment in regular, specific and measurable terms with a target date. They represent the intended outcomes of the day-to-day needs of customers and stakeholders. They are subject to frequent review and amendment. Formulation of objectives and constant references to them are important to the business.

A good objective should satisfy the following salient points:

- i. Specifically promoting the purpose and strategic aim of the organization in a clear defined term.
- ii. Conformity to the organization's values and policies.
- iii. Acceptable and suitable for usage.
- iv. Verifiable achievement in terms of time, quantity, cost or relevant ratio.
- v. Definitive of current, comprehensible and challenging targets for individuals involved.

iv. Consistency and flexibility in the light of changing circumstances especially where these are unforeseen challenges.

vii. Communicable, not imprecise fuzzy ideas.

Summarily, a good objective must be S-M-A-R-T i.e. Specific (Tangible not abstract), Measurable (Quantifiable results), Achievable (not dream world thinking), Realistic (Relevant and applicable), and Time-bound (governed by deadlines).

Forecasting

Forecasting is an important component of planning process. It involves the ideas of what resources are required, when they will be required and how many will be needed? New firms may find it difficult to forecast since they lack past figures to project into the future. However, a number of methods can be used by new business owners such as:

- Consulting or talking to wholesalers may give some ideas about how competitive the products are.
- Visiting the chambers of Commerce and Industry to obtain population figures and economic estimates of the town.
- Personal tour and excursion to related existing firms.

Strategies

Strategies are clearly thought out designs, methods or methodologies that are products of research. It is the means of implementing the various objectives of business plan. The strategies of a firm must be correspondent to its resources. Strategies such as market concentration, market development, product development, innovation, turnaround and divestiture are principal strategies that could serve as the basis for achieving major long-term objectives. The SWOT analysis often used for company situational analysis is very paramount in the selection of strategies, that is, considering the Strengths and Weaknesses of the company and also the Opportunities and Threats in the external environment. Moreover, strategies must be clearly stated e.g. change unit price, change product design, withdraw from market etc.

Standing plans: This is used wherever an organizational activity occurs repeatedly because they enable a single or set of decision to guide those repeated actions. Major types of standing plans are policies, procedures and rules.

Policies are general guidelines for decision making. They are actions, decisions, and thinking that monitor individuals in an organization. Formulation of policies is an important aspect of planning process done by top managers. Policies also ensure continuous framework for the

conduct of individuals in business, ensure consistency of actions, provide direction for the business and assist in delegation of authority. Production, marketing, personnel, purchasing and finance are all strategic areas that policies take care. Less strategic areas such as dressing, appearance, punctuality etc. may also be implemented through policies.

Procedures are sequences of required action detailing exact way the activities must be accomplished. Tactics are the breakdown of procedures into smaller effective units of action.

Rules are specified definite actions to be taken, whether positively or negatively in a given situation.

Organising

It is the process of describing formal relationships among people and resource to accomplish goals. It is the process of designing the organization structure to fit with its objectives resources and environment. It is the bringing together of all resources (man, money, machine and materials) in order to achieve organizational goals. It has to do with setting up of distinct functional areas with the individuals taking charge. Organizational chart or organogram is a viable tool for communicating each person's position and to whom he is responsible. This aspect helps to minimize conflicts among works.

Leading

This is the process of exerting influence on people to strive willingly and enthusiastically towards the achievement of the organizational goals. It is getting others to do what they do not like to do and like it. It has to do with the interpersonal aspect of managing. It involves clarifying, guiding, teaching and encouraging employees to perform effectively, zealously and confidently. Most problems arise from people. Since leadership implies followership and people tend to follow those who offer a means of satisfying their needs, wishes and desires. Hence, leading involves the appropriate leadership styles and approaches, and communication. Leading presents you as a pacesetter for others to follow, not standing behind the group to push and prod but rather stand in front to facilitate progress. Communication is the transfer of information, ideas, understanding or feelings among people. Motivation is creating an environment that makes staff want to work.

Controlling and Directing:

It is the act of measuring, evaluating, comparing, correcting, regulating and encouraging individuals and organizational performance to ensure conformity to plans. The control process begins after a time frame has been set. Nevertheless, the best option of philosophy is quality

management in term of service or product. This means zero-defect, no tolerance for deviation from standard. Actual results are compared with projected result to determine the level to which objectives have been attained. Control can spread to prevention of crimes by employees, keeping of keys in secure place, observation of shoppers and employees and others that will guarantee smooth running of the organization. Outcomes are controlled by controlling people's activities. There are four elements of controlling

- 1 Established standard of performance (plans).
- 2 Measuring current performance and comparing it with (1) above.
- 3 Detecting deviations from (1) for corrective purpose.
- 4 Taking steps to correct performance that deviates from standard.

These activities generally relate to objective achievement measurement.

Staffing

Staffing is the formal process of ensuring that the organization has qualified workers available at all levels to meet its short and long-term business objectives. This is the process of filling organizational positions with the right persons at the right time, incurring the minimum possible costs and keeping the positions filled. Staffing includes recruitment, selection, training and development, promotion, discipline, welfare, retirement etc. It is the aspect of Personnel Management or Human resource management.

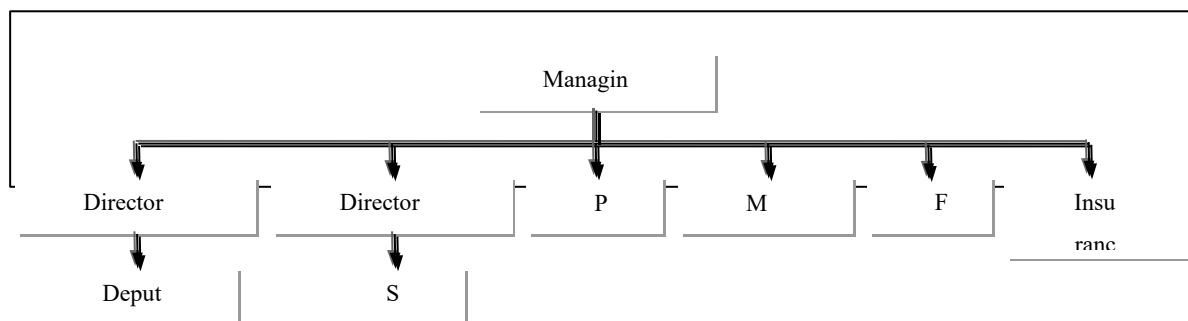


Figure 3: Model of an Organisational chart

Resource Management in an organization. It requires ensuring that the personnel needs are constantly and appropriately satisfied.

Coordinating

This is the essence of a manager. It is the harmonization of individual efforts and managerial functions. In brief, it is the act of synchronizing all the factors of production toward the accomplishment of the set objectives. Each managerial function is an exercise contributing to coordination. It is the central task of reconciling differences in approach, timing and effort to contribute to the plan. It is like an orchestra leader, whose function is to produce coordinated sound, which depends solely on the quality of the director.

Motivation

It is the ability to enable the subordinates to do things which they hope will satisfy their drives, needs, wishes and desires. It is the capability to induce the subordinates to act in a desired manner. It includes providing a conducive environment for performance. Motivation is very complex, but every employee must be self-motivated. There are different theories of motivation that can be used. There are positive and negative reinforcement like cane and carrot, special motivational techniques and so on. Job enrichment must be enhanced in every organisation to motivate adequate delivery from staff. Motivated staff are usually committed to the organisational goals maximally. There are different theories such as Maslow's theory of needs, expectancy etc. that can give credence to the motivations.

3.3 Universal Principles of Management

Principles are very vital in every aspect of life. They are like building blocks on which the structures are laid. The following are reasons for the usefulness of principles in management.

1. To increase efficiency.
2. To give a definite and concrete shape to management.
3. To improve research in management.
4. To attain social goals by increase efficiency in the use of research.

The universal principle of management has been highlighted by Henry Fayol, known as fourteen (14) principles of management are as follow:

1. **Division of work:** This is the first principle, that employees should be given specific task not multi-tasking so as to make them more productive, efficient and skilled on the long run. Work should divided among groups and individuals so as to focus on their portions. Employees are usually specialized in different areas and have different skill sets. As such, Fayol stated that specialization promotes efficiency of the workforce and increases productivity.
2. **Authority:** The responsibility of the manager must be backed up with authority, in order to ensure the employees follow his instructions. The accompanying power or authority gives the management the right to give orders to the subordinates lest he becomes a toothless bull. Authority should commensurate with the responsibility. If authority is more than responsibility, employees get frustrated and if responsibility is more than authority, the manager is frustrated.
3. **Discipline:** States that discipline is a necessity for an organisation to be effective. There must be mutual respect, clearly defined code of conducts and ethics stating roles, rules and regulations for individuals and groups. This management principle is essential and is seen as the oil to make the engine of an organization run smoothly.
4. **Unity of Command:** This means that an individual employee should receive orders from only one manager and be answerable to that manager and made it clear to him. If tasks and related responsibilities are given to

the employee by more than one manager, this may lead to confusion which may lead to possible conflicts for employees. This principle essentially brings about accountability.

5. **Unity of direction:** This principle is that an organisation should move towards a common goal being focused, in harmony and unity. All employees deliver the range of activities that can be linked to the same organisational goals and objectives. It these activities must be described in a plan of action. The manager is responsible for this plan and he/she monitors the progress of the defined and planned activities.
6. **Subordination of Individual Interest to the general interest:** Fayol indicated that personal interests are subordinate to the interests of the organization. Organisation should come up with approaches that ensure organisational interest is aligns with the personal interest as closely as possible.
7. **Remuneration:** Remuneration should be sufficient to keep employees motivated and productive. There are two types of remuneration, namely, non-monetary (a compliment, more responsibilities, credits) and monetary (compensation, bonuses etc.). Motivation and productivity are close to one another in terms of the smooth operation of an organization are concerned.
8. **Centralization:** is about the authority for decision making which is usually concentrated to the top management level. However, there is need for decentralization, which is the sharing of authorities for the decision making process with lower levels (middle and lower management). Nevertheless, there should be appropriate balance between the top and lower level in decision making considering the size, nature of work, circumstances and weight of decision to be made.
9. **Scalar chain:** this is basically the hierarchy in an organization. The principle states that there should be a clear line in the area of authority. This

can be seen as type of management structure. Each employee should be aware of their position and who they are to report to in the chain of command.

10. **Order:** This principle states that employees in an organization must have the right resources at their disposal so that they can function properly in an organization. The arrangement of staff and things be made convenient. In addition to social order the work environment must be safe, clean and tidy.
11. **Equity:** This occurs in the core values of an organization. Employees must be treated kindly and equally. They also must be in the right place in the organization to do things right. Managers should supervise and monitor this process and treat employees fairly and impartially.
12. **Stability of tenure:** This principle represents deployment and managing of personnel. This should be in balance with the service that is provided from the organization. Management should strive to minimize employee turnover and attrition but rather staff retention.to have the right staff in the right place. Focus areas such as frequent change of position and sufficient development must be managed well.
13. **Initiative:** Fayol argued that with these management principle employees should be allowed and empowered to express new ideas. This encourages interest, involvement and creates added value for the company. Employee initiatives are a source of strength for the organization. This encourages the employees to be involved and interested.
14. **Esprit de corps (Team work):** This stands for striving for the involvement and unity of the employees. Managers are responsible for the development a team spirit, harness harmony, high morale and unity of purpose among personnel. Esprit de corps contributes to the development of the culture and creates an atmosphere of mutual trust and understanding.

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3.4 Management versus Entrepreneurship

Management is not entrepreneurship. Management is the process of setting objectives and coordinating resources to achieve them while entrepreneurship is the process of introducing a new economic activity into the market place to improve the standard of living of the people. Management is task-oriented while entrepreneurship is innovation-oriented. Whilst management rewards individualism, entrepreneurship rewards team work. Management responds to current competitors while entrepreneurship anticipates future competitors. Management invests in advancing current technology while entrepreneurship explores new and emerging technologies. Management attempts to refine current employee capabilities and skills while entrepreneurship attempts to develop new skill sets. Management has zero tolerance to failure (hire and fire) but entrepreneurship tolerates failure has learning curve. The manager undertakes the duty of management while the entrepreneur is the driver of entrepreneurship.

The manager is a planner, organizer, leader, controller, coordinator and motivator while the entrepreneur is a visioner, opportunity-seeker, creator, innovator, calculated risk-taker etc. Managers are charged with the responsibility to effectively (i.e. doing the right things) and efficiently (doing things right) utilize the resources under their control whilst the entrepreneur is concerned not with what is, but with what can be. The manager finds solution by systematically observing, classifying and studying facts in relation to the problem at hand while the entrepreneur envisions the future, recognize emerging patterns. identify untapped opportunities and comes up with innovation to exploit it. A manager is confined to his world while an entrepreneur creates his world whether as an employee or employer.

Great organisation in the contemporary seek to employ a manager and an entrepreneur. Entrepreneurs in large organisation are champions, they are employed to introduce entrepreneurship in to the existing organisation. However, often, organisation seem to neither require a manager nor and entrepreneur but rather and an individual that will

combine the roles, features and duties of a manager with that of an entrepreneur for survival and competitive advantage. They are called the entrepreneurial manager.

4.0 CONCLUSION

In managing SMEs, it is imperative to understand the actual meaning of management as a concept. The functions and principles as well as distinction between the management and entrepreneurship. This chapter has dealt extensively with these. It is worth of note that the preference should be an entrepreneurial manager for maximum benefit.

5.0 SUMMARY

In this unit, the various schools of thoughts on management were highlighted. The management functions were given full attention while the universal principle of management were exhaustively discussed. The unit ended with management versus entrepreneurship in a nutshell.

6.0 TUTOR MARKED ASSIGNMENT

1. Pick a perception of management and write three reasons that made it appeal to you.
2. Differentiate between management function and management principles.
3. Is a manager the same as an entrepreneur? Discuss.

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Module 2

Unit 6 Strategic Management and Strategic Entrepreneurship

Unit 7 Strategic Marketing and Marketing Strategy

Unit 8 Strategic Marketing Planning Process

Unit 9 Marketing Mix: Pricing Policies and Strategies

Unit 10 Marketing Mix: Products

Unit 11 Marketing Mix: Place (Channels of Distribution)

Unit 12 Marketing Mix: Sales Promotion and Personal Selling

UNIT 6 STRATEGIC MANAGEMENT AND STRATEGIC ENTREPRENEURSHIP

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1.0 INTRODUCTION

Strategic management and entrepreneurship is referred to as strategic entrepreneurship. Strategic management is an aspect of management that concerns corporate organisation basically for a competitive advantage above others. Entrepreneurship in recent times has been typically associated with new business creation, new product, process, market and organisation development, self-employment, owner-manager of small business and offerings by individuals. This is a narrow perspective, entrepreneurship can be found in firms of any sizes and types, inside or outside an organization, profit or non-profit, and business or non-business activities, economic or social in nature. An entrepreneur can feature in the environment as self-employed, employer of labour or an employee. This usher's us to the concept of corporate entrepreneurship in this unit.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- ✓ Distinguish between strategy, strategic management & strategic entrepreneurship.
- ✓ Explain strategic management decision making and the various strategic levels.
- ✓ Understand the concept of Corporate Entrepreneurship and its importance in strategy.
- ✓ Expatiate the strategic pathways to corporate entrepreneurship.
- ✓ Introduce an entrepreneurial culture into an organization.

3.0 MAIN CONTENT

3.1 Strategy, Strategic management and strategic entrepreneurship

A strategy represents a firm's game plans that provides a framework for managerial decisions or a plan of action designed to achieve a long-term or overall aim of the organisation. A strategy reflects a company's awareness of whom, when, where, and for what to compete. It is "the art of planning operations in a way, especially of the movements of armies and navies into favourable positions for fighting." We will however adopt the definition used by aerospace and service conglomerate (Bovee and Thill, 1992). This definition is simple and quite insightful. Whilst strategic is the how, that is, the means and method of achieving the plans. On one hand, strategic management is the set of decisions and actions taken in formulation, implementation, measurement and evaluation of strategies designed to achieve the organisational objectives for a competitive advantage. On the other hand, strategic entrepreneurship is concerned with taking entrepreneurial actions in the strategic perspective. It is the application and/or stimulation of entrepreneurial activity to achieve strategic goals (Kuratko & Audretsch, 2009). Strategic management enhances the entrepreneur to have a competitive advantage over others. While entrepreneurial strategy encompasses the strategic decisions and steps to be competitive innovatively.

3.2 Strategic Management in a Business Decision

Strategic management involves attention to no less than nine areas as shown below.

- i. Determining the mission of the company including broad statement about its purpose, philosophy, and goals.
- ii. Developing a company profile that reflects internal conditions and capabilities.
- iii. Assessment of the company's external environment, in terms of competitive and general contextual factors.
- iv. Analysis of possible options uncovered in the matching of the company's profile with the external environment.

- v. Identifying the desired options uncovered when possibilities are considered in the light of the company mission.
- vi. Strategic choice of a set of long-term objectives and the strategies needed to achieve the desired options.
- vii. Development of annual objectives and short-term strategies combined with long-term objectives and grand strategies.
- viii. Implementing strategic choice decisions based on budgeted resource allocations and emphasizing the matching of tasks, people, strategies, technologies, and reward systems.
- ix. Review and evaluation of the success of the strategic process as a basis for control and as an input for future decision making.

As these nine areas indicate; strategic management involves the planning, directing, organizing, and control of the strategy-related decisions and actions of a business. By strategy, managers make their large-scale oriented plans for interacting with the competitive environment to ensure achievement of organisation objectives.

3.2.1 Levels of Strategy

The decision-making hierarchy of business firms typically contains three levels, as shown below.

- i. At the top is the corporate strategy level, composed principally of the management staff, that is, board of directors, the chief executive and administrative managers responsible for the directional strategy. Typically focused on long-term objectives but may influence near term activities. It is about how to allocate resources across different business units and set up the overarching strategy.
- ii. The second is the Business-level strategy segment, are heads of business units within the company responsible for competitive strategies. It is about

the decisions related to positioning, differentiation, and competitive advantage on which a company can compete in product-market arena or industry. This must translate the general statements of direction and intention of the corporate level into concrete, functional objectives and strategies of individual business divisions or SBUs. While so doing, they strive to identify most profitable and promising market segment.

- iii. The third is the strategic functional level, composed principally of product, geographic, and functional managers. It is their responsibility to develop annual objectives and short-term strategies in such areas as production, operations, research and development, finance and accounting, marketing and human relations. However, their greatest responsibilities are in the implementation of a company's strategic plans. While corporate and business-level managers centre their planning concerns on —doing the right things, managers at the functional level must stress —doing things right. Thus, they directly address such issues as the efficiency and effectiveness of production and marketing systems, the quality and extent of customer service, and the success of products and services in increasing market shares.
- iv. The strategic operational level is a subset of the functional levels like team leaders. They are concerned with the day to-day activities and processes necessary to effectively execute the higher level strategies. Some companies do not have this level.

3.2.2 Characteristics of Strategic Management Decisions

The characteristics of strategic management decisions vary with the level of strategic activity considered. Corporate-level decisions tend to be value oriented, conceptual, and less concrete than those at the business or functional level of strategy formulation and implementation. Corporate-level decisions are also characterized by greater risk, cost and profit potential, as well as by longer time

horizons and greater needs for flexibility. These characteristics are logical consequences of the more far-reaching futuristic, innovative, and pervasive nature of corporate-level strategic activity. Examples of corporate-level decisions include the choice of business, dividend policies, sources of long-term financing, and priorities for growth. See table 1 for details.

Table 1: Characteristics of Management Decisions of Different Levels

	Level of Strategy		
Characteristic	Corporate	Business	Functional
Type	Conceptual	Mixed	Operational
Measurability	Value judgment dominant	Semi-quantifiable	Usually quantifiable
Frequency	Periodic sporadic or	Periodic or sporadic	Periodic
Adaptability	Low	Medium	High
Relation to present activities	Innovative	Mixed	Supplementary
Risk	Wide range	Moderate	Low
Profit potential	Large	Medium	Small
Cost	Major	Medium	Modest
Time horizon	Long range	Medium range	Short range
Flexibility	High	Medium	Low
Cooperation required	Considerable	Moderate	Little

Source:

Regardless of the eventual profitability of strategic plans, several behavioural effects can be expected to stance of the firm. One of the enhancing factor is to introduce an entrepreneurial culture as a fundamental strategy of the organisation.

3.3 . Corporate Entrepreneurship/ Intrapreneurship

Competitive advantage is about the desirable position of an organization to outshine other rivals or competitors. Only corporate or large organisation and sometimes Hi-tech firms can strive for sustainable competitive advantage. Corporate entrepreneurship or intrapreneurship is the introduction of

entrepreneurship into an existing corporate organization. It is often used to depict entrepreneurial behavior inside established medium and large organizations. Sometimes they are referred to as ‘organizational entrepreneurship,’ or ‘intrapreneurship,’ (Morris et al, 2012).

The entrepreneur in-charge is an employee of the organisation and referred to as ‘intrapreneur’ or ‘champion’. He is a person who focuses on creativity and innovation, and transforms a dream, vision or an idea into a profitable venture within the structure for revitalization. Corporate entrepreneurship, by Zahra (1991) is the process of creating new business within established firms to improve organizational profitability and enhance a firm’s competitive position. In other words, it is the strategic repositioning of an existing business to facilitate performance and revenue streams.

Corporate entrepreneurship, therefore, may be formal or informal activities targeted towards the creation of new businesses in established firms by undertaking any form of innovation. It could take place in the main office, branch office or any place of choice with the ultimate aim of repositioning the company’s competitiveness, sustained growth and financial uplift. The term “new resource combinations” is interpreted to be synonymous to ‘innovation’ in the Schumpeterian sense. Whilst, Sharma and Chrisman (1999), perceived corporate entrepreneurship as the process whereby an individual or a group of individuals, in association with an existing organization, create a new organization or instigate renewal or innovation within that organization.

3.3.1. Importance of Corporate and Strategic Entrepreneurship

The motive for entrepreneurship at all levels is for innovation (Schumpeter, 1934; Drucker, 1985). It commences with the urge to identify sources of existing and emerging customer’s dissatisfaction and developing solutions to eliminate that gap (Ramachandran, 2003) strategically.

1. With the onset of intensifying global competition, there is an increasing need for business organizations to become more entrepreneurial in their strategy. If not done, such companies will get stagnated, become obsolete, decline, lose personnel, and eventually die (Kuratko, 2009). That is, to liquidate, stop trading or be out of business. Thus, innovation is necessary as the life blood of an organization.
2. There are fast growing numbers of sophisticated competitors that are ready to push complacent and lethargic traditional firms out of market. Therefore, to ensure continuity in business, firms must be strategic to innovate.
3. The campaign for entrepreneurship is on the increase in publicity, status and economic development, in order to flow with the trend, there is a great need for strategic entrepreneurship.
4. People with innovative skills that are located in unentrepreneurial organizations may be uncomfortable. Young innovative employees may not be conducive remaining in traditional organizations. On one hand, they may seek to transfer their skills to a corporate entrepreneurship while on the other hand; they may strike out on their own to become small-business entrepreneurs (Hamel and Prahalad, 1996). Corporate entrepreneurship will enable a firm to retain and sustain innovative staff and their contributions through strategic management.
5. It is crucial for corporate firms to be entrepreneurial so as to exploit the underutilized resources by outsourcing the internal capabilities that have been lying dormant.
6. Corporate entrepreneurship places pressures on firms to extract more values on existing resources that have value in product market not currently served. It is a means of spreading the risk and cost of product development since other products are arising outside the firm core products. It makes a company to be alive and alert as a pacesetter.
7. Corporate entrepreneurship is necessary to acquire knowledge to develop future revenue streams (Stokes et al., 2010), for international success (Covin and Miles,

2006), and the effective configuration of resources to develop competitive advantages (Kuratko and Morris, 2008).

8. Finally, the power of information communication technology (ICT) influences the spread of rapidly changing consumers' tastes, fashions, ideas and products. Corporate entrepreneurship enhances vigilance in responding to current market trend to avoid being stale and resistance to change. Thus, innovativeness by firms will lead to sustained growth (Lumpkin and Dess 1996), consequently job creation, wealth generation (Acs, 2007; GEM, 2016), improved standard of living and economic development (Venkataraman, 1997; GEM, 2016).

Corporate entrepreneurship makes an entrepreneur to function as an employee rather than an employer in order to salvage the firm from death by introducing entrepreneurial activities into the venture. He could explore either corporate venturing or strategic entrepreneurship as the means of bringing innovation so as to convert the firm into an entrepreneurial organization. Entrepreneurship is developmental while intrapreneurship is restorative. Entrepreneurs start businesses but intrapreneur revitalize to counter stagnation and be competitive.

3.3.2 The Pathways to Corporate Entrepreneurship

The decisions facing a business at this point is strategic, therefore, deserve strategic management attention. It is the corporate entrepreneurship pathways.

Typically, strategic issues have some identifiable dimensions, as shown.

Strategic issues require top-management decisions. Strategic decisions overarch several areas of a firm 's operations. Therefore, top-management involvement in decision making is imperative. Strategic issues involve the allocation of large amounts of company resources. Strategic decisions, characteristically, involve substantial resource deployment. The people, physical assets, or moneys needed must be either redirected from internal sources or secured from outside the firm. In either case, strategic decisions commit a firm to a stream of actions over an extended period,

thus involving substantial resources. Thus, if a firm is to succeed in positioning itself in future competitive world, its strategic managers must look beyond the limits of the firm's ownership. They must consider what other relevant factors (e.g., competitors, customers, creditors, government, and labour) are likely to do.

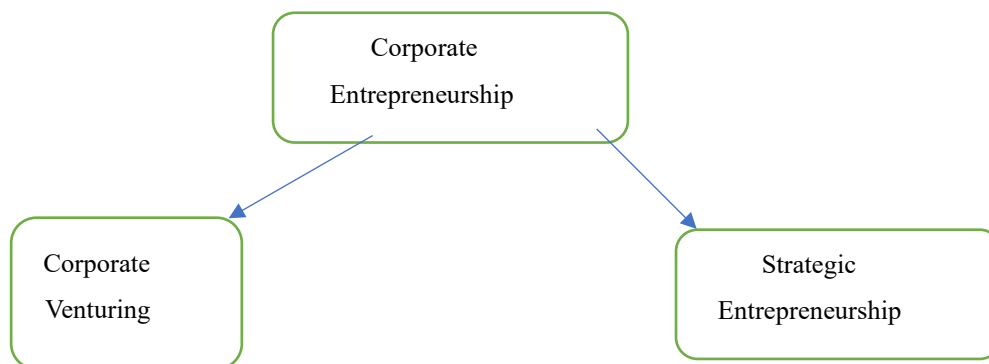


Figure1: Pathways to Corporate Entrepreneurship
Source: Adeyeye (2014)

The corporate entrepreneurship pathways as two distinct but related dimensions: corporate venturing and strategic entrepreneurship. They are directional decisions to be taken at the corporate level.

3.3.2.1 The Corporate Venturing

The first pathway to achieve this is by the corporate venturing. Corporate Venturing simply means 'capital venture investment activity'. It is the different ways of 'introducing, creating, adding to, or investing in new business within an existing company'. It could be implemented through internal, cooperative or external corporate venturing (Morris et al., 2012 p.81). It is mainly for sustainability, firms that are struggling and about to collapse can choose all or any of these. A firm must stand before considering being competitive.

i) Internal corporate venturing is about new ventures being created within the corporate structure of the organization and owned by that company. The new

venture may be established in the vicinity other than where the organization is situated or domiciled within the existing firm but with a certain level of autonomy.

ii) The cooperative corporate venturing or collaborative venturing. As the name implies, it is the creation and joint ownership of an entirely new venture by the company together with one or two other companies or individuals as stakeholders.

iii) The external corporate venturing, that is, the acquisition of or an investment in a young firm in its early growth stage by a company in order to exercise its entrepreneurial behaviour. Thus, a firm's total entrepreneurial activity is equal to the total of the ventures enacted through the internal, cooperative and external modes (Kuratko, 2013).

3.3.2.2 The Strategic entrepreneurship

Corporate entrepreneurship is the spark and catalyst that is intended to place firms on the path to competitive superiority or keep them in competitively advantageous positions. Hence, the second main pathway to attain Corporate Entrepreneurship is through strategic entrepreneurship.

Strategic entrepreneurship is an array of entrepreneurial behaviours, activities and initiatives that are adopted and capitalized upon, in pursuit of competitive advantage. It is the innovation that differentiates a company from others in the industry. Strategic entrepreneurship can be expressed in five ways: Strategic renewal, sustained regeneration, domain redefinition, organizational rejuvenation and business model reconstruction (Covin and Miles, 2006).

i. The Strategic renewal, according to Guth and Ginsberg (1990) is the transformation of organizations through renewal of the key ideas on which they are built. Examples of such are redefinition of the business concept, reorganization, and the introduction of system-wide changes. It implies the implementation of a new business strategy that differs significantly from previous practices in ways that better leverage the firm's resource. It is to fully exploit the

available product-market opportunities or reposition itself within its competitive space.

ii. **Sustained regeneration**, which is the act of regularly and continuously introducing new products and services or entering new markets. Such firms tend to be learning organizations that embrace change and willingly challenge competitors in battles for market share. Simultaneously, they cull older products and services from their lines in an effort to improve overall competitiveness through product life cycle management techniques.

iii. **The domain redefinition**. This is the label used for the CE phenomenon that the organization proactively creates or actively seeks to exploit a new product-market arena that is unrecognized by others. The firm in effect imprints the early structure of an industry and assumes a pioneering or early mover status that is hoped to produce some bases for sustainable competitive advantage. Under such a scenario, the entrepreneurial firm may be able to create the industry standard or define the benchmark against which later entrants are judged. Thus, firms that engage in domain redefinition are entrepreneurially strategic by the fact that they exploit market opportunities in a pre-emptive fashion, redefining where and how the competitive game is played in the process (Morris et al., 2012).

iv. **Organizational rejuvenation**. This enables organization to sustain or improve its competitive stand by altering its internal processes, structures, and/or capabilities. It is sometimes perceived as organizational renewal (Hurst, Rush, & White, 1989) often adopted by firms that need not change their strategies to be entrepreneurial. It involves efforts to sustain or increase competitiveness through the improved execution of, pre-existing business strategies. Improved strategy execution via organizational rejuvenation frequently entails actions that reconfigure a firm's value chain (Porter, 1980) or otherwise affect the pattern of internal resource allocation. For example, Procter and Gamble has been able to greatly improve its inventory and distribution systems in recent years through the extensive adoption of bar-coding technology. This technology has not only

revolutionized the entire outbound logistics function within P&G but also enabled the firm to sustain its position as a leading consumer products company by setting the customer service standard as a measure against which other competitors are judged.

v. **The business model reconstruction.** A business model is a concise representation of how an interrelated set of decision on venture strategies are addressed to create sustainable competitive advantage in a specified market. Business model symbolizes the “stories that explain how enterprises work”. Example of such model is Dell computer with its direct sales model within the established Hi-tech industry. Similarly, is the eBay creation of a new industry with its online auction model. Business reconstruction model, therefore, is about a firm redesigning its core business model(s) to improve its operational efficiencies or distinguish itself from competitors in ways valued by the market. Such reconstruction could be done by outsourcing (use of external suppliers to perform previous activities carried out within the firm) or vertical integration. A prominent example is Apple Computer that adopted business model reconstruction by the introduction of iPod and iTunes online music service was propelled to a leading position within its industry from its proprietary software design niche player. The journey through these pathways is not simply a matter of managerial choice since the outcomes of entrepreneurial processes are uncertain. However, most paramount and compelling is the entrepreneurial philosophy that must permeate the entire organization's climate in outlook and operations to serve as a platform for corporate.

3.4 Entrepreneurship culture

It is an organizational culture that includes entrepreneurship in his vision and mission thereby encouraging continuous innovation as the lifestyle of the firm. It is the culture that encourages innovation as a way of life among all cadre of employees and every facet of the organization. It is a culture that promotes and rewards creativity and innovation. It breaks every bureaucracy and conventions

to have a favourable environment. It inculcates entrepreneurship concept in its work, moment and life in the firm.

Establishing an entrepreneurial culture in an organization, management experts encourage large organizations to exert strategies like downsizing, right sizing, and budget-cuts to overcome their saggy economies. However, the entrepreneurial perspective encourages firms to become entrepreneurial to flounder through the economic challenges in the business environment. Firms' orientation and culture must become entrepreneurial to guarantee the ideal atmosphere for entrepreneurship. The culture of an organization is its way of life, basic beliefs, and assumptions in an organization. In one of the earliest studies, Peterson and Berger (1971) show that entrepreneurial culture helps companies to develop new businesses that create revenue streams. Such culture enhances a company's success in promoting innovations. It is the ground on which the seed of entrepreneurship germinates. Nevertheless, certain fabrics must exist to support or promote entrepreneurial behaviour (Sharma et al., 2007). Foremost, is the employment of enthusiastic staff that can champion entrepreneurial initiatives and climate. The inception and maintenance of an entrepreneurial culture must be preceded by the following conditions:

- ❖ Encourage and support new ideas (creativity) even if it appears odd with short term profit because the more ideas the more innovations.
- ❖ Encourage trial and error by allocating time for employees to brainstorm and experiment, especially by allowing the technical people to spend about 15 percent of their time working on whatever they want.
- ❖ Encourage multi-skilled teams through networking and collaborations but keep divisions small.
 - ⊞ Allow and tolerate failure, no failure means no innovation. Failure is a learning curve.
- ❖ Allocate adequate resources for research and development (R&D) and also cutting edge operations in particular corporate venturing or strategic entrepreneurship of choice.
- ❖ Allow approval with/out management authorization or supervision for employees to keep rolling out new ideas. This will also serve as inspiration for others to do the same.
- ❖ Persist in getting an idea to market, do not kill a project.

- ❖ Encourage personnel to circumvent rigid procedures and bureaucratic red tape.
- ❖ Structure the organogram of the firm to encourage informal communication and informal meetings whenever possible.
- ❖ Create a system of feedback and positive reinforcement by rewarding any innovation for innovation's sake and moreover, reward and promote innovative personnel.
- ❖ Emphasize personal commitment and responsibility because confidence, trust and accountability are main features of successful innovative programs.
- ❖ Stay close to customers.
- ❖ Use the language, acronyms, jargon, slangs, signs, slogans, metaphors, gossip, gesture, and songs that portray innovation. [Adapted from Kuratko and Hodgetts (2008) and Stokes et al. (2010)]. When the following conditions are largely met, the climate turns entrepreneurial and becomes a platform for entrepreneurial initiatives to thrive in an organization.

4.0 Conclusion

In this unit, the concepts of strategy, strategic management and strategic entrepreneurship were distinctly clarified. The essence of strategic management and entrepreneurship were basically established for sustainable competitive advantage especially for pursuit in corporate Organisations.

4.0 Summary

Strategy is a noun but used as an adjective that qualifies and differentiates another noun like management and entrepreneurship in this context for strength to stand out and excel above the equals. There are dimensions to strategy as well as levels of strategic plans for orderliness and accomplishment. The concept of corporate entrepreneurship was elucidated and the need for entrepreneurial culture to foster innovation was discussed.

6.0 TUTOR MARKED ASSIGNMENT

- 1 . What are the differences among strategy, strategic management and strategic entrepreneurship?
2. What differences are the differences in entrepreneurship and intrapreneurship?

How would you convert the normal organisational structure into entrepreneurial culture?

4. Clearly discuss the characteristics of strategic management dimensions.

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UNIT 7: STRATEGIC MARKETING AND MARKETING STRATEGY

CONTENT

1.0 Introduction

2.0 Objectives

3.0 Main Content

3.1 Strategic marketing, Marketing Strategy and Managerial Marketing

3.2 Sources of Competitive Advantage

3.3 Functional Strategic Areas

3.3.1 Principal Strategic Options

3.4 Reasons for Strategic Plans Failure

4.0 Conclusion

5.0 Summary

6.0 Tutor-Marked Assignment

7.0 References/Further Reading

1.0 Introduction

In this unit, marketing role is to communicate a consistent message to the ideal customer. Discover what customers want and need as well as what price they will pay. Knows where to find customers that will most likely buy. Builds foundation for sales through multiple channels. In short, marketing creates the sale opportunity. We are going to discuss the concept of marketing strategy and define Planning. We will also discuss the importance of planning, the types of planning, principles of planning, the planning process and how to evaluate it and the elements of planning.

2.0 Objective

At the end of this unit, students would be able to:

- Understand the concepts of Strategic marketing, Marketing Strategy and managerial marketing;
- Discover the sources of competitive advantage;

- Identify the functional strategic areas;
- Explain the different principal strategic options; and
- Elucidate the various reasons for strategic plans failure.

3.0 Main Content

3.1 Strategic Marketing, Marketing Strategy and Managerial Marketing *Strategic marketing*

Strategic marketing focuses on the choice of marketing policies aiming at improving the competitive position of the firm by taking account of challenges and opportunities discovered in the competitive environment. It is an approach that aligns every marketing scheme with the overall business goals to build a sustainable competitive edge. Furthermore, it deals with the high-level functions like products strategy, branding, and reputation marketing.

The marketing strategy

The marketing strategy is the foundation of a marketing plan. Marketing Strategy is an organisation's strategy that combines all its marketing goals into one comprehensive plan. A good marketing strategy should be drawn from market research and focus on the right product mix to achieve the maximum profit potential and sustain the business. It is tied to carrying out specific plans for individual product or services. It is the analysis of the strategic initial situation of a company and the formulation and selection of market-oriented strategies that contribute to the goals of the company, implementation, measurement and evaluation. The marketing strategy then involves segmentation, targeting (target market selection), positioning the product within the target market, value proposition to the target market

Managerial marketing

Managerial marketing or marketing management is the use of marketing, techniques, methods, orientation and all business activities which direct the movement of goods from the producer to the consumer for satisfaction and accomplish the organisational goals. It has the fundamental goal of increasing sales and achieving a sustainable competitive advantage. It includes all basic, short-term, medium –term and long-term activities in the field of marketing. It is the processes, strategies and tools applied to promote their product or services.

3.2 Sources of Competitive Advantages

Competitive advantage is very salient if the business must thrive. Every competitor's wish is to dominate the market and push the next business out of trade. There are different sources of competitive advantage. Few will be discussed her.

1. **Defining the rules of the game:** This is setting a high standard on the product quality, price, distribution channel, and warranties after sales service, promotional appeals and budgets. When the standard is set, no Dick and Harry can just come in without meeting the standard. This might not be very easy for new entrants.
2. **Captioning of market segment:** Win the heart of the market segment so much that your product or service becomes the standard of assessment of another brand. This could be done by captivating a segment before going into another segment.
3. **Distribution channel:** This is a well-designed and easy method of distribution with retailers and wholesalers. In these days of Information Communication Technology (ICT), the E-distribution will be of great advantage. A network of the renowned and effective distributors is an advantage. When it is taken advantage of, at a good time, distributors are often reluctant at taking second or third brands. This makes your product dominant the market.
4. **Economics of scale and experience:** Come out on a large scale or accept inevitable cost disadvantage. Increase in production means decrease in cost and unit price lowered. This will afford opportunity to give discounts to customers. Cash discount is reduction

in price to encourage prompt payment while trade discount is given to encourage bulk purchase. 10% reduction on the invoice price if you purchase up to 6 dozen and above. This in turn will increase the rate of turn over (net sales) and higher profitability.

5. Product differentiation: This is by trying to find ways of overcoming existing brand loyalty by customers so that your own product or brand will be more acceptable. Distinguish your products by making it unique to win customers' preference.

6. Capital requirements: This is a considerable sum of money that must be invested on sales promotion, research and development, preliminary expenses etc. in order to increase sales.

7. Switching costs: This is the use of modern or local technology for an innovation that will not make switching over by competitors very cheap. It will consequently close the market for a long time to competitors while you take advantage of situation.

8. Government policy: This often happen through licensing and legal regulations. Government can limit or prevent new entrants into the industry if there is much proliferation.

3.3 Functional Strategic Areas

Strategies could be developed in all its functional area of the enterprise, for examples;

i. Product strategies: This is when organization intends to (a) Maintain existing products, (b) develop a range of new products, (c) focus on product quality and value-for – money, (d) continuously improve product performance, (e) deliberately build in obsolescence/short – shelf – life span into our products, (f) employ the latest technology for production and distribution processes, (e) drop unprofitable products from our range vehemently and (g) maintain inventories at lowest possible levels.

ii. Market strategies: This is when management and staff agreed to (a) concentrate on current markets, (b) seek to develop new markets locally and internationally, (c) concentrate on identifying and supplying specialists market segment (niche), (d) maintain existing brands, rebranding and repackaging (e)

develop new brands, (f) strive consistently for price advantage over our competitors, (g) determine value provision for our customers and (h) constantly promote the company's reputation for quality/rehabilitate (i) seek new customers for existing/new brands (J) Rearrangement and redisplaying the products.

iii. Financial strategies: This is when company intends to (a) increase the level of borrowing (leverage) to fund new developments, (b) reduce the extent of debtors' liabilities, (c) increase proportion of retained profits, (d) maintain tight budgetary control over expenditure, (e) acquire suitable companies and/or negotiate joint ventures to achieve desired market position.

iv. General strategies: These are other strategies that are employed, apart from the ones mentioned above, such as for personnel. The company may decide to (a) retain and develop skilled care personnel, (b) bring in temporary and/or casual staff when required, (c) provide continuous training and updating of managerial staff, (d) encourage share participation amongst all core employees, (e) constantly update mechanisms for facilitating strategic change and developing learning through the organization.

3.3.1 Principal Strategic Options

Strategy formulation can take place at any time and at more than one level, depending on the firm's size and shape. It is answering the question on what to do next in the light of what has been discovered? This is the time for decision-making, to make choices between alternative ways forward and time to focus on the priorities. The following principal strategic options are open to an enterprise.

- i. Consolidation (following previous strategy for stabilization).
Market penetration (a similar approach i.e. building on the current approach being employed).
- ii. Market development (taking present product into new market).
- iii. Product/service development (introducing new products into existing market).
- iv. Diversification (branching out with new products/services in new markets).

- v. Price leadership (offering the keenest prices in the market).
- vi. Differentiation (developing a product or service that is seen as unique in the industry).
- vii. Niche strategy (strengthens market position in one or few segments with potential for continued profit).
- viii. Growth through acquisitions or purchases and/ or joint ventures.
- ix. Divestment or Divestiture (selling off part of the business/subsidiaries etc., in early stage of decline).
- x. Withdrawal (selling up entirely or closing or liquidation)
- xi. Skimming and early withdrawal (quick sales, maximize profit and withdraw as competitors' rush
- xii. Mass market penetration (captures and maintains a commanding share of the market and build large contingent of customers before competitors come in).
- xiii. Fortress or position defence strategy (improves customers' loyalty and satisfaction and make offering more attractive to new customers).
- xiv. Flanker strategy (a lower quality product designed appealing to a low-price segment instead of allowing them to fall into a competitor's hand).
- xv. Confrontation strategy (almost being pushed out by competitors, attack its flank or look for his failure or loophole, re-establish the competitive advantage and re-engineer.)
- xvi. Market expansion or mobile strategy (almost pushed out by competitors, concentrate on market broadening and diversification – focus on your competitors' weakness).
- xvii. Contraction or strategic withdrawal (competitors are more powerful, withdraw from where it is most vulnerable and concentrate on the areas you can capture).
- xviii. Frontal attack (on relatively homogeneous product, lower cost or differentiated position in the market).
- xix. Leapfrog strategy (not with capital products. Offering a product that is attractively differentiated from the competitors offering especially with more superior technology).

- xx. Encirclement attack strategy (targeting several smaller untapped or underdeveloped segment for a unique attack).
- xxi. Guerrilla attack strategy (use of sales promotion like coupon drops, merchandising deals (send three bottle tops for a free drink), short-term price reduction etc.).
- xxii. Maintenance strategies (continue with sales promotion; focus sales force etc. or anything to maintain your customers).
- xxiii. Profitable survivor strategy (increase your share as others pull out encouraging weak competitors to pull out of business).
- xxiv. Horizontal integration strategy (acquisition of firms that supply it with inputs (raw materials) or customers for its outputs)
- xxv. Concentric diversification (distinctive departure from a firm existing base of operation and acquisition of business that are related in terms of technology, markets or products).
- xxvi. Conglomerate diversification (a very large firm acquiring a business because it represents the most promising investment opportunity).
- xxvii. Turnaround strategy (the business streamlines its operation and eliminates wastes and inefficiencies through retrenchment and re-engineering to gain new strength)

3.4 Reasons for strategic plans failure

Strategic plans may fail due to many reasons that may not be far from the following under listed:

- Failure to understand the customers. (Why do they buy? Is there a real need for the product? Is there any inadequacy incorrectness in marketing of the product?)
- Inability to predict environmental reactions. (What will competitors do? Fighting brands? Price wars? Will government intervene?)
- Over-estimation of resource competence. (Can the staff, equipment, and processes handle the new strategy? Failure to develop new employee and management skills)
- Failure to coordinate (reporting and controlling relationships inadequately, inflexibility of the organizational structure).

- Failure to obtain senior management commitment (failure to get management involved right from the start. Failure to obtain sufficient company resources to accomplish task).
- Failure to obtain employee commitment (new strategy not well explained to employees, no incentives given to workers to embrace the new strategy).
- Underestimation of time requirements (no critical path analysis done).

Entrepreneurs need to engage in strategic marketing for sustainability of the competitive advantages over competitors. They should also guard against probable failure symptom.

6.0. Tutor-marked Assignment

- a. How would you distinguish between a functional and principal strategic option?
- b. Define these concepts: Strategic Marketing, Marketing Strategy and Managerial Marketing.

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UNIT 8 STRATEGIC MARKETING PLANNING PROCESS

CONTENT

1.0 Introduction

2.0 Objectives

3.0 Main Content

3.1 Steps to Strategic Marketing Planning Process

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3.1.2 Marketing Objectives

3.1.3. Positioning and differentiation

3.1. 4 Target Market and Market Demand

3.1.5 Designing a Strategic Mix

3.2 Marketing Process

3.3 Annual Marketing Planning

3.2.1 Purposes and Responsibilities of an Annual Marketing Plan

3.2.2 Contents of an Annual Marketing Plan

3.4 The marketing plan

4.0 Conclusion

5.0 Summary

6.0 Tutor-Marked Assignment

7.0 Further Reading

1.0 INTRODUCTION

In this unit, we are going to discuss the strategic marketing planning process; that is the situation analysis, marketing objectives, positioning and differential advantage, target market and market demand and the marketing mix. It will also discuss the annual marketing plan, the purpose and responsibility of an annual marketing plan and contents of an annual marketing plan.

2.0 OBJECTIVES

At the end of this unit, students will be able to;

- Understand and explain the strategic marketing planning process
- Market Assessment and its important
- Develop, discuss and know the purpose, content and responsibilities of the annual marketing plan.

3.0 MAIN CONTENT

3.1 Steps to strategic marketing process

Strategic marketing planning is a five-step process. With the plans in place, the marketing programmes are implemented, while the results are monitored. If the Plans work well, the feedback provides the good news. However, if the marketing programme does not meet expectations, the feedback mechanism helps marketers adjust the processes. You should realize that strategic marketing planning is a controlling process, not a one-time event. Therefore, continuous monitoring and feedback is the surest way to stay in touch with dynamic market conditions.

We have already noted that strategic marketing planning is a five-step process as listed below:

- (i) Conduct a situation analysis/ market Assessment
- (ii) Develop marketing objectives.
- (iii) Determine positioning and differential advantage.
- (iv) Select target markets and measure market demand.
- (v) Design a strategic marketing mix

Let us carefully discuss each as their steps:

3.1.1 Framework for Situation Analysis/ Market Assessment

Situation analysis is the first step in a strategic marketing planning. Market assessment refers to the process by which information is collected and analysed based on which marketing opportunities and problems identified. This information is about past performance, current market position, future trends, etc. It serves as the basis for identifying opportunities to satisfy unfulfilled customer needs. In addition, the firm must understand its own capabilities and the environment in which it is operating. The situation analysis should include past, present, and future aspects. A history outlining how the situation evolved to its present state, and an analysis of trends to forecast where it is going. Good forecasting can reduce the chance of spending a year bringing a product to market only to find that the need no longer exists. If it reveals gaps between consumers want and what currently is offered, there may be opportunities to introduce products to better satisfy those consumers. Hence, the situation analysis should yield a summary of problems and opportunities. From this summary, the firm can match its own capabilities with the opportunities to satisfy customer needs better than the competitors. There are several frameworks that can be used to add structure to the situation analysis:

- **5C Analysis** - company, customers, competitors, collaborators, climate. Company represents the internal situation; the other four cover aspects of the external situation

- **PEST analysis** - for macro-environmental political, economic, societal, and technological factors. A PEST analysis can be used as the "climate" portion of the 5 C framework.
- **SWOT analysis** - strengths, weaknesses, opportunities, and threats - for the internal and external situation. It can be used to condense the situation analysis into a listing of the most relevant problems and opportunities and assess how well the firm is equipped to deal with them. The application of SWOT analysis to competitors is part of a larger effort known as *competitor intelligence*, which is a systematic process of understanding competitions and their influence on your markets.

When carrying out a SWOT analysis, this tool focuses on the entrepreneur and the potential competitors. Strength and Weakness are internal to the business or product whereas the Threats and are Opportunities are external aspects on the business or product. These aspects may focus on number of items as seen below.

1. **Strength.** These are the strong points or things that put the businessperson at an advantage when compared to their competitors they are internal under business strength; one may look at aspects such as ➤ Increasing sales.
 - Excellent marketing techniques.
 - Having good customer care, ➤ Having a good location business site.
 - Very good business reputation.
 - A good brand name.
 - Good public relations.
 - High quality products.
 - Attractive packaging facilities.
2. **Weakness.** These are the constraints for limitations that the business or product may encounter in the market arising from within the business or product itself, Weaknesses are internal to the market. Weaknesses may be manifested in the following forms.

- Few customers.
- Limited financial resources.
- Poor and inefficient marketing skills.
- Location of selling points not being convenient.
- High costs of productions.
- Having a small sales team.
- Weak distribution network.
- Unreliable supply of inputs.

3. **Opportunities.** Opportunities are external advantages that may exist in the surrounding and can benefit the business. It is important to note that the business has no direct control over such factors. In case they happen, the business takes advantage of their opportunities available.

These include: -

- Reducing number of competitors in the market.
- A shift in the tastes and preference of customers in favour of the business' products.
- An expanding market.
- Possibility of merger with a large competitor.

4. **Threats.** These are external undesirable events or occurrences which may take place in the market to the disadvantage of the business or products.

Threats can be in form of.

- Scarcity of raw materials in similar products.
- Setting up of new business dealing in similar products.
- Reduction in population thus the available market, ➤ Lowering prices by the competitors.
- Increasing sales of substitute goods.
- Negative change in tastes & preferences of the products in question.
- Higher taxes (increments in Taxation).
- Entry of lower cost firms in the market.

Procedures to assessing a given product

1. Select the given product {good or service} for the assessment.
2. Choose the market area for the assessment.
3. Decide on the approach and methods to be used in assessment.
4. The development and validation of data collection instrument(s) on information regarding to price, product, place, positioning and promotion.
5. Analysis of the data collected
6. Analyse the proposed market strategy.
7. Assess the feasibility and viability of the selected products in the market.

3.1.2 Marketing Objectives

This is the second step in strategic marketing planning. A company strategy usually translates into a marketing goal. For example, to reach an organizational objective of a 25 percent return on investment next year, one company strategy might be to reduce marketing costs by 20 percent. Thus, this company strategy could become a marketing goal. Since strategic management involves matching an organisation's resources with its market opportunities. Each objective should be assigned a priority based on its urgency and potential impact on the marketing area, and, in turn, the organization. These priorities should be the basis for allocating the company's resource. Generally, it is recommended that each objective should be SMART, an acronym for Specific, Measurable, Attainable, Realistic, and Time-bound. It helps to push further, give sense of direction, and organised to reach the goals.

3.1.3 Positioning and differential advantages

Two complementary decisions are involved in the third step of strategic marketing planning. The process of achieving a desired position in the mind of the market is called positioning. For instance, you can position your company, your products, your technologies, or any other entity that commands customer attention. After

the product is positioned, a viable differential advantage should be identified. Differential advantage refers to any features of an organization or brand perceived by customers. Examples of positioning includes:

- 1. Marketing presentation:** A relatively low price may be set to stimulate the growth of the market and to increase the firm's market share. Certain conditions may favour the setting of the low prices, such as to discourage actual and potential competitors, if the unit production and the distribution costs are reduced with an increase in volume or where the market appears to be highly sensitive.
- 2. Market skimming:** A high price may be set up to take advantage of the buyers who attribute a high prestige value to the product and are willing to pay high prices for it. However, the prices may gradually be lowered as the value attached to the product diminishes, and the buyer becomes price conscious.
- 3. Satisfying objective.** The price is set to achieve a rate of return suited to the business objectives and the character of the entrepreneur. Some may set prices to maximize returns but with a lot of uncertainties, yet others may be satisfied with lower returns with less problems and difficulties.
- 4. The product line promotion:** The entrepreneur may establish a price that will promote sales of the entire product line e.g. a loss leader pricing in which a proper product item is lower or even at a loss to attract buyers to buy a whole set or induce many buyers to buy other product of the enterprise.
- 5. Early cash recovery:** A price might be set up that will lead to a rapid recovery of cash either because of cash needs of the business, short life cycle of the product or future uncertainty of the business.

Marketing skills for Positioning

Marketing skills have to do with finding out consumers 'wants, planning and developing products or services that will satisfy those wants, determining the best way to price, promote and distribute those products or services. Marketing is the

process by which the productive potentials of the company is used to satisfy individual and social needs of all kinds. Marketing can also be explained as making available a product or service at the place, at the time and in the form in which they are required by customers. It also includes provision of services as an integral accompaniment of products, investigation of customers' needs and initiation of a product or service to satisfy customers' needs.

These marketing skills are required: -

- i) knowledge of seasonal fluctuation of goods;
- ii) ability to determine the extent to which products will sell; iii) familiarity with various aspects of sales and salesmanship; iv) ability to budget and forecast; v) ability to determine current trends in sales of products; vi) ability to determine what customers need and shortage of such goods;
- vii) knowledge of advertising; viii) ability to determine and interpret factors which indicate extent of and strength of competition; and ix) ability to determine availability of goods/raw materials for product and shortage of finished goods.

Others competencies skills needed:

- I. salesmanship;
- II. negotiation;
- III. sales record keeping;
- IV. sales promotion;
- V. stock record keeping.
- VI. pricing;
- VII. advertising channels;
- VIII. advertising media;
- IX. consumer behaviour appreciation; and X. transportation.

Operationalised marketing skills using seven aspects namely;

- a. ability to apply competitive strategies (e.g. cutting prices, improve quality, design new products, packages, fashion, colour, etc (Innovativeness.);
- b. ability to develop a marketing budget (Risk-taking);
- c. ability to identify new markets and/or customers (Innovativeness.);
- d. ability to respond quickly to competitive forces (Proactiveness);
- e. ability to identify and satisfy customer needs (Innovativeness);
- f. ability to identify competitors' strength and weaknesses (Proactiveness); .

3.1.4 Target marketing and marketing demand

The fourth step in strategic marketing planning is the selection of target markets. A target market refers to a group of people or organizations or a niche at which a firm directs a marketing programme. Regarding an existing firm, management should routinely examine any changes in the characteristic of its target markets and alternative markets. It has been suggested that target markets must be selected based on opportunities. To analyse these opportunities, a firm need to forecast demand or sales in its target markets. The results of such demand forecasting will indicate whether the firm's targets are worth pursuing, or whether alternatives need to be identified and shared.

Determinants of the target market population

- 1. Income levels.** This refers to the earnings of different categories of people.
- 2. Consumption habits.** This looks at the behaviour of consumers in consuming different products.
- 3. Business competitors.** This refers to business which are dealing with and selling similar products and services.
- 4. Age and sex composition of a particular group of people.** Different age groups and sex may require a variety of different specified products and colours.

5. Market share of the business. The quantification of how many potential customers exist in an area and estimate how many can be attracted from his competitors.

5. Economic trend over time or fashions. An entrepreneur should put into consideration the following factors when determining the target market population.

- (i) Population shifts i.e. are more coming in to live in the target area, changes in population.
- (ii) Legal or regulatory developments (change)
- (iii) Changes in the economic situation e.g. are there more people getting employed? Are there more goods being sold? Lifestyle changes. etc.
- iv) Are cheaper goods being sold?

There may be need to conduct a market research to arrive at the right target market and market demand.

Market research

Market research is a study aimed at identifying the market gaps to be filled in the market. It is needed to identify the niche and measure market demand. The techniques are usually non-probability because any case could be included in the sample size since there is no sampling frame. It is a non- random sampling with a range of alternative techniques to select samples. Quota sampling, purposive, snowball, convenience sampling etc. that are not acceptable for academic research are used for sample selection if it is appropriate and relevant for the investigation. The methods could be survey, case study, observation, experimentation, interviews etc. The objectives include:

1. To know your competitors' strength and weakness so as to convert their weaknesses to your strength.
2. To establish the opportunities of the product over others.

3. To check the effectiveness of the promotion or advertising methods.
4. To know the potential customers of the business.
5. To find out whether there are problems and know the areas of expansion to meet the customer needs.
6. To enable sensitization of the product without launching expenses.

Market research respondents

The market research respondents would include any one or more on this list.

- 1. Employees (workers):** They are often aware of customers' requests that are not available and their complaints. They probably also give a good profile of the customers from their day to day interactions and contacts.
- 2. Customers:** Encouraging and collecting customer's comments is an effective form of research which involves asking customers to explain how the product could be improved to satisfy their needs. Constructive market research is done as well as instilling customer's confidence in the product.
- 3. Competitors (competition):** Monitoring the competitors can be a valuable source of information. Small business owners can capitalize on unique points of their products that their competitors do not offer.
- 4. Company records and files:** Examining company records and files can be very informative. E.g. looking at the sale records, complaints, receipts or any other records can reveal where the customers live or work, their preference, amount purchased, etc. With this kind of information, he could cross Reference to customer's address and product they purchased. This helped him check the ineffectiveness of his advertising.
- 5.** Data can also be obtained by the business through visiting shops, making observations, interviewing, questionnaire, telephone survey, etc.

3.1.5 Designing a Strategic Marketing Mix

The last step in the strategic marketing planning process is the designing of an appropriate marketing mix, i.e. the combination of product, price, promotion and distribution (place). These four elements were the initial mix but as research increased it became 8 Ps. These should collectively satisfy the needs of the organisation's target markets and, at the same time achieving marketing process plan. Marketing Mix is a tool used by businesses and marketers to determine a product or brands offering. The 8 Ps have been associated with the Marketing Mix since their creation. A mix is made of ingredients that are blended to meet a common purpose. As with a cake, it must be blended together to produce something very special. In the same way that there are many cakes to suit all tastes, a marketing mix can be designed to suit the precise requirements of the market.

The elements of marketing mix: 8 Ps

Marketing mix is the combination of the marketing variables that creates an integrated and consistent offering to potential customers that satisfies their needs and wants. Creating the right mix, when marketing their products, from (business) need to create a successful mix of;

□ The right product.

- In the right place
- Using the most suitable promotion
- Sold at the right price

Thus, the marketing mix includes.

- **Product** - The Product should fit the task consumers want it for, it should work and it should be what the consumers are expecting to get.
- **Place** – The product should be available to where the target consumer finds it easiest to shop. This may be High Street, Mail Order or the more current option via e-commerce or an online shop.

- **Price** – The Product should always be seen as representing good value for money. One of the main tenets of the marketing concept is that customers are usually happy to pay a little more for something that works really well for them.
- **Promotion** – Advertising, PR, Sales Promotion, Personal Selling and, in more recent times, social media are all key communication tools for an organisation. These tools should be used to put across the organisation's message to the correct audiences in the manner they would most like to hear, whether it be informative or appealing to their emotions etc,
- **People** – All companies are reliant on the people who run them from front line Sales staff to the Managing Director. Having the right people is essential because they are as much a part of your business offering as the products/services you are offering.
- **Processes** –The delivery of your service is usually done. Mode of service delivery is part of what the consumer is paying for.
- **Physical Evidence** – Almost all services include some physical elements even if the bulk of what the consumer is paying for is intangible. For example, a hair salon would provide their client with a completed hairdo and an insurance company would give their customers some form of printed material. Even if the material is not physically printed, they are still receiving a —physical product by this definition.
- **Productivity & Quality** - This P asks —is the customer offering a good deal? This is less about you as a business improving your own productivity for cost management, and the emphasis is more about how your company passes this onto its customers.

3.2 The Marketing Process

Under the marketing concept, the firm must find a way to discover unfulfilled customer needs and bring to market products that satisfy those needs. The process of doing so can be modelled in a sequence of steps: the situation is analysed to identify opportunities, the strategy is formulated for a value proposition, tactical decisions are made, the plan is implemented, and the results are monitored.

The Marketing Process



I. Situation Analysis

The situation analysis thus can be viewed as an analysis of the internal and external environment of the firm itself. The marketing environment consists of three components, which are the micro-environment, market environment, and

macro-environment. Each of these sub-environments consists of variables which can influence an enterprise, its workers and their families.

The micro-environnement (Internal environment)

The micro-environment refers to all the activities that are executed by that enterprise in order to function properly and to attain the profit objectives. These variables are also known as controllable variables where the strength and weaknesses can be discovered. These variables in the micro-environment are Product, price, Promotion, place etc

The Market/ Task Environment The key variables are the stakeholders such as the consumers, competitors, intermediaries, suppliers etc. These variables will influence the enterprise, which makes it imperative for management to analyse the strength and weakness and react to opportunities and threats in the market environment.

The Macro-Environment

The enterprise operates within a wider macro environment, in which variables directly or indirectly influence cannot be controlled. They must be continually evaluated to ensure that potential opportunities or threats are correctly identified. The following six macro-variables in the macro-environment may either individually, or together, affect the enterprise at any time: the technological environment, the economic environment, the social environment, the natural or physical environment, and the institutional/political environment, the international environment. Since it cannot be controlled, management should be alert to changes in the macro-environment.

II. Marketing Strategy

Once the best opportunity to satisfy unfulfilled customer needs is identified, a strategic plan for pursuing the opportunity can be developed. Market research will

provide specific market information that will permit the firm to select the target market segment and optimally position the offering within that segment. The result is a value proposition to the target market.

III. Marketing Mix Decisions

Detailed tactical decisions are made for the controllable parameters of the **marketing mix**. The action items include:

- Product development - specifying, designing, and producing the first units of the product.
- Pricing decisions
- Distribution contracts
- Promotional campaign development

IV. Implementation and Control

At this point in the process, the marketing plan has been developed and the product has been launched. Given that few environments are static; the results of the marketing effort should be monitored closely. As the market changes, the marketing mix can be adjusted to accommodate the changes. Often, small changes in consumer wants can be addressed by changing the advertising message. As the changes become more significant, a product redesign or an entirely new product may be needed. The marketing process does not end with implementation - continual monitoring and adaptation is needed to fulfil customer needs consistently over the long-term

3.3 Annual Marketing Planning

Annual marketing plan is the master blueprint for a year's marketing activity for a ***specified organizational division or major product***. It is usually a written document serving at least three purposes:

(i) It summarizes the marketing strategies and tactics that will be used to achieve specified objectives in the upcoming year. Thus, it serves as a "how-to- do-it" document that guides executives and other employees involved in marketing.

(ii) The plan also points to what needs to be done with respect to the other steps in the management process, such as implementation and evaluation of the marketing programme.

iii) It also outlines who is responsible for which activities, when they are expected to be carried out, and how much time and money can be spent. Very often, the executive responsible for the division or product covered by the plan typically is the task to subordinates.

3.3.1 Contents of an Annual Marketing Plan

The following are the contents of an annual marketing plan:

- (i) Executive Summary and Table of Contents.
- (ii) Current marketing situation.

This section presents relevant background data on sales, costs, profits, the markets, competitors, distribution, and the macro environment. The data are drawn from a product fact book maintained by the product manager.

(iii) Opportunity and issue analysis:

(iv) Objectives: With the summary of the issues given, the product manager must decide on the plan's financial and marketing objectives.

(iv) Marketing strategy:

This outlines the broad marketing strategy or "game plan". The product manager consults with the purchasing and production personnel to confirm that they will supply enough materials and produce enough units to meet the target sales volume levels. In addition, the sales manager should confirm sufficient sales force support and the accountant to obtain sufficient funds for advertising and promotion.

(vi) Action programmes:

The marketing plan must specify the broad marketing programme for achieving the business objectives. Each marketing strategy element must be elaborated to answer such questions as: what will be done? When will it be done? Who will do it? How much will it cost?

(vii) Projected profit-and —loss statement:

Two kinds of financial information are required: On the revenue side, this budget shows forecasted sales volume in units and the average price.

On the expense side, it shows the cost of production, physical distribution, and marketing, broken down into finer categories. The difference between these two sides is the projected profit. With its approval, the budget is the basis for developing plans and schedules for material procurement, production scheduling, employee recruitment, and marketing operations.

(viii) Controls:

The last section of the marketing plan outlines the controls for monitoring the plan. Typically, the goals and budget are spelled out for each month or quarter. The results for each period are reviewed by senior management. Some control sections often include contingency plans, which outline the appropriate steps to be taken by management with respect to specific adverse developments, such as price wars or strikes.

The Production Plan (Operational plan)

An operational or production plan in a business plan is a description of how the work will be done, the flow of work from input to end results, including the machines to be used. It is an analysis of the projected needs for producing or buying the proposed goods and services. The Operating/production section of the business plan into two parts; the development section and the production process section.

The development section

This section describes how the product or service will be made, and the problems that may occur in the production process.

Then show your awareness of your industry's standards and regulations by telling which industry organisations you are already a member of and/or which organisations you plan to join, and telling what steps taken to comply with the laws and regulations that apply to your industry.

- a. Explain who the suppliers are, their prices, terms, and conditions.
- b. Describe alternative arrangements made or will be made if these suppliers let you down.
- c. Explain the quality control measures set up or to establish to ensure production of quality goods and services.

When you are writing this section, start by explaining what you have done—to date for the business to be operational, explanation of what still needs to be done. Follow with a subsection titled —Risks that outlines the potential problems that may interfere with the production process and what to be done to negate these risks. The rest of the development stage part of the operating plan will be divided into subsections that include:

- i. Industry Association Membership:
- ii. Suppliers
- iii. Quality Control.

The Production Process Section

The following details will be included in this part of the production plan:

- i. **General:** Do an outline of your business' day to day operations, such as the hours of operation and the days the business will be open. If the business is seasonal, be sure to say so.
- ii. **The physical plant:** What type of premises are they and what is the size and location? If its applicable, include drawings of the building, copies of lease agreements, and/or recent real estate appraisals. You need to show how much the land or buildings required for your business operations are worth, and tell why they are important to your proposed business.
- iii. **Equipment:** Besides describing the equipment include its worth and, cost, and explain any financing arrangements.

- iv. **Assets:** Make a list of the assets, such as land, buildings, inventory, furniture, equipment and vehicles. Include legal descriptions and the worth of each asset.
- v. **Special requirements:** If your business has any special requirements, such as water or power needs, ventilation and drainage among others, provide the details in your operating plan - as; as what you have done to secure the necessary permissions, such as zoning approvals (allowance by government to use the land for that business).
- vi. **Materials:** State where to get the materials needed for the product or service production and terms negotiated with suppliers.
- vii. **Production:** Explain the length of time to produce a unit, and when to start production. Include factors that may affect the time frame of production and how to deal with potential problems such as rush orders.
- viii. **Inventory control:** Explain how you will keep track of inventory.
- ix. **Feasibility:** Describe any product testing, price testing, or prototype testing that you have done your product or service.
- x. **Cost:** Give details of product cost estimates.

3.4 The Marketing Plan

A marketing plan is a business document written for the purpose of describing the current market position of a business and its marketing strategy to achieve the business marketing objectives for the period covered by the marketing plan. It details the activities to be used to achieve the marketing objectives of the business within a set timeframe.

When writing the marketing plan, the entrepreneur should explain his target market, the product or service he is offering, an analysis of the competition he or she expects to face and the competition strategies he expects to use in the market, his pricing and sales strategies, his promotion and advertising strategies, his

projected sales per week/month or business cycle, his selling and distribution strategies and his projected marketing expenses as based on the collected and analysed market survey data. The Marketing Plan section explains how you are going to get your customers to buy your product and/or services.

Therefore, the easiest way to develop your marketing plan is to work through each of these sections referring to the market research you completed when you were writing the previous sections of the business plan.

- (i) Products and/or Services and your Unique Selling Proposition (intended message for customers).
- (ii) Pricing Strategy
- (iii) Sales/Distribution Plan
- (iv) Advertising and Promotions Plan

However, a marketing plan may be developed as an independent document or as part of a business plan. When you are developing a marketing plan on its own, not as part of a business plan, you will also need to include a Target Market and a Competitive Analysis section. But if you are preparing a marketing plan as part of a business plan, you don't include them since you will have already written them before reaching the marketing plan.

3.4.1 Marketing plan as part of the business plan

The market plan as segment of any business plan can be fully explained under the following categories:

i. Description of Products /Services

This part of the marketing plan focuses on the uniqueness of your product or service, and how the customer will benefit from using the products or services you're offering.

These questions can be used to write a marketing plan:

a. What are the distinctive features of your product or service?

b. How will your product or service benefit the customer? (intangible and tangible).

c. What is it that sets your product or service apart or unique from all the rest? It may be high quality or ease of use. In other words, what is your Unique Selling Proposition

ii. Pricing Strategy

The price charged must be competitive but still allows making a reasonable profit. Keyword here is "reasonable"; there is a limit to how much the consumer is willing to pay. "How do you know what price to charge?" It may be useful to conduct a Break-even Analysis. The pricing strategy you outline in your marketing plan will answer the following questions:

- How does the pricing of your product or service compare to the market price of similar product or services?
- Will your business be more competitive, if you charge more, less, or the same as your competitors ?
- What kind of Return on Investment or net profit are you expecting with this pricing strategy and within what time frame?

(iii) Sales and Distribution Plan

The primary goal of the marketing plan is to get people to buy your products or services. The Sales and Distribution part of the marketing plan details how this is going to happen.

Traditionally there are three parts to the Sales and Distribution section of the marketing plan, although all three parts may not apply to your business.

1. The distribution methods to be used. The following questions will be examined;

- What distribution channel is going to be used? Outline all the different companies, people and/or technologies that will be involved in the process of getting your product or service to your customer.
- What are the costs associated with distribution channel?

- What are the delivery terms?
- How long will it take to get your product or service to your customer?
- If your business involves selling a product, you should also include information about inventory levels and packaging in this part of your marketing plan. For instance:
 - How are your products to be packaged for shipping and for display?
 - Does the packaging meet all regulatory requirements (such as labelling)?
 - Is the packaging appropriately priced, -and complementary to the product?
 - What minimum inventory levels must be maintained to ensure that there is no loss of sales due to problems such as late shipments and back orders?

2. The transaction process between your business and your customers.

‘What system will be used for processing orders, shipping, and billing?

- What methods. of payment will customers be able to use? Is
- What credit terms will be offered to customers? What is your return policy? Do you accept goods returned by customers or not? What warranties or guarantees will be offered to the customers? A warranty is a promise to replace or repair an item if the item does not satisfy the terms of the warranty in the period granted while a guarantee is a promise to return the money paid to purchase an item if the item does not satisfy the terms of the guarantee in the period granted.

What after-sale support or services will you offer customers and what will you charge (if anything) for this support? Some products need installation like DSTV equipment and solar panels.

Is there a system for customer feedback in order to get comments on customer satisfaction?

3. Your sales strategy: Outline it if it is applicable to your business

- What types of salespeople will be involved?

- Describe your expectations of these salespeople and how sales effectiveness will be measured. Will a sales training program be offered? If so, describe it in this section of the marketing plan.
- Describe the incentives salespeople will be offered to encourage their achievements.

4. Advertising and Promotion Plan

What distinguishes a successful Advertising and Promotion plan from an unsuccessful one is focus - and that's what your Unique Selling Proposition provides.

5. Advertising

Which media will be the most effective in reaching your annual advertising budget you are going to spend on each medium. What percentage of your annual advertising budget will be spent on each type, about how much business the advertising will bring in. The inclusion of sales promotion activities into your advertising and promotion plan.

Marketing Materials - The common marketing materials globally in some countries include business card, brochures, credit card, fliers, pamphlets etc.

Publicity: Publicity is all about making people or the media spread the word usually free about your business. Eg. Press releases, that is, written, audio taped, or videotaped news sent out or released by the business to the public about its products and activities, Product launches etc.

Tradeshows - Tradeshows can be incredibly effective promotion and sales opportunities where you reach a wide section of customers if you go the right trade shows.

Other Promotion Activities: These may include conducting an E-mail or even a text message campaign and teaching a course about the product to a specific target group among others.

5. Projected marketing expenses

The final section of the marketing plan should include a projected marketing expenses section gives a brief breakdown of the costs associated with your marketing strategy. So if you plan to exhibit at three trade shows per year, for example, you will include the costs to participate in the shows. If you plan to use radio and television adverts and marketing materials like fliers, business cards and brochures, then include their cost. If you find the promotional methods you selected are too costly, you can go back and make revisions before you arrive at a final budget.

3.4.2 Benefits of a Marketing Plan

- 1. A (guide to the team):** The marketing plans gives your team something to rally behind and can help your team unite for a common cause and make your employees committed to the company especially when developed and shared with them. It is more likely to convince investors that a company needs additional funding and support. It also enhances relationships with bankers.
- 2. Guide to success:** A marketing plan outlines the marketing tactics you will use and a time line for when you will use them to achieve the set goals and objectives and therefore ensure business success.
- 3. Company operational instruction:** It gives operational instructions to be followed by the marketing department while working towards achieving the marketing department goals of the business.
- 4. Acts as a reference point (captured thinking):** Well written documents can be used to guide new employees in the marketing department or a reminder on what had been agreed on .
- 5. Top level reflection (Helps in performance measurement):** Marketing plan includes' a measurement strategy, which allows you to track your

performance and see exactly which of your marketing tactics worked and which ones did not do so well.

5.0 Conclusion

A company that wants to compete successfully in the marketplace must show sufficient commitment to creating and retaining satisfied customers. The company must also know how to adapt to a continually changing marketplace.

6.0 Summary

Market—oriented strategic planning is the managerial process of developing and maintaining a viable fit between the organisation's objectives, skills and resources, and its changing market opportunities. The main goal of strategic planning is to help a company select and organize its businesses in a way that will keep the company healthy even when unexpected events adversely affect any of its specific businesses or product lines.

6.0 TUTOR - MARKED ASSIGNMENT Question:

- a. What are the purposes of an annual marketing plan?
- b. List the contents of an annual marketing plan.

7.0 FURTHER READING

Adeyeye, M. M. (2018) *A Fundamental Approach to Entrepreneurship, Small and Medium Scale Enterprises Second Edition*. Ibadan: Evi-Coleman and Co. Publishing House.

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UNIT 9: MARKETING MIX: PRICING POLICIES AND STRATEGIES

CONTENTS

- 1.0 Introduction
- 2.0 Objectives
 - 3.0 Main Content
 - 3.1 What is Price?
 - 3.2 Strategic Pricing Policies Decisions
 - 3.3 Alternative Pricing Methods
 - 3.4 Risk taking in Business
- 4.0 Conclusion
- 5.0 Summary
- 6.0 Tutor-Marked Assignment
- 7.0 References/Further Reading

1.0 INTRODUCTION

Price is an important element of the marketing mix. It can be used as a strategic marketing variable to meet competition. It is also a direct source of revenue for the firm. It must not only cover the costs but leave some margin to generate profit for the firm. However, price should not be so high as to frighten the customers. This unit examines pricing policies and some strategies adopted by company executives.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- Define price

- State the Strategic pricing decision
- Explain Alternative price methods
- Expatiate on product positioning and price
- Understand risk taking in business.

3.0 MAIN CONTENT

3.1 What is price?

Price refers to the monetary value of a good or service. The price of a firm may change for its output depending on many factors which include the following: -

1. Consumer's perception of the attributes and quality of the product.
2. Total demand for the good which depends on consumer's income, size of the market seasonal and demographic factors.
3. The degree of competition in the market.
4. Price elasticity of demand for the product. E.g. the extent to which a price change leads to an alternative demand.
5. Competitors likely reaction to a price cut.
6. Consumer's knowledge of the availability of substitute products.
7. The products brand image and the degree of consumer loyalty.
8. Cost of production.

Price is just one element of the marketing mix and it must reflect the product's position in the market. A toilet soap meant to be a novelty to attract the elite must be sold at a higher price. This is the basic idea behind product differentiation, i.e. to avoid a situation where the product has to compete only on the basis of price.

Pricing is affected not only by the cost of manufacturing the product, but also by:

- (i) the company's objectives in relation to market share and sales
- (ii) the nature and intensity of competition
- (iii) stage of the product life cycle at which the product is currently positioned

(iv) nature of product whether as consumer or industrial product, and if the former, whether it is a luxury or necessity. Before making any pricing decision it is important to understand all these factors.

Pricing Right

Pricing right is the fastest and most effective way for enterprises profitability. The organization must determine on what fair price to place on its product. Price is the exchange value, according to Adeyeye (2018), for the goods and services supplied or to be supplied. Price is very important in marketing as a factor that can establish the venture or push it out of the system. There are four significant period of price decision-making in an establishment.

- When a product is newly introduced.
- Need for price alteration due to economic or other conditions.
- Competition imposed change.
- Engagement in a multiple brand strategy e.g. a soap production firm marketing three or four brand names at different prices.

3.2 Strategic Pricing

Strategic pricing decisions are usually determined by cost, demand and competition that could position the product in the market arena. We shall discuss each of these factors separately.

1. Penetrative pricing. This is whereby a low price is combined with aggressive advertising aimed at capturing a large percentage of the market. The firm hopes that unit production costs would fall as output is expanded. The strategy will fail, however, if competitors simultaneously reduce their prices.

2. Target pricing. This is where the firm predetermines a target level of profits, estimates its potential sales at targeting prices and then charges a price to generate target profits.

- 3. Skimming.** This is where a high price policy suitable for top quality versions of established products is set. The firm must convince high income consumers that the expensive model offers distinct improvements over the standard version.
- 4. Product life cycle pricing.** Here, the price is varied according to the products stage in its life cycle. Initially, a high price may be set to cover development and advertising costs. The price might then be systematically lowered to broaden the products appeal.
- 5. Pricing with the market:** The new company has no option but to follow the price level set by the established companies. It then charges price according to what exists in the industry.
- 6. Price above the market:** This is common with the specialty goods for the high classes. The pricing is the fixture of price higher than the market price.
- 7. Product line promotion:** Bring down the price of a product as a loss leader in order to attract a large number of buyers who are expected to buy other less popular products of the firm. The price of one is used as a bait to attract them to the other.
- 8. Target rate of return on investment:** Setting a level of profit that would result from the price level given for the product.
- 9. Price discrimination.** This involves charging different prices in different markets for the same good. It can only work if there exist barriers e.g. consumers ignorance or high transport costs that prevent intermediaries buying from low price markets and re-selling elsewhere.
- 10. Limit pricing.** Mere existing firms in an industry collectively choose to charge lower prices than the market would bear, to discourage the entry of new firms to the industry.
- 11. Demand oriented pricing.** This refers to pricing based primarily on the intensity of demand. A higher price is charged when or where the demand is strong and low price is set where the demand is weak. This is regardless of the product cost in both cases i.e. even if the product cost is the same in both cases.

12.Competition oriented pricing. This is pricing that is determined mainly by the prices of the competitors for the same products. The entrepreneur may keep his prices higher or lower than those of his competitors in view of certain considerations. Price changes however mainly | depend on the competitors.

13.Auctioning. The highest bidder takes the product. Prices are determined depending on who offers the highest price.

14.Haggling or bargaining. Price is determined by the discussion of prices and other conditions with the aim of reaching an agreement on the prices of the product.

15.Government pricing policy. The government dictates on some prices of more especially the essential products and services like sugar, petrol, etc.

16.Fashion oriented pricing. Prices will be determined based on different fashions or models. For example, some people prefer clothes designed by Marks and Spencer to those made locally.

17.In pure competition, all that the individual seller can do is to accept the price prevailing in the market i.e. he is in the position of a price taker. If he wants to charge a higher price, buyers will purchase from other sellers. He needs not charge less since he can sell his small supply at the going market price.

18.Under a monopoly, a single producer has complete control of the entire supply of a certain product. The main features of a monopoly are (i) there is only one seller of a particular good or service and (ii) rivalry from the producers of substitutes is so remote that it is almost insignificant. Thus, he is in the position of a price setter.

However, even in the case of a monopolist, there are limits to the extent to which he can increase his prices. Much depends on the elasticity of demand for the product. This, in turn, depends on the extent of availability of substitutes for the products. And in most cases, there is rather an infinite series of closely competing substitutes. The closer the substitute and greater the elasticity of the demand for

a monopolist's product, the less he can raise his price without frightening away his customers. The high price of oil has led to the development of alternative sources of energy, such as solar energy. Monopolies are constantly reducing due to the following reasons:

- 1) shifts in consumer demand
- 2) continuous process of innovation and technological developments leading to development of substitutes
- 3) lack of stimulus to efficiency provided by competition
- 4) entry of new competitors' intervention by governments.

19.Oligopoly is a market situation characterized by a few sellers, each having an appreciable share in the total output of the commodity. The automobile, cement, tyre, tractor, aluminium and razor blade industries provide examples of oligopolies. In each of these industries, each seller knows his competitors individually in each market. Each oligopolistic realizes that any change in his price and advertising policy may lead rivals to change their policies. Hence, an individual firm must consider the possible reactions of the other firms to its own policies. Thus, oligopolists follow the philosophy of **“live and let live”**. Oligopolistic industries are usually characterized by what is known as price leadership – a situation where firms fix their price in a manner dependent upon the price charged by one of the firms in the industry, called the price leader. The price leader has lower costs and adequate financial resources, a substantial share of the market and a reputation for sound pricing decisions. Price leaders with the strongest position in the market may often increase their prices with the hope that competitors will follow suit. Price followers may delay raising their prices in the hope of snatching a part of the market share away from the leader.

20.Monopolistic competition is a market situation, in which there are many sellers of a particular product, but the product of each seller is in some way differentiated in the minds of consumers from the product of every other seller. None of the sellers is in a position to control a major part of the total supply of the commodity, but every seller so differentiates his/her portion of the supply from the portions sold by others, that buyers hesitate to shift their purchases from his/her product to that of another in response to price differences. At times, one manufacturer may differentiate his/her own products. For example, a blade manufacturer may manufacture more than 25 **brands** of blades. This differentiation of products by each manufacturer by giving it a brand name gives him some amount of monopoly if he is able to create goodwill for his products and he may therefore be able to charge higher prices to some extent. As long as a consumer has an impression that a particular product brand is different and superior to others, he/she will be willing to pay more for that brand than for any other brand of the same commodity. The differences, real or illusory, may be built up in his or her mind by;

Recommendations by friends, Advertising, personal experience and observation.

Whilst the producer gains and retains his customers by;

Competitive advertising and sales promotion, use of brand names, quite as much as by Price competition.

Product differentiation is more typical of the present day economic system, than either pure competition or monopoly. And, in most cases, an individual firm has to face monopolistic competition. It tries to maintain its position and promote its sales by either;

- a) changing its price and indulging in price competition, or
- b) intensifying the differentiation of its product, and /or
- c) increasing its advertisement and sales promotion efforts.

There is a popular belief that costs determine price. It is because the cost data constitute the fundamental element in the price setting process. However, their

relevance to the pricing decision must neither be underestimated nor exaggerated. For setting prices, apart from costs, a number of other factors have to be taken into consideration.

If costs were to determine prices, why do so many companies report losses?

Price decisions cannot be based merely on cost because it is very difficult to measure costs accurately. Costs are affected by volume, and volume affected by price. The management must assume some desired price and volume relationship for determining costs. It is not possible to determine costs without having an idea of what volumes or numbers can be sold. Since there is no experience of volumes, costs and prices, one starts with the going market price for similar products. Costs must be taken into consideration while setting prices. In fact, in the long run, if costs are not covered, manufacturers will withdraw from the market and supply will be reduced which, in turn, may lead to higher prices. The point that needs emphasis is that cost is not the only factors in setting prices. Cost must be regarded only as an indicator of the price, which ought to be set after taking into consideration the demand, the competitive situation, and other factors.

3.3 Alternative Pricing Methods

After discussing the various strategic pricing decisions, it would be useful to discuss the alternative pricing methods most used. They are:

- 1) Cost-plus or Full-cost pricing
- 2) Pricing for a rate of return, also called target pricing
- 3) Marginal cost pricing
- 4) Going rate pricing, and
- 5) Customary prices.

The first three methods are cost-oriented, as the prices are determined based on costs. The last two methods are competition-oriented, as the prices are set based on what competitors are charging. While from the company's point of view, price

represents a kind of maximum‘ that it can charge given its own costs and nature of competition, from the costumer’s viewpoint it is a representation of quality of the product

Cost–Plus or Full–Cost Pricing

This is the most common method used in pricing. Under this method, the price is set to cover costs (materials, labour and overheads) and a predetermined percentage for profit. The percentage differs strikingly among industries, among member–firms and even among products of the same firm. This may reflect differences in competitive intensity, differences in cost base and differences in the rate of turnover and risk.

In fact, it denotes some vague notion of just profit. What determines the normal profit? Ordinarily margins charged are highly sensitive to the market situation.

They may, however, tend to be inflexible in the following cases:

- 1) They may become merely a matter of common practice.
- 2) Mark–ups may be determined by trade associations either by means of advisory price lists or by actual lists of mark–ups distributed to members.
- 3) Profits sanctioned under price control as the maximum profit margins remain the same even after the price control is discontinued. These margins are considered ethical as well as reasonable. Their inadequacies are:
 - a) It ignores demand – there is no necessary relationship between cost and what people will pay for a product.
 - b) It fails to reflect the forces of competition adequately. Regardless of the margin of profit added, no profit is made unless what is produced is actually sold.
 - c) Any method of allocating overheads is arbitrary and may be unrealistic. In so far as different prices would give rise to different sales volumes, unit costs are a

function of price, and therefore, cannot provide a suitable basis for fixing prices. The situation becomes more difficult in multi-product firms.

d) It may be based on a concept of cost which may not be relevant for the pricing decision.

Explanation for the widespread use of Full-cost Pricing

A clear explanation cannot be given for the widespread use of full-cost pricing, as firms vary greatly in size, product characteristics and product range, and face varying degrees of competition in markets for their products. However, the following points may explain its popularity:

1. Price based on full cost looks factual and precise and may be more defensible on moral grounds than prices established by other means.
2. Firms preferring stability, use full-cost as a guide to pricing in an uncertain market where knowledge is incomplete.
3. In practice, firms are uncertain about the shape of their demand curve and about the probable response to any price change. This makes it too risky to move away from full-cost pricing.
4. Fixed costs must be covered in the long run and firms feel insecure if they are not covered in the long run either.
5. A major uncertainty in setting a price is the unknown reaction of rivals to that price. When products and production processes are similar, cost-plus pricing may offer a source of competitive stability by setting a price that is more likely to yield acceptable profit to most other members of the industry also.
6. Management tends to know more about product costs than factors which are relevant to pricing.
7. Cost-plus pricing is especially useful in the following cases:
 - a) Public utilities such as electricity supply, and transport, where the objective is to provide basic amenities to society at a price which even the poorest can afford.

- b) Product tailoring, i.e. determining the product design when the selling price is pre- determined. The selling price may be determined by government, as in the case of certain drugs, cement, and fertilizers. By working back from this price, the design and the permissible cost is decided upon. This approach is from the viewpoint of the buyer in terms of what he wants and what he will pay.
- c) Pricing products that are designed to the specification of a single buyer as applicable in case of a turnkey project. The basis of pricing is estimated cost plus gross margin that the firm could have got by using facilities otherwise.
- d) Monophony buying – where the buyers know a great deal about suppliers' costs as in the case of an automobile maker buying components from its ancillary units. They may make the products themselves if they do not like the price. The more relevant cost is the cost that the buying company, say the automobile manufacturer, would incur if it made the product itself.

General counsel on full cost pricing:

- * Set your prices so as to make a reasonable profit.
- * Reduce items that are most costly in the running of your business.
- * Watch how the costs might be affected by any changes to introduce.
- * Find out the direct costs which are a component of direct materials, direct labour and direct expenses. These costs are traceable to the particular unit of goods being made e.g. raw materials, spare parts, foreman, carriage inwards (mail-barrow) etc.
- * Add to indirect expenses often referred to as overhead expense e.g. rents, electricity, salaries, depreciation of fixed assets, telephone, advertisement, etc.
- * Direct cost and indirect cost = Total Cost Price
- * Consider the mark-up which is profit expressed as a fraction or percentage of cost price. Mark-up = $\frac{\text{Profit}}{\text{Cost Price}}$ as a fraction or multiply by 100 for percentage.

* Consider the margin which is profit expressed as a fraction or multiply by 100 as percentage of selling price. $\text{Margin} = \frac{\text{Profit}}{\text{Selling Price}}$ as a fraction or multiply by 100 for percentage.

* $\text{Cost Price} + \text{Profit} = \text{Selling Price}$.

To be on the safe side, add 50% to 80% Mark- up to your unit price except where you enjoy the economy of scale. e.g

A travelling bag cost	500
A 50% mark-up being	250
Selling Price	<u>750</u>

The Margin Percentage is $\frac{250}{750} = \frac{1}{3} = 33\%$

All the products may not sell at that price. The competitors' prices are important too. If a similar product is N600 in the market, then there is need to cut down your price.

Establishing Relationship between Mark-up and Margin.

This is a simple way of expressing your profit. Take the same denominator and add or minus it from the numerator.

$$\begin{array}{r} \text{Mark-up} \text{-----} \rightarrow \\ \frac{1}{4+1} = \frac{1}{5} \\ \frac{2}{11+2} = \frac{2}{13} \end{array}$$

$$\begin{array}{r} \text{Margin} \\ \frac{1}{4+1} = \frac{1}{5} \\ \frac{2}{11+2} = \frac{2}{13} \end{array}$$

$$\begin{array}{r} \text{Margin} \text{-----} \rightarrow \\ \frac{1}{6-1} = \frac{1}{5} \\ \frac{3}{13-3} = \frac{3}{10} \end{array}$$

$$\begin{array}{r} \text{Mark-up} \\ \frac{1}{6-1} = \frac{1}{5} \\ \frac{3}{13-3} = \frac{3}{10} \end{array}$$

The right price will boost profit faster than increase in sales volumes, whereas, the wrong price can shrink profits just quickly. It has been proved by research that 1% improvement in price will lift operating profits by 11% and a 1% reduction in average pricing brings operating profits down by just as much. This is called the “pricing lever double-edged sword”. Conclusively, prices should be assigned to each and every customer transaction depending on the volume of sales, payment plans and the demand in the market at the time of transaction.

Pricing for a Rate of Return

An important problem that a firm might have to face is one of adjusting the prices to changes in costs. For this, popular policies that are often followed are as:

1. Revise prices to maintain a constant percentage mark-up over costs.
2. Revise prices to maintain profits as a constant percentage of total sales.

3. Revise prices to maintain a constant return on invested capital The use of the above policies is illustrated below:

ILLUSTRATION

A firm sells 100,000 units per year at a factory price of N12 per unit.

The various costs are given below:

Variable	Costs Materials	N360,000
	Labour	N420,000
Fixed	Costs Overhead	N120,000
	Selling & Administrative charges	N180,000
Total investment in cash, inventory and equipment		N800,000

Suppose the labour and materials cost increases by 10 per cent. The question is how to revise price according to the three policies discussed above.

The above data reveal that costs are N1,080,000. The profits as percentage of costs, sales and capital employed (according to the three policies are):

1 Percentage over Costs	$\frac{120,000}{1,080,000} = 11.1$
2 Percentage of Sales	$\frac{120,000}{1,200,000} = 10$
3 Percentage on Capital employed	$\frac{120,000}{800,000} = 15$

The revised costs are N1,158,000 (N1,080, 000 + 36,000 + 42,000)

According to the first formula, we have to earn a profit of 11.1 per cent on costs. Our revised profits should be #128,667 and sales volume on this basis would be N1,286,667. The selling price would, therefore be N 12.87 per unit.

Under the second formula, the profit should be 10 per cent on sales. If sales are (S), the profit would be $S/10$ and cost would be $9S/10$. The cost known to us and we have to find out the sales.

If $9S/10 = \text{N}1,158,000$ then $S = \text{N}1,286,667$.

Therefore, the price per unit is N12.87.

Under the third formula, we assume that the capital investment is the same. Therefore, the required profit is N120, 000 (15 per cent on N800,000). The sales value would then be N1,278, 000 and the selling price per unit would be N12.78. Rate of return pricing is a refined variant of full-cost pricing. Naturally, it has the same inadequacies, viz. it tends to ignore demand and fails to reflect competition adequately. It is based upon a concept of cost, which may not be relevant to the pricing decision in hand and overplays the precision of allocated fixed costs and capital employed.

Marginal Cost Pricing

Under full-cost and rate-of -return pricing, prices are based on total costs comprising fixed and variable costs. Under marginal cost pricing, fixed costs are ignored and prices are determined on the basis of marginal cost. The firm uses only those costs that are directly attributable to the output of a specific product. With marginal cost pricing, the firm seeks to fix its prices so as to maximize its total contribution to fixed costs and profit. Unless the manufacturer's products are in direct competition with each other, this objective is achieved by considering each product in isolation and fixing its price at a level, which is calculated to maximise its total contribution.

Advantages

1. With marginal cost pricing, prices are never rendered uncompetitive merely because of a higher fixed overhead structure. The firm's price will be

rendered uncompetitive by higher variable costs, and these are controllable in the short run while certain fixed costs are not.

2. Marginal cost pricing permits a manufacturer to develop a far more aggressive pricing policy than does full-cost pricing. An aggressive pricing policy should lead to higher sales and possibly reduced marginal costs through increased marginal physical productivity and lower input factor prices.
3. Marginal cost pricing is more useful over the life-cycle of a product, which requires short-run marginal cost and separable fixed data relevant to each particular state of the cycle, not long run full-cost data. Marginal cost pricing is more effective than full-cost pricing because of two characteristics of modern business:
 - a. The prevalence of multi-product, multi-process and market concerns makes the absorption of fixed costs into product costs absurd. The total costs of separate products can never be estimated satisfactorily, and the optimal relationships between costs and prices will vary substantially both among different products and between markets.
 - b. In many businesses, the dominant force is innovation combined with constant scientific and technological development, and the long-run situation is often highly unpredictable. There is a series of short runs. When rapid developments are taking place, fixed costs and demand conditions may change from one short run to another, and only by maximising contribution in each short run will profit be maximized in the long-range.

Limitations

1. The encouragement to take on business, which makes only a small contribution to the business arises. Such business may have to be foregone

because of inadequate free capacity, unless there is an expansion in organisation and facilities, with the attendant increase in fixed costs.

2. In a period of business recession, firms using marginal cost pricing may lower prices in order to maintain business and this may lead other firms to reduce their prices, leading to cut-throat competition. With the existence of idle capacity and the pressure of fixed costs, firms may successively cut down prices to a point at which no one is earning sufficient total contribution to cover its fixed costs and earn a fair return on capital employed.

In spite of its advantage, due to its inherent weakness of not ensuring the coverage of fixed costs, marginal cost pricing has usually been confined to pricing decision relating to special orders.

Going-Rate Pricing

The firm adjusts its own price policy to the general pricing structure in the industry. Where costs are particularly difficult to measure, this may seem to be the logical first step in a rational pricing policy. Many cases of this type are situations of pricing leadership. Where price leadership is well established, charging according to what competitors are charging may be the only safe policy. It must be noted that going-rate pricing' is not quite the same as accepting a price impersonally set by a near perfect market. Rather it would seem that the firm has some power to set its own price and could be a price maker if it chooses to face all the consequences. It prefers, however, to take the safe course and conform to the price of others.

Customary Pricing

Prices of certain goods become more or less fixed, not by deliberate action on the seller's part, but as a result of their having prevailed for a considerable period of time. With such goods, changes in costs are usually reflected in changes in quality or quantity. Costs change significantly only when the customary prices of these goods are changed. Customary prices may be maintained even when products are

changed. For example, the new model of an electric fan may be priced at the same level as the discontinued model. This is usually so even in the face of lower costs. A lower price may cause an adverse reaction on the competitors leading to a price war so also on the consumers who may think that the quality of the new model is inferior. Perhaps, going with the prices as long as possible is a factor in the pricing of many products. Another possible way out, especially when an upward move is sought is to test the new prices in a limited market to determine the consumer reaction.

3.3.1 Objectives of Pricing Policy

Before a marketer fixes a price, he should keep in mind certain basic considerations. The pricing policy he adopts is closely related to this other policies, like production programme, advertising policy, and selling methods. For example, it may be necessary to reduce the price to offset the probable loss of sales from a lower advertising budget or to enable fuller utilisation of plant capacity more quickly. Aggressive sales campaign may be necessary to meet the advent of a new competitor. Your price should not be so high that it attracts others to compete with you. A low price may result in such a high volume of sales and low unit costs that profits are maximised even at low prices. If a marketing manager is to make effective pricing decisions, he should be clear about the firm's long-term marketing objectives for the entire range of products and services. If the firm is interested in increased market share, it would have to resort to penetration pricing. If it is interested in short-term profitability, it may have a higher price even at the expense of sales volume and market share. The following table gives a summary of some marketing objectives and their pricing implications:

Some Marketing Objectives & their Pricing Implications

Marketing Area	Marketing Objectives	Pricing Implications
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Product	Improve Quality Acceptance	Higher cost = Price increase or lower profit.
Advertising and Promotion	Stronger Support	Increased Advertising and Publicity budget = Price increase or lower profit
Distribution	Additional Selling Points	Possibly higher Distribution costs (margin increase)
Consumers/Users	General Acceptance	Increase Advertising and Publicity effort.

Source: J.J. Ward (Editor), (1985). *The Export Marketing Management*. Geneva:

International Trade Centre.

3.3.2 Consumer Psychology and Pricing

Sensitivity to price change will vary from consumer to consumer. In a particular situation, the behaviour of one individual may not be the same as that of the other. Some important characteristics of the consumer as revealed by research and experience are detailed below:

1. From the point of view of the consumer, prices are quantitative and precise whereas product quality, product image, customer service, promotion and similar factors are qualitative. It is easier to speculate about what consumers would do if prices rose by 5 per cent than if the quality improved by 5 per cent.
2. Price constitutes a barrier to demand when it is too low just as when it is too high. Above a particular price, the article is regarded as too expensive and, below another price, as constituting a risk of not giving adequate value. If the price is too low, consumers will tend to think that a product is of inferior quality.
3. Price inevitably enters the consumer's assessment of quality. There are two reasons for this:
 - (a) It needs expert knowledge and appropriate equipment to test the quality or durability of some particular products (to say nothing of the time and cost involved in carrying out a proper test).

(b) Customers tend to look upon price itself as a reasonably reliable indicator of quality. What is costly is thought to be of high quality. A higher price is ordinarily taken to be a symbol of extra quality, or extra value of extra prestige.

It is very difficult to convince people that something cheap is of good quality and that something expensive is of poor quality. It may be easier to prove that an expensive product is of superior quality than to prove that a cheap product is of good quality. This is especially true of durable consumer goods which are very often differentiated, at least psychologically, through branding, packaging and advertising. In such cases, the sale of certain goods could be stimulated more effectively through higher rather than lower prices for two reasons:

- (i) The higher price increases the appeal of the goods.
- (ii) The higher price creates confidence in the customer that he/she is getting good quality.
- (iii) To conclude, in many cases, price is used by the prospective customer as a clue for sizing up the quality of the product. This price quality association is well established.
- (iv) With an improvement in incomes, the average consumer becomes quality conscious. An improvement may, therefore, lead to an increase in demand. If this is so, a time may come when a rise in prices results in an increase in demand. This extreme situation may arise if price in increasingly affluent societies comes to serve merely as an indicator of quality.
- (v) Consumers may be persuaded to pay more for heavily advertised goods. A firm's size, its financial success, and even its age are often perceived by consumers as measures of quality. Well known firms very often assert that by virtue of their reputation they are able to charge 5 to 10 per cent higher than other firms but definitely not much more.

(vi) In a comprehensive survey of consumer consciousness, it was revealed that the basic postulate of the demand theory, i.e., the consumer has an appropriate knowledge of market prices, was not fundamentally wrong.

An experimental study in Nigeria showed that more than 50 per cent of the respondents revised their ratings of ready-made shirts after knowing their prices, indicating thereby that price information does have a significant effect on quality perception.

In fact, higher prices that increase consumer readiness to buy may sound uneconomic, but may not be unrealistic. The price-quality concept has equal relevance to new product pricing. The lesson from this discussion is that the producer has considerable flexibility in pricing his products, provided he can create a psychological image of quality.

3.3.3 Nature and Use of Price Discounts

There are two popular types of discounts:

1. Quantity Discounts: Quantity discounts are price reductions related to the quantities purchased. It only appears on invoice not in any account. Quantity discounts may be related to the size of the order being measured in terms of physical units of a commodity. This is practicable where the commodities are homogeneous or identical in nature, or where they may be measured in terms of truck-loads. quantity discounts are based upon the money value of the quantity ordered. Money becomes a common denominator of value.

One important objective of quantity discounts is to reduce the number of small orders and thereby avoid the high cost of servicing them. Quantity discounts can facilitate economic size order in three ways:

- a. A given set of customers is encouraged to buy the same quantity but in larger lots.

- b. The customers may be induced to give the seller a larger share of their total requirements by giving preference over competitors.
- c. Small size purchasers may be discouraged, and larger size customers may be attracted.

2. Cash Discounts: Cash discounts are price reductions based on promptness of payment. In practice, the term cash discounts may vary widely. Cash discount is a convenient device to identify and overcome bad credit risks. In certain trades where credit risk is high, cash discounts would be high. If a buyer decides to purchase goods on credit, this reflects his weak bargaining position, and he must pay a higher price by foregoing the cash discount. By prompt collections, manufacturers reduce their working capital requirements and thus save their interest costs. However, allowing discounts may involve paying 36.5 per cent in order to save 18 per cent. On the basis of 2 per cent off if paid in 10 days, full involve price in 30 days, the seller's cost comes to 36.5 per cent (for getting the money 20 days before he has to lose 2 per cent which amounts to 36.5 per cent per year). He could get accommodation from any bank at about 18 per cent.

3.4 RISK TAKING IN BUSINESS

Meaning

Life in its entirety is a risk. No matter the dynamism of a business environment, risk-taking is part of business and an entrepreneur is distinguished by the calculated risk taking. Decision must be made without complete information and contingencies of life. In real world situation, enterprises generally and investment projects are exposed to different degrees of risk. Risks exist because of the inability to make perfect forecast in decision making. A risk is a situation where one is required to make a choice between different alternatives which may result into differing rewards for success or penalties for failure. A risk situation occurs

when a choice is required between two or more alternatives whose potential outcomes are not known and must be subjectively evaluated. A risk situation involves potential loss and potential success. The greater the possible loss or gain the greater the risk involved. Risk is the condition under which individuals can define a problem, specify the probability of certain events, identify solutions and state the probability of each solution leading to the desired result (Hellrigel et al. 2003). Risk can also be seen as the chance of loss or injury usually associated with life business or trips. Risk is not the same as uncertainty.

Risk taking is entrepreneurial. Low risk situations are very conservative and not entrepreneurial while high risk situation is gambling and can be very costly in case of failure. A wise entrepreneur will tow the middle-of-the-line risk situation, calculate and take challenging risks situation. Risk takers make decisions and balance potential success against potential loss. Choosing a risky alternative depends on:

- i. how attractive the alternative is.
- ii. the extent to which the risk taker is prepared to accept the potential loss
- iii. the relative probabilities of success and failure
- iv. the degree to which one's own efforts increase the likelihood of success and decrease the likelihood of failure.

3.4.1Types of Business Risks

The different types of risks are classified based on levels, low, moderate and high. Low level are minimal risks that do not yield a lot of benefits and tend to discourage from investing resources into new ventures due to fear of loss. Moderate risks can be forecasted, calculated and managed in case it happens, it does not affect the business. High risks have a high chance of occurrence or happening with little or no control over them but tend to fetch higher profits in case they succeed. Horton (2015) asserted that business risk comes in variety of tangible and intangible forms in a business cycle. Risk situation involves potential

loss or failure on potential gain or success. A risk situation entails two types of costs-(1) cost of potential loss that turns actual loss and (2) cost of reducing or eliminating the risk and potential loss.

Perez (2014) identified eight major risks situation: First, **Credit Risk** which includes credit default risks that from debtors' inability to pay his debt for more than 3months upward; **Concentration risk** is the risk associated with the whole industry or any single name concentration that can threaten the core of the organisation; and **Country risk** is associated with the country's macroeconomic performance and political stability e.g. Foreign currency payments (transfer/conversion risk). Second, **Market Risk** also referred to as systematic risk, that affects the overall performance of the market. Most used are equity risk, interest rates, terrorist attack, natural disaster, currency, commodity, basis etc. Thirdly, **Operational Risk** are risk resulting from failed internal processes such as inadequacies of people in processing of transactions, breakdowns in controls, human errors, failures and deficiencies in systems. Others are **liquidity risk; business risk; reputational risk; while systemic risk and moral hazard** are unrelated to routine operations.

All the risk can categorized into two generically: Speculative risk and pure risk. Speculative risk is where there is a probability of loss or gain. Example is stock exchange market, shares and stock. This could be minimized by combination of high risk or high return shares with low risk or low returns shares. Pure risks are circumstances where losses and injuries occur from certain eventualities like fire, burglary, motor or industrial accident, natural disasters (famine, flood) etc.

3.4.2 Risk Assessment

This involves determining the potential success (will arise out of the risk not happening) or potential loss (arising out of the risk happening), Risks can be assessed based on the following factors:

- a. Viability of the idea: Whether the chosen business idea would be profitably done in the area, given the available resources, skilled staff, etc.
- b. Availability of the market: Whether the people in the area in need, willing and able to buy the products of the business.,
- c. Experience and abilities: Whether the person involved in promoting; and managing the business, possesses the required knowledge and experience.
- d. Pricing policies and strategies: Whether the proposed price at which the goods will be sold will be competitive in the prevailing competition in the market.
- e. Establishing whether the business will generate enough cash inflows to cater for the planned cash outflows and if not, to determine whether the business will be in position to look for other sources to bridge the gap.
- f. Flexibility of the business: Whether the chosen business can be easily changed without having any disastrous effects on the resources invested.
- g. Honesty and reliability: Finding out if the people whom the business is dealing with are honest and reliable e.g suppliers, workers, customers etc.

3.4.3 Procedures for Analysing a Risk Situation

Although risk taking is a behavioural trait, calculated risk-taking is a skill that can be improved. The following are the suggested procedures for analysing a risk situation.

- i. **Assess the risk:** Is there a potential loss involved in choosing one particular alternative? for example *you* may need to increase production to meet increased demand, your choices are to
 - stay with the current level of demand
 - purchase or lease more equipment to meet the demand
 - subcontract production to smaller contractors
 - hire a new employee

For the case of financially strong businesses, if demand is certain to grow in the foreseeable future, there is little risk involved in deciding on any of the alternatives, although the first alternative would cause the opportunity growth to be Ignored. However, continued demand may not be assured, for instance a product or service may become obsolete due to competitive innovations, there is clearly a risk involved in deciding whether to expand production, however, there are clearly different degrees of risk and corresponding degrees of potential success for the different alternatives.

- ii. **Determine goals and objectives:** This involves considering the company's policies and procedures. A company objective might be to achieve slow growth, steady growth, no growth in other product areas. If the risk involved is consistent with the company's objectives, then the decision making process continues and then assessment of the alternatives is undertaken.
- iii. **Clarify the alternatives;** Since some degree of risk taking is consistent with the company's objectives, one needs to survey the various alternatives which should be specified in sufficient detail so that the costs involved can be assessed objectively. Though most costs will be financial, others will include personal, physical and social when appropriate, e.g excessive personal effort, whether failure will lead to a loss in social prestige, etc, all these costs for each of the viable alternatives should be clearly specified.
- iv. **Gather information and weigh the alternatives:** This involves carrying out market estimates for demand under various conditions, assessing the likelihood of competitive reactions, e.g., whether there are other new markets if competitive activity decreases current market share, whether machinery can be easily modified to handle other products, or whether suppliers are likely to increase their charges if demand grows, etc.

The likely return to the company for each alternative should be assessed on the basis of market information, forecasts of future demand, assessment of competitive reactions, etc.

v- **Minimise risks:** This involves a realistic assessment of the extent to which the entrepreneur can affect the odds (the number of times something is likely to happen or not to happen), this involves clear awareness of the entrepreneur's abilities and the company's capacities, the ability to plan strategy and tactics to effect the change, etc.

vi- **Plan and implement the best alternative:** Once an alternative has been selected, a plan must be drawn up for its implementation. This would include a timetable, a clear definition of the goal, a set of plans for possible outcomes and a feedback process so that necessary changes can be implemented quickly. **NB:** Be a calculated risk-taker. Remember that in business, as in life, there is no clear way of avoiding risk taking. When you take risks, you discover your own abilities and you will become better able to control your own future. You will become more self-assured. You will have a more positive outlook towards risk taking because you will have faith in your own abilities.

3.4.4 Risk Management

In view of establishing the fact and reality of risks, there is need for risk management. It is the continuous process of identifying, analysing, evaluating and treating loss exposures, monitoring risk control and financial resources to mitigate the adverse effect of loss. Stephen and Joseph (2015) described it as the practice of identifying potential risks in advance, analysing them and taking precautionary steps to reduce it.

Risk management is an aspect of management that is concerned with:-

- Handling complete destruction through accident.

- Safeguarding the firms' ability to continue in spite of accidental loss that could hinder continued earnings.
- Planning and supervising the treatment of non-insurance risk and funded self-insurance schemes.
- Liaising with the insurance company for proper and prompt indemnity, and defences outside the insurance function.
- Monitoring the implementation of planned emergency and catastrophe schemes.

3.4.5 Risk Management Techniques

In managing risk, identify the source/ variables through interviews with staff, brainstorming sessions, scenario analysis, SWOT analysis etc. and devise methods to quantify the risk especially mathematical models.

There are different techniques of managing risks (Horton, 2015) as listed below:

1. Risk avoidance which implies not engaging in the activities that have very high potential for loss.
2. Risk reduction that involves the reduction of the risk in developing a new product through careful planning, strategizing and market testing. Taking of appropriate precautionary measures and procedures like fire and smoke alarms, burglary alarms and security guards, workers safety procedures etc.
3. Risk shifting which is the shifting or transferring of risks that cannot be avoided or reduced to insurance companies who then assume the risk. The burdens of loss resulting from pure risk are passed to insurance company in exchange for a premium.
4. Risk acceptance is a dangerous scheme as the organization may become vulnerable if the incident occurs.

Risk should be assessed and courageously embarked on. Taking risk is an adventure. Invention and innovation are risky. Taking risk is exploitative. Risk

can lead to progress. It is all embracing in decision making. Entrepreneurship entails risk and forecasting. Risk taking when desirable should be done systematically. Often, risk taking is an investment on its own, by and by, it will generate long-term returns. An entrepreneur must not be generally averted towards risk, if not, investment will be low in spite of promising returns. Investment involves risk taking. The investment climate of a country must be favourable enough before taking investment risk decision. This includes the government policies, relevant data and information with available infrastructural facilities.

Subsequently, the following factors should be considered before investing.

- a. Security: Investment should at least maintain their capital values.
- b. Liquidity: Short – term funds investment must be capable of being converted back into cash at short notice.
- c. Return: The highest return compatible with safety should be sought.
- d. Spreading risk: Spread investment over several types of security so that a possible loss with one may be offset by gains in others. When planned it is called portfolio.
- e. Growth prospects: The most profitable investments are likely to be in companies with growth potentials.

A positive assessment could make an entrepreneur to go ahead with the decision.

4.0 CONCLUSION

Pricing policies are considered one of the most marketing mix elements. The psychological pricing affects mainly from one consumer, to another. The importance attached to the price of a company's product by the consumer is significant to the marketing activities. Thus, in fixing a price for a product, marketing executives should consider necessary pricing policies and other market elements.

5.0 SUMMARY

In this unit, we examined, Pricing methods, Objectives of pricing policy, Nature and use of pricing discounts and Product positioning and price.

6.0 TUTOR-MARKED ASSIGNMENT

i. Let us assume that consumer behaviour in terms of units bought of this manufacturer is as follows:

Price	No. of units sold
22	50,000
21	60,000
20	70,000
23	40,000
24	30,000
25	20,000

What is the price at which the manufacturer should sell the product?

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UNIT 10 MARKETING MIX: PRODUCTS

CONTENT

- 1.0 Introduction
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 - 3.1 What is a Product?
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1.0 INTRODUCTION

Businesses are set up to produce products - goods and services. Goods are normally tangible items. Services are intangible items that can provide value and satisfaction and are also classified as products. This unit introduces you to various definitions of a product, classification of products and their characteristics.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- define a product
- Describe the levels of products
- classify products into either consumer or industrial products
- differentiate between consumer and industrial goods.

3.0 MAIN CONTENT

3.1 What is a Product?

A decision as to what PRODUCTS to sell must have been made. A product can be described as goods, services, ideas, people, places, and even organisations that are offered for exchange. Also, a product is defined as anything offered or sold for the purpose of satisfying a need or want on both sides of the exchange process and subject to review in the light of environmental factors like change in tastes, expectation, technology, income, fashion etc. It includes a tangible object that marketers refer to as a good, as well as an intangible service (such as ideas, a place, an event, an organisation), or any combination of tangible objects and intangible services. However, Stanton (1981:161) defined a product as a set of tangible and intangible attributes including packaging, colour, price, manufacturer's prestige, retailer's prestige, and manufacturer's and retailer's services, which the buyer may accept as offering want-satisfaction. It should however be noted that the consumer is not interested in your goods. He/she is interested in himself or herself and what benefits he/she will get, and not in you or your organisation. Other decisions that goes in line with products are branding, packaging, trademarks, labelling, number of products offered, time of introduction of new products, method of introduction and possible effects on competitors.

Branding: It is the combination of name, words, symbols or designs that depict the quality of a product and the company. Branding is the creation of an identity and goodwill for a product or line-of-products by assigning to it a name or symbol to avoid adulteration e.g. Omo, Maggi,

Knorr. Once customers identify the brand name with quality, it has won customers awareness and possible loyalty resulting to steady sales. Brand is associated with anything directly or indirectly linked or attached to the memory of the brand. It may be a slogan – m-1-10. Branding must be short and catchy. It distinguishes a product and the company from the competitors thereby taking it to the consumers' domain.

Brand selection guide any of this method can be used in selecting your brand name

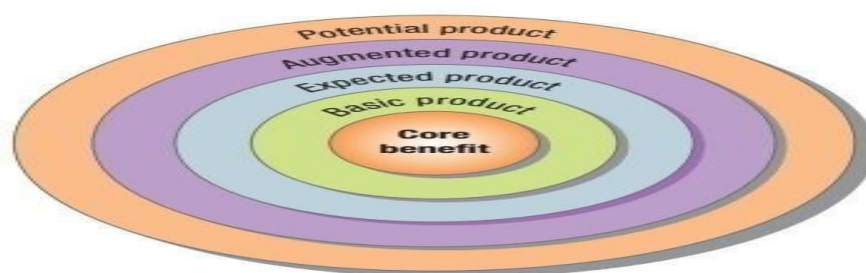
- (i) Individual brand name: Give every product a name so that if one product has a problem the reputation of the company still stands for other products. Cadbury Nigeria uses this style including Lever Brothers, Eva waters etc.
- (ii) An Umbrella Family name: Every product bears the family name like Philips, Hp etc. if one product is advertised, the goodwill will affect its entire product. If otherwise all its product line will be negatively affected.
- (iii) Separate family names: Each product has its own distinct name and image e.g. Coca-cola bottling company, 5-Alive, 7-up, Eva waters etc. This does not cause confusion at all.
- (iv) Company trade name combined with individual products e.g., Dangote flours, Dangote rice, Dangote sugar etc.

Packaging: This is the container or wrapper that contains the product, protects and identifies it. It must be attractive in colour, design, appealing, communicative of brand and usage, functional and economical.

Labelling: This is the printed material which carries information about the product and the seller, which may be part of the package or tag. The label is the mouthpiece of the product or producer. Hence it must be simple, clear, definitive and not congested or wordy.

3.2 Product Levels

This can be illustrated with the aid of a diagram as shown below:



Source: Kotler (1987). *Principles of Marketing*

(a) The Core Benefits: The fundamental service or benefit that the customer is really buying. For instance, the core benefit enjoyed by a guest in a hotel is rest and sleep.

(b) The Basic Product: Marketers must turn the core benefit into a basic product. For example, in the case of the hotel, such things as a bed, table, chair, bathroom, and dresser are the basic products enjoyed by a guest in the hotel.

(c) The Expected Product: Marketers prepare an expected product. A set of attributes and conditions buyers normally expect when they purchase a product. For example, in a hotel, guests expect a clean bed, fresh towels, constant power supply, and a relatively quiet environment.

(d) Augment Product: Marketers are concerned with preparing augmented products that exceed customers' expectations. For example, a hotel may have a remote-controlled TV set, remote controlled air conditioner, fresh flowers, etc.

(e) Potential Product: This consists of all the possible augmentations and transformations the product might undergo in the future, just as we have new products in our markets daily due to modifications and diversifications undertaken by manufacturers.

3.3 Classification of Products

Generally, products are classified into two types namely: consumer products and industrial products.

3.3.1 Consumer Products

Consumer goods are those which are used by ultimate consumers or households and in such form that they can be used without further commercial processing. Consumer goods can further be classified according to the amount of efforts consumers are willing to expend for purchases and the extent of their preferences for such products and services. Thus, consumer goods can be divided into:

- convenience goods
- shopping goods
- specialty goods
- unsought goods.

The functions of marketing can be classified into three, namely merchandising function, physical distribution, and auxiliary function as discussed in unit one.

Convenience Products/Goods

These are standardised products and services usually of low unit values that consumers wish to buy immediately as needs arise and with little buying efforts. The purchase is almost spontaneous and the person has already, a predetermined brand in mind. These convenience goods include soaps, newspapers, toothpastes, cigarettes, etc. Often, convenience goods are bought impulsively or spontaneously. For example, when a person goes for shopping and sees a product which attracts his eyes, he buys it on impulse. Such goods are not purchased on a regular basis.

Shopping Goods

These are goods which are purchased after going around shops and comparing the different alternatives offered by different manufacturers and retailers. In other words, these are durable items with differentiated product attributes that consumers wish to compare in order to be able to find the most suitable for their needs before buying. In this case, the emphasis is on quality, price, fashion, style, etc. They therefore have to be marketed differently. Examples of such goods are clothing, household appliances, and furniture.

Specialty Goods

These are products that consumers insist on having. The buyers are willing to wait until the right products are available before they buy them. Consumers have either developed special taste or liking for such goods. Specialty products are usually

specific branded items rather than product categories. They are specific products which have passed the brand preference stage and reached the brand insistence stage. Examples of these are cars, jewellery, fashion clothing, photocopy machines, and cameras. They are usually very costly items and include luxury items.

Unsought Goods

These are goods that people do not seek, either because they did not plan ahead to buy them, or they did not know they exist before they saw them on displays at the point of purchase. Most new and recently introduced products will fall into this class. Therefore, aggressive and continuous promotion is necessary for them. Examples of unsought products include life insurance, encyclopaedia, and blood donation to the Red Cross Society.

3.3.2 Industrial Products

These are products that are used by producers who convert them into consumables or consume them in their processes of conversion or production of their goods. Industrial products are those purchased for further processing or for use in conducting a business. The distinction between consumer and industrial goods is based on the purpose for which the particular product is bought. The classification of industrial goods is based on how they are used by industries.

Akanbi (2002) classifies industrial products into five namely:

- Installation
- Equipment, Tools and Accessories
- Raw Materials
- Semi-Processed Components and Parts
- Consumables and Operating Supplies.

Installation

These are major capital items that form the main assets of production firms. They are very costly items that need major decisions before they are purchased. They

include product items as buildings, heavy manufacturing machines, computers, etc. These are usually custom made items that will require direct negotiations between the buyers and the sellers.

Equipment, Tools and Accessories

These are usually standardised items that are used by a wide range of industrial users. They are products like typewriters, hand tools, filing cabinets, and air conditioners. They are production operating items.

Raw Materials

They form the major parts of the finished items. They are the materials that go through the production line to make up the finished items. They include the raw materials of agricultural products, mining products, forestry products, sea and water products. They are usually standardised items that are sold based on and their Reliability of supply.

Semi-Processed Components and Parts

These types of industrial goods also form part of the finished items, although some of them are finished items already like buttons for shirts, radio and batteries for cars. Parts can be used by themselves or can be used to form components of the final items.

Consumables and Operating Supplies

These are the convenience items of industrial products. They are used to aid the running and maintenance of the organisations equipment and for keeping the organisations and their machines in proper shape. They are usually standardised items and of low prices. Examples are stationery, fuel, water, grease, etc.

3.3.3 Characteristics of Industrial Products

- i. The demand for industrial goods is derived from the demand for the final goods which they are used to produce. The higher the demand for the

final item, the higher will be the demand for the industrial goods and vice versa.

- ii. The demand for industrial goods is mostly inelastic. The amount of items bought of an industrial product remains essentially the same regardless of the price. This is because most items are not made of one single product, but a combination of products. For example, a car is made of the body, tyre, radio, air conditioners, lights and so on. If the price of the items is increased, they will still need the same number for each car. Although if the price falls, they may buy more to stock in anticipation of a rise in price in future.
- iii. Most industrial goods have joint demands with other industrial items. As in (ii) above, most finished goods are a combination of very many products and an increase in the demand for one item will lead to an increase in the demand for the other product.
- iv. The industrial goods markets are usually concentrated and few than the consumer goods markets. Most of the users of industrial goods are usually concentrated in industrial estates. Government, parastatals and other institutions that use industrial goods are usually concentrated in few locations. The typical industrial buyer is very well informed about what they want to buy. They also know the alternative sources of these items.
- vi. The industrial buying process is usually more rational or the decisions to buy them are more economically based than in the consumer buying process.

3.4 Delineation between Consumer and Industrial Products

The distinction between consumer and industrial goods is based on the purpose for which the particular product is bought. Industrial products are generally subject to greater standardization, as against certain consumer products which require frequent changes in fashion and style. Advertising normally is an

important promotional tool for consumer products, but may not be so in the case of industrial products. Personal selling and after sales service are generally more important for industrial products. Industrial products generally involve high value purchases and this involves competitive bidding based on price competition. Selling is done on the basis of quality or tangible attributes. As against this, consumer products are very often sold for psychological satisfaction. For example, in case of soaps, Lux soap is said to offer you a complexion like that of a film star!

Consumer products require elaborate channels of distribution, but industrial products are sold through fewer outlets and often directly by the organisation itself. These are some of the salient features of marketing of consumer products as against industrial products.

4.0 CONCLUSION

A product is the key marketing mix variable on which all the other marketing mix variables revolve. It cannot be diverted from other marketing mix variables, because all of them contribute to form the images of the product from the point of view of the buyers. These images determine the values and satisfaction expected from a given product and how much the buyers will offer for it. It is therefore important for the manufacturers and marketers to understand what a product means to consumers and their expectations from that product.

5.0 SUMMARY

In this unit, you learnt what a product means, various classifications of products and necessary strategies adopted for consumer and industrial products.

6.0 TUTOR-MARKED ASSIGNMENT

- i. What is a product?
- ii. Differentiate the following with the aid of examples:

- a. Convenience goods.
- b. Specialty goods
- c. Shopping goods.
- d. Unsought goods.

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UNIT 11 MARKETING MIX: PLACE (CHANNELS OF DISTRIBUTION)

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1.0 INTRODUCTION

Placing goods and services where they are required and when they are wanted is the area of concern of this unit. A company's channel decision directly affects every other marketing decision. For example, the company's pricing depends on whether it uses mass merchandise or high quality specialty stores. The firm's sales force and advertising decisions depend on how much persuasion, training and motivation the dealers need. Whether a company develops or acquires certain new products, may depend on how well those products fit the abilities of its channel members.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- Elucidate the channels of distribution
- explain types of channels
- describe the role of distribution channels in the overall marketing of products
- state the factors involved in selection of an appropriate channel mix.

3.0 MAIN CONTENT

3.1 Channels of Distribution

The term channel of distribution is used to refer to the various intermediaries who help in moving products from the producer to consumers. There are a variety of middlemen and merchants who act as intermediaries between the producers and consumers. Stanton (1981:283) defined a channel of distribution for a product as ‘the route taken by the title to the ultimate consumer or industrial users’. A channel always includes both the producer and the final customer for the product, as well as all middlemen involved in the title transfer. Even though agent middlemen do not take actual title to the goods, they are included as part of a distribution channel. This is because they play such an active role in the transfer of ownership. A channel of distribution is also defined as a system designed to move goods and services from producers to customers, which consists of people and organizations supported by various facilities, equipment, and information resources. However, Armstrong and Kotler (1994) argued that distribution channel is a set of interdependent organisations involved in the process of making a product or service available for use or consumption by the consumer or industrial user‘.

Channels of distribution are the most powerful element among marketing mix elements. Many products which were intrinsically sound have died in their infancy because they never had the right road to the market. However, by developing a sound distribution network and launching aggressive advertisement campaigns, a company can carve out a niche for itself. However, it is better to study the distribution network before launching a product.

Channels of distribution help movement of goods from one place to another and thus create place utility. They make it possible for the consumer to get the goods when he wants them and thus create time utility. They bring goods to the consumer in a convenient shape, unit, size, style and package and thus create convenient value. They make it possible for the consumer to obtain goods at a

price he is willing to pay and under conditions which bring him satisfaction and pride of ownership and thus create possession utility.

It should however be noted that the concept of marketing channels is not limited to the distribution of physical goods alone. Producers of services and ideas also face the problem of making their goods accessible to their target consumers. Channels of distribution can be grouped under two major headings namely, Direct Selling by Manufacturers and Indirect Selling through Middlemen.

3.1.1 Functions of distribution channel

A distribution channel moves goods and services from the producers to consumers. It covers the gaps that separate goods and services from those who would use them. Members of the distribution channels perform many key functions which include the following.

1. **Information.** Gathering and distributing market research and intelligence information concerning customers' competitors.
2. **Contact.** Finding and communicating with prospective buyers.
3. **Matching.** Shaping and fitting the offer to buyer's needs, including activities such as manufacturing, grading, assembling and packaging.
4. **Negotiation.** Reaching an agreement on price and other terms of the offer so that ownership or possessions can be transferred.
5. **Financing.** Acquiring and using funds to cover the costs of the channel work.
6. **Risk taking.** Assuming the risks of carrying out the channel work.
7. **Transport.** This function may be provided by the supplier, the distributor or may be subcontracted to a specialist for some products such as perishables, transport planning is vital.
8. **Stock holding and storage.** For production planning purposes, uninterrupted flow of production is often essential. A good stock or inventory control system is designed to avoid stock outs while keeping stock holding costs.

9. **Local knowledge.** As production has intended to become centralized in pursuit of economies of scale. The need to understand and be close to local market is of a paramount importance.
10. **Promotion:** Developing and spreading persuasive communications about an offer.
11. **Physical distribution:** Transferring and storing goods to the appropriate place.

3.2 Intermediaries in the Channel of distribution

An intermediary is someone who mediates or brings about a settlement between two or more persons. In distribution these are middlemen who, form a link between the original supplier/manufacture and the ultimate buyer/consumer. The following are different types of intermediaries (channel members) who exist in the channel of distribution.

1. **Retailers.** These are traders operating outlets which sell directly to households (final Consumers)
2. **Jobbers.** These buy from wholesalers and sell to small retailers who generally are not served by larger wholesalers.
3. **Wholesaler.** These buy or stock ranges of produces from potentially competing manufacturers which they sell to retailers. Many wholesalers specialize in products.
4. **Distributors or dealers.** These contracts to buy a manufacturer's goods and sell them to customers. Their function is similar to wholesalers but they usually offer a narrow range of products, e.g. in case of car dealers may be Toyota. Nissan, etc. they have only combination of a number of manufacturers and serve as their distributors.
5. **Agents.** These differ from distributors in that they do not purchase and resell the goods but sell goods on behalf of the supplier and earn commission on their sales.

6. **Franchisee.** These are independent organizations who buy there right to own and operate one or more units of the parent company. An initial fee and usually a share of sales revenue is paid to the parent company for a specific period of time to allow the franchisee to sell under the patent name/trade mark of the parent company.
7. **Multiple stores.** These buy goods for retailing direct from the producer. Sometimes under their own label or brand names e.g. supermarkets, departmental stores, etc.
8. **Direct sales/distribution methods.** These include mail order, telephone, door to door selling, personal selling, suppliers retail outlets, etc.

3.3 Types of Distribution Channels

Distribution channels can be described by the number of channel levels involved. Each layer of middlemen that perform some work in bringing the product and its ownership closer to the final buyer is a channel level. The producer and the final consumer both perform some work as part of every channel. We use the number of intermediary levels to indicate the length of a channel. All of the institutions in the channel are connected by several types of flows. These include the physical flow of products, the flow of ownership, the payment flow, the information flow, and the promotion flow.

Consideration will be given to two types of marketing channels – channels for consumer goods and channels for industrial goods.

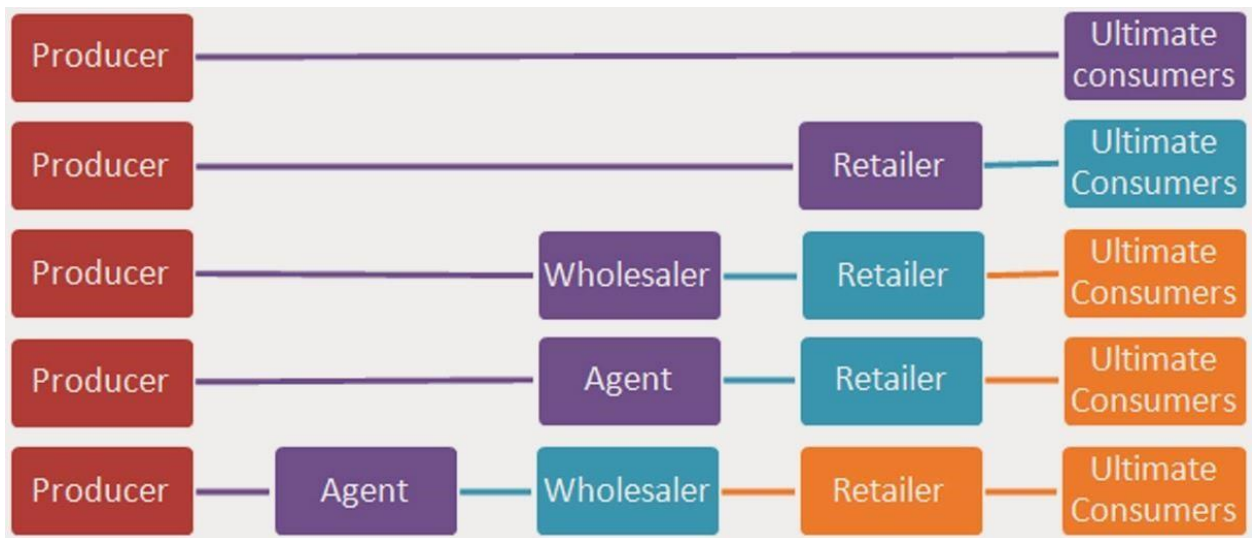


Fig. 1: A Channel for Consumer Goods

Source: Amstrong & Kotler (1984)

(1) Producer to the Consumers: When there are no intermediaries between the producer and the consumer, the channel is direct. This type of channel is most commonly used with organisational products, especially where the product is new. This is aimed at creating awareness and to gain access to target consumers.

(2) Producer to Retailer to the Consumer: The channel from producer to retailer to the consumer is common when the retail establishments involved are relatively large.

(3) Producer to Wholesaler to Retailer to the Consumer: The most common channel for consumer goods. It employs a wholesaler to take care of the shipping and transportation needs. Wholesalers offer the accumulating and allocating functions that allow small producers to interact with large retailers, and vice versa.

(4) Producer to Wholesaler to Jobber to Retailer to the Consumer: the producer chooses to use agents (Jobbers) to assist the wholesalers in marketing goods. The use of Jobbers could be attributed to their specialised experiences.

(5) Manufacturer to agent to wholesaler to retailers to consumers. This channel involves the producer supplying goods to his agent who sell to the whole

sellers who in turn sell to the retailers and finally from the retailers to the final consumers.

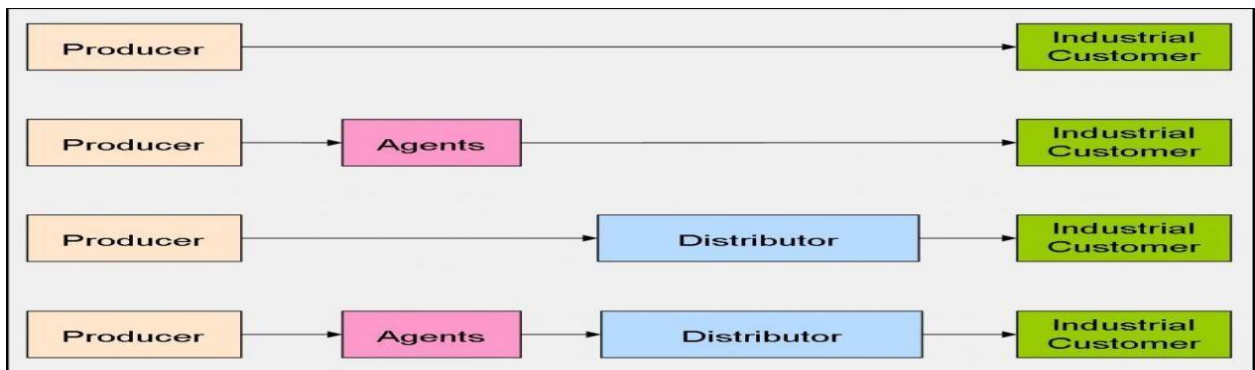


Fig. 2: Channels for Industrial Goods Source:

Armstrong & Kotler (1994)

- 1. Manufacturer (producer) to Industrial Customer (Buyer):** From the diagram above, manufacturers use direct marketing to distribute their products to the industrial users. This is mostly associated with complex products that require a good deal of pre-sale and post-sale support. It should be noted that post-sale support is often best handled through a direct channel, because the manufacturer might be the only entity with sufficient expertise to help the customer. This route is suitable where there are few customers who may also be geographically concentrated.
- 2. Manufacturer to Industrial Distributor to Industrial Customer:** This is the most used channel for industrial products. Distributors take title to the goods and specialize in different lines of goods. Some of the disadvantages associated with this channel are that:
 - a. Distributors will want access to large accounts that the manufacturer may try to keep for itself.
 - b. Distributors try to keep their product selections wide, which frequently means carrying competing lines.

Sometimes distributors do not always respond to manufacturers' advice regarding promotions, pricing and operational policies. It is used where there are many customers who may be geographical dispersed.

3. This channel of distribution for industrial goods is mostly adopted by manufacturers which wish to maintain control over their products. It also applies to those goods that are sold across countries. Other factors include cultural factors, and government policies, etc. This route is used by the producer who wants to enter a new market of which he has no knowledge about
4. The fourth channel of distribution is adopted by manufacturers which wish to have control of marketing activities of their products. However, some titles to the goods are given to industrial distributors, who sell to the industrial customers when needed and at the quantity needed. This route is used by manufacturers who industrial buyers purchase in small quantities and must be re-supplied frequently and the company has no sales to carry the distribution activities.

3.3.1 The Importance of Channels of Distribution

The importance of channels of distribution is summarised below:

1. Channels of distribution are the most powerful element among marketing mix elements. Many products which were intrinsically sound died in their infancy because they never found the right road to the markets.
2. Channels take care of the transaction aspects of marketing, including the selling, the financing and the risk taking associated with strong products in anticipation of future sales.
3. They perform the logical function of moving products from the point of production to the point of purchase.
4. They help producers promote goods and services.

3.4 Selecting a Distribution Channel

The channel decisions are important (for two reasons). The costs involved in the use of a channel entail the price that the consumer must pay. The channel decision also has a bearing on other marketing decisions like pricing and product line. Through proper market feedback, an appropriate selection of channels can reduce fluctuations in production. A rational decision regarding choice of channels of distribution should ensure:

- (a) maximum geographical coverage of the markets
- (b) maximum promotional efforts, and (c) minimum cost.

The following factors usually govern the selection of channels:

- 1. The nature of the product.** This refers to the make of goods being distributed. Generally bulky and heavy Products are distributed directly to minimize the transportation cost of goods. Similarly, perishable and expensive products are sold directly or through a short channel. Whereas goods that are long lasting and can easily be stored, any channel can be used including the long ones.
- 2. The nature of the market.** The market where the goods are going to be sold does influence the distribution channel to be used in the distribution of goods and services. Normally, the short channels of distribution is preferred when the market is small and is located in a narrow area. On the other hand, in case of a large market and with geographically scattered customers, along channel is normally used.
- 3. The nature of the business.** The nature of business determines the kind of channel to be used. For example, the trading business can use all the distribution channels available while a business such as agric-business will need to use a short channel of distribution. In addition to this in cases, where a manufacturer desires control over distribution, direct selling is preferable.
- 4. Nature of the middlemen** the nature of middlemen required in the distribution of goods should be considered when determining the channel of

distribution to be used. When the desired type of middlemen is not available, the short channel of distribution is used while on the other hand, if the nature of the available middlemen is desirable, the long channel or medium channel of distribution can be used.

5. The value of the product. If the product is of a high value and does not need a lot of handling (i.e. if a lot of handling negatively affects its value), then a short distribution channel should be used. On the other hand, if the product is of low value, a longer distribution channel may be used to minimize on the costs.

6. Distribution policies of an enterprise. This will depend mainly on the financial and production capacity of the enterprise. In cases where an enterprise is financially stable and desires control over distribution, direct selling may be used and in cases where the financial capacity is limited, longer channels of distribution may be used.

7. The cost of the channel. The cost effectiveness of the channel used in the distribution of goods should be considered. The cost involved should be considered and the entrepreneur should select the least cost but effective channel of distribution i.e. manufacturer should compare the cost of distributing goods through all the available channels.

8. Speed and urgency of the product. Products which are needed urgently by the consumer in a short period of time always need to be distributed through the short channel. On the other hand, goods which are not urgently needed may use any channel of distribution.

9. Level of competition in the market. If there are high levels of competition in the market, a short channel of distribution should be used in order to ensure that goods are delivered in time to out compete the others. On the other hand, in cases where the level of competition is low, medium or long channels of distribution can be used.

10.The availability of the required storage facilities. This is in relation to products which are to be sold to distant parts of the country where storage facilities are required. In cases where storage facilities are available and can be rented, the entrepreneur can choose the middlemen i.e. a medium channel of distribution. On the other hand, absence of storage facilities would require the manufacturers to sell directly to the customers.

11.Quantity to be bought: If the consumer is willing to buy on a large scale, then it is possible that the producer can sell directly to the consumer hence a shorter channel of distribution is used, On the other hand, if a consumer is buying a small quantity i.e. on a small scale, the producer may end up selling using medium or long channels of distribution i.e. through wholesalers, agents, etc.

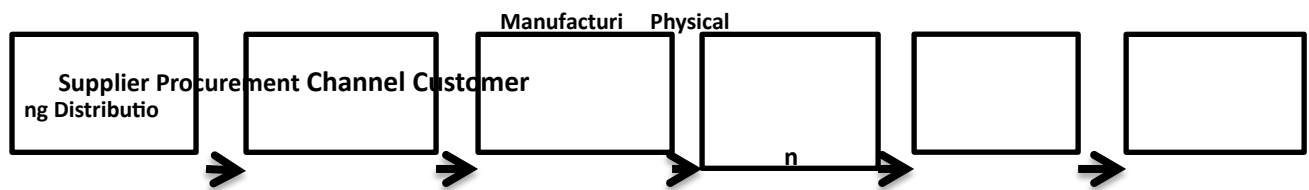
NB. An effective distribution channel is one which;

- (i) Maximizes profits.
- (ii) Minimizes risks.
- (iii) Maximizes sales.
- (iv) Minimizes costs.
- (v) Captures a large market share.
- (vi) Convenient to operate by the entrepreneur, seller and the customers.

3.5 Physical Distribution Tasks

Producers/manufacturers must decide on the best way to store, handle and move their goods and services so that they are available to customers at the right time and place. Producers typically need to employ the services of physical firms – warehouses and transportation companies - to assist in this task. Armstrong and Kotler (1994) observed that physical distribution tasks involve planning, implementing, and controlling the physical flow of materials and final goods, from points of origin to points of use, to meet customer requirements at a profit.

The aim of physical distribution is to manage supply chains and value-added flows from suppliers to final users, as shown below:



Source: Armstrong and Kotler (1994). *Principles of Marketing*. 6th Edition. Englewood Cliffs, New Jersey

There are several tasks that have to be accomplished as part of physical distribution. These are:

1. Location of Manufacturing Facilities: There are two interrelated issues.

Firstly, where to locate the manufacturing facility and secondly, how many facilities should be set up. The basic decisional parameters would be the availability of the basic raw material and the location of the market. It may decide to locate the manufacturing facility nearer to the source of supply and ship the finished outputs to the outlying markets or to erect the production facility near the geographical market to be served and arrange the shipment of the inputs. The location of NNPC for example, in Port Harcourt was based on the availability of raw material

(crude oil) yonder. The basic consideration involved obviously is the relative costs of transporting inputs and outputs, including the economics of different modes of transportation which may be used to transport raw materials and finished products.

2. Location of Warehouses: One important consideration in this context is the nature of the product being sold. If the product is a household item, such as tea, soap, or toothpaste, the retail outlets will be at the bottom of the distribution channel. A manufacturer of capital equipment on the other

hand, can have only one centralised warehouse for the main product, but has to maintain a number of service centres to stock spare parts.

- 3. Mode and Method of Transportation:** There are several key decisional points in this context which for long were considered the heart of distribution management. These are:
 - a. Which mode of transportation would be optimal?
 - b. Which method of distribution would be optimal?
- 4. Inventory Decisions;** Inventory holding costs are always on the increase due to all round increase in prices as well as cost of capital. As a result, very careful attention has to be paid to how much inventory should be maintained, of what items and where. Many of these decisions have to be taken, keeping in view the broader corporate objective of service reliability, i.e. the capacity of the firm to deliver on time.
- 5. Using External Distribution Agencies;** Much of what has been discussed above refers to firms which want to distribute products on their own. However, a firm may decide that because of resource constraints or lack of in-house expertise, it would like to concentrate on production and leave the task of distribution to an outside agency such as Independent Marketers in Nigeria. Whether to contract out distribution or not, is a major decision and would require an in-depth analysis of the relative costs and benefits, both tangible and intangible, of the alternative courses of action.

4.0 CONCLUSION

Distribution is the all-important link between a manufacturer and his customers. The concern is for designing a distribution channel to facilitate the smooth physical flow of products from the manufacturers to the place where the customers can buy them.

5.0 SUMMARY

In this unit, you learnt what marketing channels are, the role of distribution channels in the overall marketing of products, and factors responsible for selecting an appropriate channel mix. Channels of distribution refer to the alternative paths through which the goods can be routed. Direct selling and indirect selling through intermediaries such as wholesalers and retailers are the two alternative channels of distribution to choose from. The final choice will depend on the type of product which you are dealing with, number and location of customers and their buying habits and costs involved. The manufacturers should also consider the specific advantages of each type of intermediary before taking a final decision.

6.0 TUTOR-MARKED ASSIGNMENT

- i. Explain factors to be considered while selecting an appropriate channel of distribution.
- ii. Briefly explain the term —Marketing Channels

4 REFERENCES/FURTHER READING

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UNIT 12: Marketing Mix: Promotion

CONTENTS

1.0 Introduction

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1.0 INTRODUCTION

Sales promotion covers areas where publicity and advertisement does not cover. In contrast to advertising and publicity, which use impersonal methods of communication, personal selling makes use of direct personal communications to influence the target customers. Personal selling is a highly distinctive method of promotion, and makes use of oral presentation in conversation with existing and potential customers, for the purpose of making a sale. It is one of the oldest and most expensive methods of business promotion. An increasing number of firms making use of it, and a good number of them realize that they cannot, perhaps, live without it. Any innovation in goods and services are not complete until it is accepted in the market place. Acceptance in marketplace is evidenced in buying and selling. This unit deals with certain salient information needed for effective buying and selling.

2.0 OBJECTIVES

On completion of this unit, you should be able to:

- Explain sales promotion
- Discuss the process involved in planning sales promotions
- List different types of sales position and sales promotion schemes
- Describe the steps involved in the selling process.
- Understand the various terms of selling goods and services
- Discover various conditions involved in credit sales
- Highlight the modes of proper cash management
- Explain the procedures from inquiry to delivery of goods
- Comprehend the way to choose a supplier

3.0 MAIN CONTENT

3.1 Sales Promotion

Of all the methods of promotion that constitute the promotion mix, sales promotion is the only method that makes use of incentives to complete the push-pull promotional strategy of motivating the sales force, the dealer and consumer in transacting a sale. There is no single universally accepted definition of sales promotion. One can, however, gather its essence by perusing a few definitions. Let us look at some of the popular definitions of sales promotion:

According to the American Marketing Association, sales promotion refers to:

'those activities other than personal selling, advertising and publicity, that stimulate consumer purchasing and dealer effectiveness, such as display shows and exhibitions, demonstrations, and various other non-recurrent selling efforts not in ordinary routine.' This definition suggests that sales promotion is a catch-all for all those promotion activities which do not fall clearly into advertising, personal selling or publicity.

Roger A. Strang offers a simple definition *'Sales Promotion is short term incentives to encourage purchase or sale of product units or service.'* Yet another perception that seems fairly exhaustive, and hence, will be used in this unit is Stanley view on sales promotion as:

'all the marketing and promotion activities, other than advertising, personal selling, and publicity, that motivate and encourage the consumer to purchase by means of such inducements as premiums, advertising specialties, samples, cents-off coupons, sweepstakes, contests, games, trading stamps, refunds, rebates, exhibits, displays, and demonstrations. It is employed as well, to motivate retailers', wholesalers the manufacturer's sales forces to sell through the use of such incentives as awards or prizes (merchandise, cash and travel), direct payments and allowances, cooperative advertising, and trade shows'. It offers a direct inducement to act by providing extra worth over and above what is built into the product as its normal price. These temporary inducements are offered usually at a time and place the buying decision is made.

Summing up, sales promotion deals with promotion of sales by the offer of incentives which are essentially non-recurring in nature. It is also known by the names of Extra-Purchase-Value (EPV) and below-the-line- selling.

Like in other market economies, the use of sales promotion is catching on in Nigeria in terms of volume. In terms of the expenditure incurred, the large size companies are stated to be spending between 40 and 50 per cent of their advertising and sales promotion budget on this activity. In terms of product groups, the major users of sales promotion are: tea, coffee, and beverages, soaps, detergents and washing soaps, toothpaste, textiles, food products and baby foods, household remedies, and consumer durables like fans, refrigerators, sound systems, television and other household appliances. Among the various types of sales promotion schemes used, **contests** at the consumer, dealer and sales force levels have made a significant headway.

3.1.1 Sales Promotion Methods

Sales promotion methods are built around these three target groups. Further, in terms of the impact desired, the variety of sales promotion schemes offered are grouped into two categories: one, aimed at producing immediate impact, and the other delayed impact i.e. carrying on the impact over a period. On one hand, immediate impact schemes are those schemes where the consumer, dealer or salesperson gets the incentive on first contact, purchase or on performing a one-time act. On the other hand, under the delayed impact schemes, the consumer, dealer or sales force is called upon to comply with the scheme over a period of time before receiving the full benefit of the scheme. Table 2 presents the variety of sales promotion schemes directed at the consumer, dealer and sales force levels according to their grouping under immediate impact or delayed impact categories. The meaning and objectives of these schemes are given in Table 2. than the normal price.

Table 2: Sales Promotion Scheme

Impact	Users	Non-Users	Trading/Suppliers	Sales force
Immediate	Price Off	Price-Off	Discount allowance	Pre-requisite
	Quantity- Off	Sampling	Shell space allowance	
	Over the counter	Over-the-counter		
	Package Premium Branded Premium Container Premium	Gift Push money Position of sales force		
	In Production	Media Dorr	Merchandise	Sales contests
Delayed over a period of time	Coupon	Coupon	Deals	
	Personality	Returns	Coupons	
	Premium offers	Refund	Displayed contests	Honors and recognition
	Trading stamps	Cooperative allowance		Customer service awards
	Self-liquidators	Sales contest		
	Contents/Lucky Draws			

Source: Donald W. Cowell's article on Sales Promotion and the Marketing of Local Government Recreation and Leisure Services, *European Journal of Marketing*, 18.2.

Table 3: Sales Promotions: Meaning and Objectives

S/N	SALES PROMOTION	MEANING	OBJECTIVES
1	Price-Off Offers	Offering product at lower than the normal price.	To encourage immediate sales, attract non-users, induce new product trial, counter competition, inventory clearance at the retail level, inventory build-up at the trade level.
2	Quantity-Off Offers	Offering more quantity of the same product at no extra cost or with a very nominal increase in the price of the larger quantity packs	To encourage more/longer duration consumption, higher or excess quantity movement from the factory, trade up consumer for higher quantity packs size.
3	Premium packs.	Offer of an article of merchandise as an incentive in order to sell product or service. Its forms are;	To encourage purchase, stimulate loyalty, off-season sales promotion, induce trial of new product, ensure reach of premium to the consumer.
	a. Packaged premium	When the incentive article is packed inside the package of the product	
	b. Branded premium	Where the premium article is handed to the package of the product say with cello tape, etc.	Sampling new products, adding speed to show moving products.

	c. Over-the-Counter premium	When the premium article is neither inserted inside nor branded to the product package but is given away to the consumer over the counter along with the product package.	To counter competition, improve inventory clearance at the trade level.
	d. Container premium	When the product itself is home placed in an attractive and reusable container which serves as a gift.	As a durable reminder at home.
	e. Self-Liquidating Premium	Where the consumer usually is asked to pay a specified amount to liquidate or offset a part or full cost of the premium article or the scheme administration costs	To induce consumer to appropriate premium article, reinforce brand image, encourage more consumption, enables sponsor to offer better quality premium.
	f. Personality premium	Where the consumer is required to redeem a specified proof-of-purchase.	To build loyalty and reward the consumer for that to counter to purchase for the premium article. Proof-of-purchase may be labels, pack tops, bottle tops, corks, etc.
4	Coupons	When the consumer is entitled to redeem a specific standard certificate for a product/article free or a part payment. Coupons are used by both the manufacturer and the dealers for sales promotion. Coupons may be distributed by mail, by media advertisements, door-to-door, inside product package or by dealers on purchase.	To encourage product trial, build loyalty, trade-up regular users, stimulate re-purchase rate, and solicit inquiries.
5	Refund Offers	Offer of a refund of money to	To induce trial from primary

		the consumer for mailing in a proof-of-purchase of a particular product	users, motivate several product purchase, obtain displays at the retailers, help retailers tie-in with other products, switch competing brand users to sponsor's brand, loading dealers with increased stock.
6	Trading stamps	Organized by trading stamp companies or large retailers. Trading stamps are a kind of discount coupons offered to consumers linked with the quantum of the purchase.	To encourage consumer loyalty to certain retail stores.
7	Consumer contests and lucky draws	Where individuals are invited to compete on the basis of creative skills. The latter is based on the chance or luck factor	To create brand awareness and stimulate interest in the brand, acquaint consumers with brand usage and benefits, build traffic at the store, precipitate brand purchase, obtain consumer feedback, promote advertising scheme of the company.

8	Dealer Stock Display Contest	It is a type of point-of-purchase advertising which uses the show windows of the dealers for providing exposure to the sponsor's products. Dealers participating enthusiastically and creatively are rewarded.	To provide product exposure at the point of purchase, generate traffic at the store, infuse enthusiasm among dealers.
9	Dealer Sales Contents	Where participating dealers are invited to compete in terms of the sales performance.	To increase sales, buyer dealers' loyalty, motivate dealers' staff to sell more.
10	Discounts	Other than normal trade and cash discounts.	To push more sales to trade, early cash recovery.
11	Trade Allowances	These are temporary price reductions/reimbursements of expenses incurred by dealers, in full or in part, its varied types are as under;	
	a. Trade or Buying Allowance	Offer of price reduction on purchase of specified quantity of a product	To load the trade
	b. Buy-Back allowance	A secondary incentive which offers a certain sum of money to trade for each additional unit brought over and above the deal.	To encourage trade cooperation and stimulate repurchase.
	c. Count and Re-count allowance	When a specific amount of money is offered after ascertaining the number of units sold during a specified period.	To move stocks faster, reward on sale only.
	d. Merchandise (display) Allowance	An allowance to trade for providing desired sales promotion and product displays.	To create enthusiasm in trade, improve traffic and exposure at the point-of-purchase, gain larger space/effort of the trade in the promotion of sponsor's product of against the competitor's.
	e. Cooperative advertising and promotion allowance	Wherein a manufacturer shares at an agreed rate the advertising and promotional cost incurred by the dealer in the promotion of manufacturer's product.	To gain product and retail identity, motivate dealers to promote manufacturer's product, obtain local advertising and promotion.
12	Dealer Gifts	Offer of useful articles and attractive gifts to dealers for their personal, family or office use.	To improve dealer relations, make impact on consume scheme/contest offered.
13	Premium or Push Money	When an additional compensation is offered to trade or sales force for pushing additionally a specific product or product line.	To push a specific product or product line.
14	Merchandise Deals	Where additional quantity of the same, same manufacturer's product is offered to trade may be offered jointly by noncompeting manufacturers.	To load dealers with inventory, expose other products of the sponsor encouraging dealers to sell more and early to realize their incentive.

15	Point-of-Purchase (POP)	Those special displays, racks, banners, exhibits, that are placed in the retail store to support the sale of brand.	To attract traffic at retail store, remind customers, encourage impulse buying additional visibility to the advertising campaign.
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Source: Donald W. Cowell's article on *Sales Promotion and the Marketing of Local Government Recreation and Leisure Services*, *European Journal of Marketing*, 18.2.

Though ideal for consumer goods, sales promotion is also used for promoting industrial goods. The difference in the use lies in the types of schemes offered, and in the frequency of their offer. Sales promotion schemes offered to industrial customers, include product demonstration, training to customer staff, offer of interest-free instalment payment plan, ready and regular availability of repairs and spares, and posting of trained staff to assist/supervise in the working of the equipment in the client's premises, at the manufacturer's cost. The sales promotion schemes offered at the level of industrial distributors are, provision of extended credit and provision of specialized sales/technical staff at the manufacturer's cost, besides the usual cooperative advertising and sales promotion, gifts, and organisation of distributors' contests. The sales promotion schemes popularly used to motivate the industrial sales force are prizes and awards on special achievements, sales contests, new accounts contests and prompt service awards.

3.1.2 Effects of sales promotion

In addition to increasing competition, other reasons for rapid growth of sales promotion in Nigeria as pointed out by some large sized cooperating companies in surveys are summarized below:

- Sales promotion makes an immediate effect on sales.
- Measurement of the effectiveness of sales promotion is easier as against other promotional methods.
- Channels of distribution are emerging as powerful entities and demand greater use of incentives to get desired results.

- Products are becoming standardized and similar, and so need increased support of non-price factors of which sales promotion is an important one.
- Impulse buying is on the increase, and so is the rise in the number of marginal customers. With virtually no brand loyalty, offer of attractive schemes helps manufacturers to induce such customers to choose their product.
- obtains more and better shelf space and displays
- brings more customers to dealer stores
- makes goods move faster through dealers
- improves manufacturer-dealer relationship
- motivates sales forces to take the achievement higher than targets
- attracts sales force to give desired emphasis on new accounts, latent accounts, new products, and difficult territories
- rewards sales forces for active market surveillance and for rendering superior customer services
 - counters competitors' sales-promotion and marketing efforts
 - provides punch to the company's advertising efforts
 - Builds goodwill.

Companies may use any one or a combination of the above objectives in varying forms to suit the product-market needs of their product. What is of significance is that the sales promotion and marketing objectives are pursued by the company.

3.2 Personal Selling

Personal selling, as the name implies, is an individual selling that involves word-of-mouth. It is the oral presentation in a conversation with or more prospective purchasers for the purpose of making sales. It, therefore, carries the distinctive advantage of flexibility in terms of tailoring the sales presentation to the needs of the buyer. Another unique advantage comes from its two-way communication and human interaction, thereby providing instant feedback. These two unique advantages make personal selling the most result-oriented promotion method.

Generally speaking, the nature of goods marketed, as well as the distribution system adopted; determine the role of personal selling in a firm. Therefore, personal selling is used extensively in the case of industrial goods, where the salesperson performs functions such as assisting the customer in designing the product specifications, product installation, product commissioning, solving technical problems through providing service after sales and helping the customer to have optimal utilization of the product. In the case of consumer goods, on the other hand, the role of personal selling gets usually restricted to the dealer level. The scope of the tasks performed include obtaining periodic orders, ensuring supplies, offering tips to dealers on product display and attaining desired levels of stock movement. Similarly, the role played by personal selling is more in a firm, which uses the door-to-door selling method through its sale force than in the firm, which sells through large stockists, distributors or sole-selling agents. Notwithstanding the varying role of personal selling in the strategies followed by different companies, the nature of the selling function requires that the following tasks be performed:

- Sales generation
- Feedback and market information collection
- Provision of customer service covering aspects such as delivery of goods, warranty administration, timely availability of repair and spares, etc.
- Performance of sales support activities such as monitoring the distribution function, credit collection, improving manufacturer dealer relations, implementing the promotional programmes, etc.

In practice, the complexity of the selling task actually performed varies from company to company even under the above four categories.

3.2.1 Types of Selling Jobs

Robert N. McCurry classifies individual sales positions based on the degree of creativity required into seven categories. These seven categories are described:

- a. **Merchandise Deliveries:** The primary job is to deliver the product usually against routine orders, popularly called sales and delivery boys.
- b. **Inside Order-taker:** Works inside a store with the primary job of servicing the customer 's request or suggest appropriate products to meet customer wants. They are popularly called retail salesman.
- c. **Outside Order-Taker:** The salespersons engaged in the task of taking orders from the resellers. They normally do not use the hard selling approach for making orders.
- d. **Missionary Salesperson:** The job is to educate, give product detailing, build goodwill or create primary demand for the product. Strictly speaking, missionary salespersons are not permitted to take orders.
- e. **Sales Engineer:** They act as a technical consultant to the client and as per the need, helps to design products or production system for a client. They are called Technical Salesperson, e.g. Computer salesman.
- f. **Tangible Product Seller:** Sells tangible products such as furniture, appliances, automobiles, etc. The job involves abilities to persuade and convince the customer to buy.
- g. **Intangible Products Seller:** Sells intangible products or renders services such an advertising, insurance, education, etc., the common factor is the difficultly in immediate demonstration of the perceived benefits of the product. It requires the greatest degree of creativity in the salesperson.

Each company should clearly define what it expects from a salesperson in terms of the tasks to be performed, specify the time to spend on developing new accounts versus servicing existing accounts, large accounts versus small account etc. The job of a salesperson should be defined with sufficient specificity as a guideline to stay in the right direction.

3.2.2 The Selling Process

The basic step in the selling process is given in Table 1 in reverse order.

1. A salesperson must become accomplished at performing the selling steps.

Table 1: Steps in the Selling Process

Assure customers on the correctness of their decision. Check whether the order was filled and delivered when promised. Is certain product properly installed, used and served.		POST-SALE FOLLOW-UP
Make conscious effort to close. Exhibit no fear of rejection.	CLOSE THE SALE	
Understand reasons for objection Have a positive attitude. Avoid arguments.	HANDLING OBJECTIONS	
SALES PRESENTATION		Arouse Desire
APPROACH		Make initial contact with prospect
PRE-APPROACH		Study the organization and those involved in buying
PROSPECTING AND QUALIFYING		Develop sales lists from various sources Separate the suspects from the prospect
PREPARATION		Know your product. Know your customer. Know your competitor. Know your company

Sources: Ralph M. Gaedeke & Dennis H. Tootelian (1983)

Step 1

Preparation: Before starting the selling job, a salesperson should make a valuable investment of time and resources to know the products to be sold, the customers (i.e. customer types, buying motives and buying process), the competitors, and finally know the philosophy, policies and range of products of his company. In short, he should be well equipped with the fundamentals of selling.

Step 2

Prospecting: This step deals with the location and preparation of a list of prospective customers. Prospects can be located through (1) identifying the potential of buying more, by the existing customers, (2) recommendations of

existing customers, (3) winning back lost customers, (4) attracting competitors' customers, (5) customers' information request from advertisement, (6) newspaper announcements, (7) public records, (8) directories like telephone, trade associations etc., (9) other salesmen, (10) references from friends, neighbours and business associates, and (11) cold canvassing, that is, going from door-to-door.

The located prospects should first be qualified broadly in terms of (i) whether they want the product and how intense their want is, (ii) whether they have the adequate purchasing power, and (iii) whether and who possesses the power or authorization to purchase and spend the required money. The qualifying of prospects is the process of separating the prospects from the suspects.

It is worth mentioning here that the ability to prospect is the most essential ability of a successful salesperson. A good salesperson keeps examining, weeding out the already tapped prospects and updating his/her lists of prospects, and remains in constant search of new prospects.

Step 3

Pre-approach: The salesperson should possess detailed information relating to the prospects in terms of existing products consumed, scale of operation, product range, buying size, frequency, budget and the process, etc. In short, obtain customer orientation. The sources of information for this purpose include company annual reports, other salespersons, other suppliers to the prospects, census of manufacturers, professional journals, newspapers and market intelligence. The availability of the above information in as detailed a manner as possible will help the salesperson in ranking the prospect in classifying the prospects in A, B, and C categories in terms of the immediacy of the attention to be given to them.

Step 4

Approach: First impression counts.' As such, this step needs to be carefully planned. This step has two distinct parts. One, of meeting the customer with a

positive set of mind, and the second is make an impact on him. For the former, referrals of reliable persons known to prospects, calling after fixing an appointment, use of door openers, help. For the latter the salesperson should equip himself with key benefits to be emphasized, samples or new literature to be handed over, etc.

a. How to present a product?

When presenting a product to a customer:

- consider customer's privacy, convenience, ability to use the product, etc.
- consider the needs of target customers.
- consider the giving of samples, guarantee, etc to back up the product.
- consider presentation aids like photographs, catalogues and charts to back up the product.

Step 5

Sales Presentation: Through advance information relating to the prospect, every effort should be made to match the product offered to the needs/problems faced by the customer. The sales presentation should generally go according to the AIDA—Attention, Interest, Desire, and Action approach. How can this be done? Use of key benefit or a problem solver, or a unique act of the salesperson results in gaining attention. The presentation should proceed in a straightforward manner to help the prospect know that you understand his problem and that is the reason of your being there. To convince the prospect as early as possible, the salesperson should offer evidence through demonstration of the product, use of exhibits, models, sharing of acts, citing examples of successful applications/usage, showing testimonials, etc. The overall approach should be to build credibility and confidence in the supplying company, its products, and also in its competence to render specialized type of service to the complete satisfaction of its customers.

The flexibility of the sales presentations can range from the ‘canned’ or previously prepared presentation, to those allowing the salesperson complete freedom in the presentation. Though both extremes, and even the hybrid of the two, have their own situational suitability, the important point to note is that salesmanship, being a showmanship function, must arouse active participation of the prospect in the presentation process. This can be done by introducing some action which would keep the prospect captivated. One possible way would be a joint review of the problem faced by the prospect. Another is helping the prospect imagine the projected benefits of owning the product.

b. How to bargain with customers?

When bargaining, avoid dominating the customer and should try to give the customer satisfying reasons why the product is being sold at the price, may also give counter offers like reduction in price, delivery services, etc.

c. How to give personal attention to customers?

In order to give personal attention, an entrepreneurship should understand the needs of customers and come up with those products that satisfy them, i.e. the products need to be at the right price, right, quantity, should be given the right promotion and in the right place and at the right time in order to meet the needs of customers identified by the entrepreneur.

d. How to follow up orders from suppliers?

Ensure that the physical address and postal address, telephone numbers and all other contacts, you can make other methods of contacts as you follow up your order like writing a reminder letter, visiting suppliers' premises, sending an e-mail, making telephone calls, etc.

e. How to collect overdue accounts?

- Sending polite reminders to customers with overdue accounts and suggesting the dates for settling the debt.

- If no response is received within the specified time, a stronger worded reminder should be sent.
- If recovery is not affected, employ courts of law for those debtors who stubbornly fail to pay.

Step 6

Handling Objections: It is in the last phase of the sales presentation step that the prospects start expressing doubts, or raising objections whether relating to price, need for more time to think, satisfied the existing product/supplier or product quality claims.

The golden rules for handling objections are:

1. Welcome the objection and show respect to the prospect, and
2. Do not argue with the prospect. Even when the objections raised are half-baked or trivial in nature, the salesperson should handle the situation tactfully. Only in extreme necessity, should a salesperson ask the prospect to adequately explain the problem faced. Even under these circumstances, courtesy should not be lost sight of, and while the discussion is on, the salesperson should start recounting the benefits of the product agreed upon, and lead the prospect to make a favourable decision. It should be remembered that handling objections sharpens the selling skills of the salespersons.

How to handle difficult customers?

In order to handle difficult customers, an entrepreneur should:

- acknowledge and evaluate customer objections fairly,
- listen carefully to the words being used and feelings being expressed,
- leave the customer to be open such that you can understand the basis for his being difficult.
- The customer may raise some important points.

- Buy time by suggesting that you will look at the issue later.
- As you try to convince the customer from your point of view, hold your argument until the customer agrees with you.
- Compensate customers by price reduction or refund or replacement of the goods in case the previous ones had a problem like being damaged or expired.

Step 7

Closing the Sale: Closing is that aspect of the selling process in which the salesperson asks the prospect to buy the product. There is a critical point during each presentation when the salesperson should ask for the order. Pending the location of the critical point, as the objections are being met, the salesperson should help reduce the choice of options, summarize the benefits of buying, and the consequences of not buying, and if need be, make use of the large idea appeal of the buying - now' at that moment.

The salesperson should have the ability of catching the buying signals given by the prospect and should act on them fast. Some of such signals are changing the sitting/standing position and moving closer to the product; reading the instructions on the product; perusing the testimonials; showing hesitation in being able to afford; asking for another demonstration, if applicable; checking the warranty or asking questions relating to warranty terms. These signals show that the time is ripe to start taking the order.

Step 8

Post-sale Follow-up: The selling process does not come to an end by writing the order. A few repetitions reassuring the benefits of the product keep the customer sold. Follow-up provides an opportunity to ensure that the product is being rightly used, and if necessary to re-explain the method of using, handling, and storing of the product when not in use. This builds favourable feelings and nurtures the strong buyer seller relationships. Post-sale follow-up not only reinforces the customer's confidence in the salesperson and his company but also tends to keep

competition out. This also helps generate repeat business and valuable word-of-mouth publicity. The follow-up is a good source of feedback too.

Let us conclude this section by stating that although the eight steps of the selling process are essential in spirit, these may not always be followed. This could be partly the (1) the selling situation involved (e.g. in the case of insider order taker or retail salesperson the first three steps of the selling process are generally not applicable as the customer walks into the store for buying a product), (2) the expertise of the salesperson (such that he can ignore or assume some information), or (3) the seller's market of the product where customers generally queue up for the product.

Let us also look at the findings of a study by Robertson and Chase on the subject. They point out that:

1. The more closely matched the physical, social and personal characteristics of the customer and salesperson, the more likely is the sale.
2. The more believable and trustworthy the customer perceives a salesperson to be, the more likely is the sale.
3. The more persuadable a customer is, the more likely is a sale.
4. The more a salesperson can make prospective buyers view themselves favourably, the more likely a sale is.

Before you read further, attempt this exercise.

SELF-ASSESSMENT EXERCISE 2

What general procedure should be followed when qualifying prospects?

3.3 TERMS OF SELLING GOODS AND SERVICES

The act of selling goods and services is about transacting goods from a particular source till it gets to the final consumer. A source could be from the manufacturer to the wholesaler, or to the agent or any middleman with the ultimate of getting to the final destination. At any point in time there are certain terms of selling.

1. **On cash basis.** The buyer pays cash at a time of receiving goods. It may be cash on delivery or cash and carry. The seller in this case should always issue a cash receipt to the buyer.
2. **Selling on credit basis.** This involves providing a service or giving out goods to a customer who promises to pay at a later date. Normally an invoice which is a demand note is issued to such a customer.
3. **Payment in kind.** This is trade by barter. A customer pays for the service or goods by rendering another service. This exists in the informal economy where people normally do not have the money to pay for such goods or services.
4. **Payment in instalments.** This involves a part payment and continuous payments in small bits to customer until the price for the item is finally completed. The customer may not take the item with him or her until it has been fully paid depending on the policy of the enterprise.

3.3.1 ADVANTAGES AND DISADVANTAGES OF CASH SALES

The advantages include:

1. There is a constant supply of working capital.
2. The entrepreneur can plan properly for the use of his working capital.
3. There is proper management of stock.
4. There is constant supply of stock since the cash is always available.
5. There is low risk of bad debts.

The disadvantages include:

1. It has a negative effect on sales since people may not have cash on spot.
2. It is difficult to operate on a cash basis in a very competitive market.

3.3.2 PROPER CASH MANAGEMENT

When cash is received at any point of sales, depending on the terms, it must be properly managed by putting in place the following measures.

1. Businesses should receive a bank statement, on a regular basis for proper accountability and knowing the cash flow of the business. Financial reconciliation should be carried out with the business books to detect any errors.
2. All business cash should be banked. Business should run savings or current accounts with a credible banking institution. This helps the business to manage their cash because withdrawals will be controlled.
3. All cash kept at the business premises or places of work should be jealously guarded and kept under locks and the keys.
4. All cash received in the business should be receipted and be properly stored for accountability. This will prevent stealing or embezzling any business transaction since the receipts will serve as reference.
5. All documents to do with cash should be documented and authorized by the owner of the business personally and other designated officers like the cashiers, accountants, etc.
6. Proper accountability should be made whenever expenditure is made and be mindful of indiscriminate withdrawal. This makes it easy for the business to plan in relation to cash in flows and out flows.
7. A petty cashbook or imprest system be opened for day-to-day running of the business.
8. **External certified auditors** should annually audit the business books of accounts to detect any cash theft or losses.
9. At times, **employing of close relatives** to manage the finances of the company is used to ensure proper cash management.

3.3.3 CONDITIONS FOR CREDIT SALES

A lot of care should be exercised when selling on credit. Therefore, an entrepreneur should sale on credit where there is a combination of the following.

1. When there is sufficient working capital to finance the credit sales.
2. If there are strong and effective laws, which can protect the entrepreneur and recovery can easily be enforced.
3. If you cannot buy on credit, then it will not be advisable to sell on credit, since it will tend to take down the working capital in the business.
4. If faced with a deflation economic situation.
5. If a buyer can present a collateral security, which can help the recovery in case of failure to pay. A collateral refers to any asset or any other saleable material that a debtor deposits so that in case of failure-to repay the debt, the entrepreneur can sell it to recover the debt, example of collateral includes cars, buildings, house hold items such as TV set/ radios set.
6. When a buyer is well known to the seller and has been clearly observed as having the capacity and character of paying back.
7. When the means to know the credit worthiness of the customer is available, for example, the customers may get recommendations from other suppliers.
8. When the condition prevailing around the customers are conducive, since such conditions may affect his present or future income. For example, a businessman would need to think twice before granting credit facilities to an individual working for a company that is retrenching its staffs or an individual who has a lot of financial obligation to settle, etc.
9. When faced with crisis e.g. if the goods are due to expire soon, goods are getting off fashion etc.

3.3.4 ADVANTAGES AND DISADVANTAGES OF CREDIT SALES

The following advantages are associated with selling on credit:

1. High prices may be charged which increase the business' profits.
2. It is used as a marketing tool and this increases the sales. Many customers who don't have cash on spot are able to make transactions.

3. It helps in disposal of perishable or about to expire goods. This reduces the losses to the business.
4. Selling on credit enables the business to meet the customer's financial requirements.
5. Selling on credit enhances the buyer's bargaining power because of the credit that is extended to them.
6. Selling on credit helps in building customer's good will and relationship, which will result in repeat purchases. This increases the business clientele.
7. Selling on credit acts as a bridge to customers by enabling them to get their daily needs.
8. Selling on credit would favour the business during high levels of competition and recessionary economic conditions.

The following are the disadvantages associated with credit sales

1. Selling on credit may tie up the working capital of the business. This may result into reduction in stock.
2. Under credit, the buyer may not be in a better position to bargain. For that matter therefore the trader may over charge the buyer.
3. Selling on credit may come along with strings attached,
5. The business may collapse as a result of bad debts. Many people may fail to clear their debts.
6. Administering credit requires a lot of record keeping and paper work, which may be *expensive* to the business.
7. Selling on credit may be associated with high costs, which may include follow up and eventually moving to courts of law.

3.4 From Inquiry to delivery of goods

What is meant by purchasing?

Purchasing refers to obtaining materials of the right quality in the right quantity at a right price from the right source delivered to the right place at the right time.

Purchasing involves:

- Checking where they can be acquired.
- Establishing the right price and negotiating for the purchase of materials.
- Payment, Movement and Storage.

Placing order for goods (purchasing)

People involved in purchasing of materials for the business are expected to have the following purchasing skills if they are to make the right decisions on quality, quantity, time and price.

- Identification of alternative sources and solutions for the procurement of materials.
- Protecting the cost of procurement, ordering and storage of materials.
- Maintenance of a good relationship with the suppliers.
- Ensuring the right quality and quantity when ordering for the goods.

a) Right quality. The person purchasing should be able to determine the right quality of materials needed. The quality of any material comprises of the features which are relevant to its ability to meet a given need. One can take the following steps to ensure that procurement of the right quality of materials;

1. Identify the need for all types of your materials and property specification of each material to be procured.
2. Try to use standard materials available or existing in the market.
3. Assessing the supplier of the product based on the following. i. Past performance. ii. Reliability, iii. Visiting or reference to other customers, iv. Expertise and experience, and v. Quality consciousness.
4. Inspection of materials before accepting to ensure that the right quality is delivered as per the samples taken.

b) Right quantity. The quantity ordered should depend on the following.

1. The consumption rate of the raw material both in terms of time and quantity.

2. The available finance for purchasing and the costs.
3. The stock of material one can afford to maintain i.e. the ability to store,
4. The standards of packing prevalent in the market or the price for the items i.e., for small or large size packs.

(c) Right time. The time to purchase or procure materials should be decided depending on the following.

1. **Lead-time.** This refers to the time it takes from placing an order and the (exact) time of receiving the goods.
2. **Mode of transport.** The means of transport to be used for delivery. Some means of transport like railways and water transport are slow yet air transport is quick and very fast.
3. Place of purchasing materials i.e. local, national or international.
4. **Government policy.** This is mainly regarding taxes. Knowing when taxes are high, there are low helps in choosing the suitable time.
5. Market fluctuations in terms of prices and availability. Some products have high price fluctuations linked to seasons, market demand, etc.

However, the problems of right time include the following.

1. Failure to fulfil the commitment by the supplier because they also depend on other suppliers.
2. Problems involved in delivery of goods like non-availability of transport, manpower, bad roads, etc.
3. Lack of follow up or failure to remind the suppliers on the purchases,
4. Increased demand of materials in the market causing price instability.

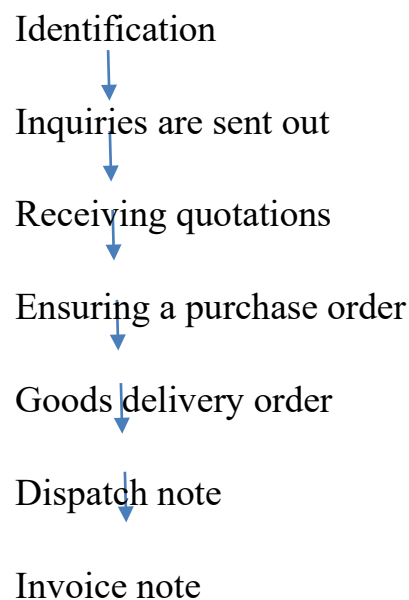
d) Right price. The right decisions can be taken to buy at a certain price will depend on the following.

1. The value as perceived by the clients,
2. Cost of production and level of production i.e. is the item produced at a high or low cost. Is it a finished, semi-finished or raw material?

3. Negotiation and bargaining capacity of your firm.
4. Competition and other market considerations like urgency, non-availability of the product, etc.
5. Added value and sales prices for products.
6. The cost of availing finance for buying i.e. borrowed finance will affect finance at a percentage interest and the ruling price in the market.

The process of ordering for goods/services

Ordering for goods and services can either be done verbally or through writing. Regardless of the methods used, the following steps are followed when ordering for the goods/ services.



1. **Identification of goods and services required.** Here the business from its needs can identify the required goods and services.
2. **Inquiries are sent to possible suppliers.** This is done together with accompanying documents like pictures and specifications which enable the supplier to quote. The following is an example of a letter of inquiry.

AFUZAB INVESTMENTS
P.O.BOX 6 ZARIA, KADUNA STATE

Tel.....

Date.....

No...987

BAZUF NIG LTD

KANO

Dear sir/ Madam

RE: SUPPLY OF MOTORCYCLES/TY

Please quote us your price, terms of payment and delivery for the following items;

Quantity	Description
15 units of motorcycles	Yamaha DT 125
04 tyres	13 x 2.75 mm size

Yours faithfully

Haruna kabiru

Purchasing officer.

3. **Quotations will be received in response to the inquiries.** This will be accompanied by the price lists, catalogue samples, quality delivery and other terms of the supplier. A **quotation** refers to a document which is prepared by the potential supplier and sent to the buyer in response to the inquiry letter e.g. prices, lead time, delivery terms, etc. The following is an example of a quotation in response to the above.

AFUZAB INVESTMENTS
P.O.BOX 6 ZARIA, KADUNA STATE

Tel.....

Date.....

No..987 BAZUF

NIG LTD

KANO

Dear Sir,

In response to your letter of inquiry No 987

Quantity	Total price	Description	Unit price (N)
15 motorcycles		Yamaha DT 125cc	50,000.00
			750,000.00

(fully assembled 13 x 25mm)

Payment/ Delivery: 15 days from date of receipt of your order and 20%
down payment Discount: 5% discount of paid in agreed period
Looking forward to receiving your order.

Yours faithfully.
Muritala Bardi

4. **A purchase order will be issued to the supplier whose quotation has been accepted.** A copy of the order is always retained for reference purposes. A **purchase order** is the document requesting to be supplied with the goods already quoted. Its components include description of items, terms and conditions, purchase price, address of the purchaser, a formal instruction of "please supply", etc. The following is an illustration of a purchase order.

AFUZAB INVESTMENTS P.O.BOX 6 ZARIA, KADUNA STATE		
Tel.....	Date.....	
No.987		
BAZUF NIG LTD		
KANO		
Dear sir,		
RF.: PURCHASE ORDER 555		
Please supply and deliver the following items,		
Quantity	Description	Unit price (N)
Total price		
15 motorcycles	Yamaha DT 125	50,000,00
	750,000,00	
	(fully assembled)	
	13 x 25mm	
Enclosed in our cheque No. 0005674 for, 750,000 being 100% full payment		
Yours faith fully.		
Zainab Bardi		
Purchasing officer		

5. **Goods delivery note.** This refers to a document that accompanies the goods supplied. The purchaser signs the document after delivery. The following is a sample of a delivery note that/ could be used.

AFUZAB INVESTMENTS
P.O.BOX 6 ZARIA ,KADUNA STATE

Tel.....
No.....987
BAZUF NIG LTD
KANO

Date.....

Delivery Note No......

Quantity price	Description	Unit price (N)	Total
.....			
.....			

6. Delivered by..... **Dispatch note.** This is normally given at the time when goods are being dispatched. It is expected to be sent separately and is expected to reach the purchaser before the arrival of the goods. It therefore, informs the purchasers that the goods have been dispatched and are on the way. This gives him chance to prepare his store in advance or make arrangement for the sale of the old stock. The means of transport can be indicated.

7. **Invoice.** This is a demand note. Once the delivery note has been received, checked and signed by the purchaser, the supplier is expected to prepare an invoice which indicates the balance due. The invoice shows that goods have been delivered on credit.

NB. The following should be observed when receiving goods and services purchased.

- Check quality and quantity against order.
- Check delivery document against order.
- Check for any damage.
- Reject deliveries that do not conform to the order.

3.4 CHOOSING A SUPPLIER.

It is important to make proper choice of the suppliers of goods to purchase at reasonable and affordable, prices. The quality needed by the customers should be emphasized. The following factors, therefore, need attention when choosing your supplier of goods.

- 1. The quality of goods and services supplied:** should be to the expected or agreed upon standards. The supplier should be one who has persistently sold items of good quality approved by the national bureau of standards.
- 2. The consistency and reliability of a supplier:** This is the ability to supply enough whenever they are ordered.
- 3. There should be ease of communication with the suppliers:** This ensures that whenever a given item is required, the supplier will easily be accessed.
- 4. The terms and conditions also need to be examined.** Suppliers have got different terms and conditions of payments. For example, some can supply goods only on cash basis, others can deliver/allow credit terms while others can allow the buyer to get goods on hire purchase, or deferred payment. Some suppliers can also offer discounts i.e. trade or cash discounts, (discount refers to a percentage reduction on price).
- 5. The lead-time together with the distance between the supplier and buyer:** The lead time will depend on several things which include mode of transport, place from where goods and *materials are to be purchased I.e. Is* It local or an international; purchase, the conditions of the chosen supplier, the number of orders, methods of production used by the suppliers, etc.
- 6. Taxes and regulatory procedures in the purchase and delivery of goods** **always** need to be considered when choosing suppliers. Normally, taxes make products more costly i.e. (they increase the cost of the product). For that matter therefore it is always very important for the entrepreneurs to look for the source of goods and services where taxes are either low or not, levied.

7. The price at which the supplier is selling the product must be considered.

This should normally be done through comparing prices of different suppliers for low-cost suppliers of quality goods.

8. The after sales services offered by different suppliers always influence the choice. Entrepreneurs take on suppliers who can offer better after sales services.

9. The reputation of the suppliers: Suppliers with a good reputation in the market is a preferred option.

10.The distance: It is at times better to choose suppliers who are close in geographical terms.

4.0 CONCLUSION

Promotion is an important marketing mix. Given the complexities in the management of the promotion function and its vulnerability to failure, it is desired that the function be managed professionally. The procedures of buying and selling are very crucial information in managing a small business. Proper cash management is important when goods are sold on cash basis. Credit sales procedures are different from cash sales. The choice of a supplier can make or mar a small business.

5.0 SUMMARY

In this unit, we discussed the nature, role, types and the planning process involved in personal selling and sales promotion methods of promotion. Personal selling is a direct person-to-person selling and promotion method. The specific role and goals of personal selling vary from firm to firm depending upon the nature of goods marketed, distribution system used, and the sales strategy adopted by a firm. The changing market environment calls upon the sales force to transform it in order to perform a more creative role.

6.0 TUTOR-MARKED ASSIGNMENT

- i. Everybody (both trained and untrained) partakes in sales jobs nowadays. List and explain 5 types of sales jobs.
- ii. Selling is a professionalized field; hence, there are processes that one should follow in order to achieve sales objectives. Briefly explain the first five 5 processes.

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MODULE 3

Unit 13: Sources of Information and Effective Communication

Unit 14: Elements of an Information System

Unit 15: Budgeting and Ratio Analysis

Unit 16: Break-Even Analysis and Chart

UNIT 13: SOURCES OF INFORMATION AND EFFECTIVE COMMUNICATION

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1.0 Introduction

This unit discusses sources of information, the strategic importance of information, characteristics and costs of useful information, and internal and external information.

2.0 Objectives

At the end of this unit, students will be able to;

- Understand the meaning of Sources of Information
- Know the strategic importance of information
- Explain the characteristics and costs of useful information
- Identify Internal and External sources of Information.
- Discover the communication skills needed for information dissemination.

3.0 Main Content

3.1 Strategic Importance of Information

Raw data are basically facts and figures. Facts and figures are not particularly useful unless they have meaning. If any form of data presented cannot be interpreted, then the data is useless. Information is a processed, interpreted or organized data that can influence someone's choices and behaviour. It is knowledge obtained from investigation, study or instruction. It is the bedrock of any communication. It can be sourced as primary or secondary

In the present hypercompetitive business environments, information is as important as capital for business success. It takes money to get businesses started, but businesses cannot survive and grow without the right information. Information has strategic importance for organizations because it can be used;

- a. To obtain informed strategic decisions by providing insights to evaluate available alternatives.
- b. Assist in risk management as changes in the market or regulatory environment that could impair the operations of the business.
- c. To create and sustain a competitive advantage. However, sustaining a competitive advantage through information technology is not easy to do, the key to using information technology to continuously improve and support the core functions of a business.

3.2 Characteristics and costs of useful information

Information is useful when it is

- **Accurate:** Information is useful when it is accurate. Before relying on information to make decisions, you must know that the information is correct.
- **Complete:** Information is useful when it is complete. Incomplete or missing information makes it difficult to recognize problems and identify potential solutions.
- **Relevant:** You can have accurate, complete information, but if it doesn't pertain to the problems you are facing, then it is irrelevant and not very useful.
- **Timely:** Finally, information is useful when it is timely. To be timely, the information must be available when needed to define a problem or to begin to identify possible solutions. Costs of useful information;
- **Acquisition costs:** This is the cost of obtaining data that you do not have.
- **Processing costs:** This is the cost of turning raw data into usable information.
- **Storage cost:** The cost of physically or electronically archiving information for later use and retrieval.
- **Communication costs:** This is the cost of transmitting information from one place to another.

3.3 Sources of Information

There are two sources of information: Internal and external sources

3.3.1 Internal Sources of Information

Internal information consists of data created for the sole use of the company that produces it, such as personal files, trade secrets etc. There are different types of

internal information such as financial, personnel, marketing, sales, manufacturing and administration. Internal information sources can be defined as follows;

- **Financial information;** this information is related to the performance and profit and loss of the company. This will include information on how much you pay for items, how much you pay for staff, the costs of rates and the taxes that you pay as a business. To monitor the financial information, you need to have a financial controller or accountants to ensure that the business continues to operate and generate a profit.
- **Personnel Information:** Personnel information is information held by the company on their employees. This information must be freely available to the employee any time they request it. It can be used to monitor an employee from entry point of documentation till exit by retirement, redundancy or death. The employee can progress within the company after their information is updated with any internal or external training programs that relate to their job.
- **Marketing Information:** Marketing information is used by the market team to identify what products or services offered by the business are most successful. The marketing team can collect information from different departments such as sales to promote certain products or services based on current success rates. Marketing information can be obtained using external sources or by using surveys to see what customers like or dislike about your product or service. This information can be used to streamline or improve your business and keep customers happy.
- **Purchasing Information:** Purchasing information is collected by the purchasing department who are involved with buying all the products needed to run your business. These products could be stationary or computers need for the day to day running of your business or multimillion dollar parts used in your manufacturing process. The purchasing

department needs to monitor the cost and quality of all purchased goods to ensure they get the best deal and maximize profits for the company.

- **Sales Information:** Just like the purchasing information sales information needs to be monitored based on the product or services offered by your company. This information needs to be passed to the financial controllers of your companies to ensure that the cost of your good or service is less than the sale price. If the sale of a certain product is down, then this information would need to be passed to the marketing team to see if it is worth launching a new marketing campaign to increase sales of the product.
- **Manufacturing information:** This is information about the cost of manufacturing goods within the company. The manufacturing cost will normally include the running cost of all machinery, the wages paid to production staff and the cost of raw materials (including waste) used up in the manufacturing process. An example of monitoring manufacturing costs would be for a company that mass produces furniture such as IKEA they would need to ensure that they create cut patterns to ensure that they got as many parts as possible from a single 8 foot by 4-foot piece of ply would. If they decreased the amount of waste cut by 10% this could save the company millions over a few years.
- **Administration Information:** Administration information links very much with personnel information but also involves communicating with external sources and storing information on customers to build successful relationships with them.

3.3.2 External Source of Information

External information is whereby documentation is made available to the public from a third party. As well as internal sources of information companies can also

use external sources to help them make the correct business decisions. Examples of external information sources are: Government, trade groupings, commercially provided information, database and research. If a company uses external sources of information, then they must be sure of the reliability of the data sources. Here are some examples of how the company could use information supplies by external sources.

- **Government:** Information supplied by the government is coming from a reliable source as this is the governing body that they business operates within. Companies need to use important legal information from the Government to help run the business successfully and legally. For example, if a company had over 1,000 employees that were being paid the minimum hourly rate as outlined by the Government and the rate changes then the company needs to take this information on board and increase the wages for the staff on this wage range.
- **Trade Groupings:** A trade grouping is a group of businesses that operate within the same sector and not within the same location. For example, tech companies would be part of the Technical Trade Association and Farmers might be part of the Farming Association within a country or region. As a business being a member of a trade grouping enables you to access information that helps you run your business successfully. For example, solicitors are part of the legal trade and will have memberships that give them access to the latest laws that they must use to support their clients in the best possible way.
- **Commercially Provided:** Companies can use commercially provided information to help them make the correct business decisions. These decisions are made based on information made available to them from other companies. For example, a hotel group might use the information about the number of flights to and from several airports along with the

information on the number of hotels beside each airport to make a decision on where to open their newest hotel.

- **Databases and Research:** Companies can research information that might help them increase the sales and level of interest in their business. The key thing to researching information that helps run your business to ensure it is accurate and reliable. Some companies will pay to access commercially available databases that offer a range of information directly based on their business sector. Many companies can make money creating this information by analysing currently available sales stats business sectors. When using any external information source, it is essential to be sure about the reliability of the data sources and sometimes it is worth paying to access relevant information.

Information is vital and communicating information is very essential for businesses.

3.4 Communication Skills in Business

Communication skills must be developed in order to communicate the information appropriately. Information is not useful until it is well communicated.

1. Communication is a two-way process that involves the transfer of information, ideas and knowledge acquired from one person or organisation (sender) to another (receiver). It simply refers to giving and receiving information and receiving feedback. It is important to develop effective communication skills, which will enable them to deal and relate very well with their clients and other parties or stakeholders who may have interest in their business.

Since not everybody is gifted with the art of communication and even those that are gifted may not be aware of the treasure they have, there is a need to have training and exposure in the skills of communication.

Basically communication skills include Reading, Writing, Speaking, Listening, Body language and Information technology. For instance, when a prospective

buyer sends an inquiry letter, he or she wishes to know about the goods or services available for sale, by an intending seller replying the inquiry with a quotation, this shows that the goods or services being inquired about are available. In this way, both the intending buyer and seller have shared information through communication.

Communication is not as simple as one may take it to be, studies have come up with different designs of the communication process, this is known as "Communication Models" or "Communication Cycle".

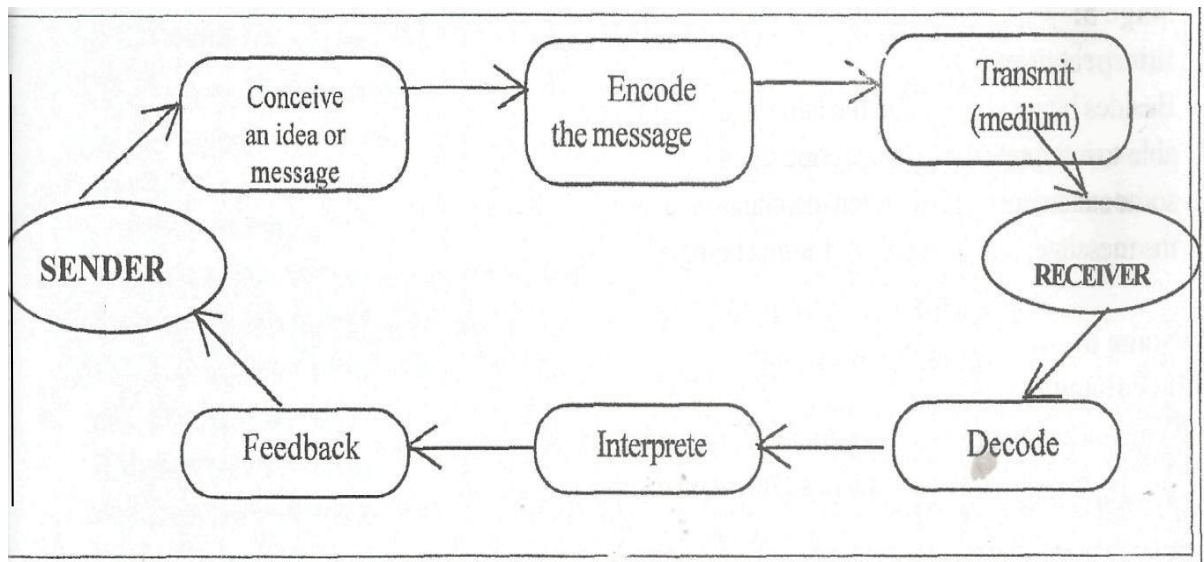
3.4.1 The communication Cycle / Process.

Communication flows in different directions depending on who is sending it.

- i. Downward communication that flows from top to bottom, for instance from Managers down to the subordinates.
- ii. Upward communication that flows from bottom to top, for instance from subordinates to Supervisors.
- iii. Horizontal and diagonal communication takes place between different functional departments of the organisation like from the Production Manager to the Purchasing Manager.

The communication cycle involves the various steps that are followed to convey a message between different parties: i.e. between the sender and the receiver. It

can be illustrated as below:



An illustration of the communication cycle

Stage 1: Conceiving

This involves getting an idea to be communicated, thinking and meditating upon it and developing it such questions include: what exactly do I want to say? What is my target receiver? What is my purpose of communication? What do I hope to achieve? etc., such questions will save the sender the embarrassment of sending half -baked message.

Stage 2: Encoding

This means putting the message into an understandable form, the sender encodes it into an appropriate "language" of communication, the spoken word (oral), the written word, body language:, numbers or numerals, visual or pictorials, etc.

Stage 3: Transmitting

The sender chooses an appropriate medium, channel or route through which the message will be sent, for instance using a telephone, post office, etc.

Stage 4: Decoding

At this stage, the message is in the hands of the receiver. To decode means; to extract the message from the codes in which it was encoded. A receiver has the

task of understanding the message. If it is an oral message, the receiver should be able to hear and understand the language of the speaker. If it is a written message, the receiver should be able to see and read a written task, or if it is pictorial or visual, the receiver should be able to identify and relate the picture or diagrams to the- message.

Stage 5: Interpretation

Besides, the receiver should be able to interpret the message correctly, this involves "reading between lines" i.e. ability to interpret some statements with hidden meanings or underlying feelings or attitudes that a sender may convey in the message, like proverbs or idioms being used in the message, etc.

Stage 6: Feedback

After the receiver has decoded and interpreted the messages, its now his turn to send a response to re assure the sender that the message has been received. The response can be in form of a written word, spoken word or body language. The sender will always wait for a feedback from the sender, otherwise the cycle would be incomplete without this feedback.

3.4.2 Essentials of Effective Communication in Business

Effective communication takes place when the message is perceived by the receiver in the same way the sender intended and is received on time. This is important for the existence of the business as it keeps the organisation running smoothly and successfully. For communication to be effective, it should possess the following 7C's of effective communication and other factors.

- **Complete:** The message should include all facts the receiver needs to know about the subject matter which is being communicated to him or her.
- **Concise:** The sender should give the message in the fewest words possible not be too wordy so as not to confuse the receiver.

- Courteous: The sender should be sincere when giving the information and avoid hurting the receiver, however, he/she should not depart or shy away from addressing the issues under concern.
- Correctness or accuracy: Information being sent should be as correct or accurate as possible.
- Considerate: The sender should have the receiver in mind when sending a message. It is better to use positive words rather than negative words or sentences.
- Concrete: The message should be concrete, not vague or too general.
- Clear: The message should be as clear as possible, i.e. the sender should choose words and language that is familiar to the receiver.
- Timing: The message should be conveyed or communicated at a time when the receiver is able to receive it.
- Environment: The environment within which the communication is being made should enable the intended target receive the message.
- Media: The sender must use a medium that the target recipient uses, for instance, when communicating to villages, it is more effective to use a radio and not newspapers.

3.4.3 Use of communication skills

Customer Service Skills

Customers is one of the most important ingredient in any organisation. It is cautioned that when these needs are ignored, customers' loyalty may change drastically. Unsatisfied customers complain, and if the complaints are not well attended to, this may lead to drop in customer patronage and sales. In this era of cut throat competition, customer service skills is needed to keep his business going.

Interpersonal Skills

Interpersonal skills are the skills a person uses to communicate and interact with others. Its referred to as social skills, its described as life skills individuals use to communicate with other people they work with. People who have developed strong interpersonal skills are usually more successful in both their chosen careers and personal lives. In business domain, the term interpersonal refers to an employee's ability to get along with others while getting the job done. It is a set of abilities that enables a person to interact positively and work effectively with others. Its the ability to relate to coworkers, inspiring others to participate and mitigate conflict with and between co-workers. six items used to measure interpersonal skills, though he called them social skills. The six items used to measure these skills among entrepreneurs include; i) ability to induce positive reaction from others (impression management); ii) ability to control own emotion (emotional intelligence ability); iii) ability to screen people's characters, motives & intentions; iv) ability to trust and share freely with workers & customers; v) ability to learn & use new environment (Social adaptability); and vi) ability to interact freely with employees and customers.

3.4.3 .1 ELEMENTS OF INTERPERSONAL SKILLS

Human relation skills,

Leadership skills,

Networking skills,

Team building skills,

Communication skills

Delegation skills.

Most of these elements have been discussed in module 1 of this manual.

Human Relations Skills

Human relations skills pertain to the ability to understand others, work with others, lead, motivate and control behaviour of others. Human relations skills are divided into (a) intra-group skills and (b) intergroup skills. Intra-group skills are essential in lower and middle management roles and intergroup skills are important in higher levels of management. They can be acquired through self-development so that one can (a) recognise the feelings and sentiments brought to a situation; b) have an attitude about own experience which enables a manager to re-evaluate and learn from them; c) develop ability in understanding what others by their actions and words are trying to communicate; and d) develop ability in successfully communicating own ideas and attitudes to others. It is important that entrepreneurs self-examine their own concepts and values, which may enable them to develop more useful attitudes about themselves and about others.

Successful entrepreneurs need to have the managerial skills necessary to evaluate potential employees, hire and train workers and put them in appropriate positions in the organisation. Human relationship skills have to do with the effective management of people at work. They determine what can be or should be done to make workers more productive and satisfied.

Networking skills

Networking refers to developing and using contacts made in business for purposes beyond the reason for the initial contact. For example, a sales representative may ask a customer for names of others who may be interested in his product. Networking is a structured plan to get to know people who will do business with your organisation or introduce the organisation to those who will. The best way to succeed at networking is to plan, be committed to the plan and execute it. Networking is one of the most important skills for entrepreneurs and businesspeople. It involves building and maintaining contacts and relationships

with other people. The personal networks which the entrepreneur accumulates over time, both socially and professionally can be an invaluable resource.

Networking is the use of both formal and informal connections between groups of colleagues to develop a career. Business networking events organised around the world bring together extraordinary groups of highly skilled and talented entrepreneurs, united around the idea of communication, sharing, creating and developing ideas and meeting with potential investors. Many exceptional opportunities can occur if potential investors or business partners are impressed. They need to know when, where and why he is going to an event, what his goals are and what he wants to achieve by his attendance at any meet up. Connections come because of other connections, and the hardest part of the whole network-building process is the start.

Team Building Skill

Team building refers to a range of activities executed to enhance the performance of a team. Team building skills refer to the ability of a manager to inculcate the importance of participation, collaboration, unity and other team building skills in the team members to enhance the performance of the group or organisation. Based on this, team building skills can be said to refer to the ability of a manager to group together suitable individuals to constitute a team or teams for the purpose of achieving a common goal or objective.

4.0 Conclusion

This unit discussed the sources of information, its strategic importance, characteristics and costs. Furthermore, Information must be communicated, hence, the essentials of communication were highlighted.

5.0 Summary

Raw data are basically facts and figures. Information is useful data that can influence someone's choices and behaviour. Information has strategic importance for organizations. Internal information consists of data created for the sole use of the company that produces it, such as personal files, trade secrets etc. External information is whereby documentation is made available to the public from a third party.

6.0 Tutor-Marked Assignment

- a. Discuss the external and internal sources of information and their different types.

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UNIT 14: INFORMATION SYSTEM AND RECORDS MANAGEMENT CONTENT

1.0 Introduction

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3.1.1 Components of Information System

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3.2.1 Concept of Records

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3.2.3 Records Management guidelines for Information Technology System

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3.2.6 Procedures of the Records Retention programme

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1.0 Introduction

In this unit we are going to discuss the concept of Information System and its elements. We will discuss the advantages and procedures of developing records retention programme. We will further highlight how small businesses can use information tools.

2.0 Objectives

At the end of this unit, students will be able to;

- Understand the concept of Information System and its elements
- Design the Records Retention programme
- Explain the procedures of a records retention programme

3.0 Main Content

3.1 Definition and Components of Information System

Almost all programs in business require students to take a course in something called *information systems*. But what exactly does that term mean?

Schneider and Valacich (2010) opined that, Information systems are combinations of hardware, software, and telecommunications networks that people build and use to collect, create, distribute and store useful data, typically in organizational settings. Also Laudon and Laudon (2012) stated that, Information systems are interrelated components working together to collect, process, store, and disseminate information to support decision making, coordination, control, analysis, and visualization in an organization. These definitions focus on two different ways of describing information systems: the *components* and their *roles* in an organization.

3.1.1 Components of Information systems

Information System is made up of five components hardware, software, data, people, and process. The first three, fitting under the technology category, are generally what most students think of when asked to define information systems. Whilst the last two, people and process, are really what separate the idea of information systems from more technical fields, such as computer science. All of these components work together to bring value to an organization.

a. **Technology:** Technology can be thought of as the application of scientific knowledge for practical purposes. From the invention of the wheel to the harnessing of electricity for artificial lighting, technology is a part of our lives in so many ways that we tend to take it for granted. As discussed before, the first three components of information systems – hardware, software, and data – all fall under the category of technology., but we will take a moment here to introduce them so we can get a full understanding of what an information system is.

ii. Hardware

Information systems hardware is the part of an information system you can touch – the physical components of the technology. Computers, keyboards, disk drives, iPads, and flash drives are all examples of information systems hardware.

iii. Software

Software is a set of instructions that tells the hardware what to do. Software is not tangible – it cannot be touched. When programmers create software programs, what they are really doing is simply typing out lists of instructions that tell the hardware what to do. There are several categories of software, with the two main categories being operating system software, which makes the hardware usable, and application software, which does something useful. Examples of operating systems include Microsoft Windows on a personal computer and Google's Android on a mobile phone. Examples of application software are Microsoft Excel and Angry Birds.

iv. Data

The third component is data. You can think of data as a collection of facts. For example, your street address, the city you live in, and your phone number are all pieces of data. Like software, data is also intangible. By themselves, pieces of data are not really very useful. But aggregated, indexed, and organized together into a database, data can become a powerful tool for businesses. In fact, all of the definitions presented at the beginning of this chapter focused on how information systems manage data. Organizations collect all kinds of data and use it to make decisions. These decisions can then be analysed as to their effectiveness and the organization can be improved.

3.2 Records retention programme or Records management

Records retention programme also known as **records and information management programme**, is an organizational function devoted to the management of information in an organization throughout its **life cycle**, from the time of creation or inscription to its eventual disposition. This includes identifying, classifying, storing, securing, retrieving, tracking and destroying or permanently preserving records. A records retention program consists of a method for determining retention periods, a records retention schedule and retention policies and procedures.

An organization's records preserve aspects of institutional memory. In determining how long to retain records, their capacity for re-use is important. Many are kept as evidence of activities, transactions, and decisions. Others document what happened and why. The purpose of records management is part of an organization's broader function of Governance, risk management, and compliance and is primarily concerned with managing the evidence of an organization's activities as well as the reduction or mitigation of risk associated with it.

3.2.1 Concepts of Record

Record is the concepts and principles from which approaches to the creation, capture and management of records are developed. While there are many purposes of and benefits to records management, as both these definitions highlight, a key feature of records is their ability to serve as evidence of an event. Proper records management can help preserve this feature of records.

Recent and comprehensive studies have defined records as "persistent representations of activities" as recorded or created by participants or observers. In organizational contexts, records are materials created or received by an organization in the transaction of business, or in pursuit of or in compliance with

legal obligations. This organizational definition of record stems from the early theorization of archives as organic aggregations of records, which is "the written documents, drawings and printed matter, officially received or produced by an administrative body or one of its officials."

3.2.2 Records management practices.

A Records Manager is someone who is responsible for records management in an organization. This part of ISO 15489 (2016) describes concepts and principles relating to the following:

- a) Records, metadata for records and records systems;
- b) Policies, assigned responsibilities, monitoring and training supporting the effective management of records;
- c) Recurrent analysis of business context and the identification of records requirements;
- d) Records controls;
- e) Processes for creating, capturing and managing records.

Thus, the practice of records management may involve:

- planning the information needs of an organization
- identifying information requiring capture
- creating, approving, and enforcing policies and practices regarding records, including their organization and disposal
- developing a records storage plan, which includes the short and long-term housing of physical records and digital information
- identifying, classifying, and storing records
- Coordinating access to records internally and outside of the organization, balancing the requirements of business confidentiality, data privacy, and public access.

- identification and maintenance of records per a specified retention period
- Executing a retention policy on the disposal of records which are no longer required for operational reasons; according to organizational policies, statutory requirements, and other regulations this may involve either their destruction or permanent preservation in an archive.

Records-management principles and automated records-management systems aid in the capture, classification, and ongoing management of records throughout their lifecycle. Such a system may be paper-based (such as index cards as used in a library), or may involve a computer system, such as an electronic records-management application.

3.2.3 Records Management Guidelines for Information Technology Systems

For information technology systems, there are two general categories of records: those records that are associated with the actual creation, maintenance and retirement of the information technology system itself and those records that comprise the data content of the system. Each of these sets of records must be managed in concert with the other. The records management requirements for the data content of the system are the same as if the records were kept in a non-electronic medium with the additional requirement that technologies must be maintained to enable the records to be accessible, accurate, authentic, reliable, legible, and readable throughout the life of the data record. Records required for the creation and maintenance of the information technology system itself include implementation project documents such as procurement proposals and system support documentation. The records management requirements and retention schedules will likely vary between these two categories of records.

3.2.4 Records management requirements

Functional requirements are grouped according to the clusters in the highlevel model:

- a. Create-** Capture, Identification, Classification
- b. Maintain;** Controls and Security; Hybrid records; Retention, migration and disposal; Long-term preservation
- c. Disseminate;** Search, retrieve and render
- d. Administer;** Administrative functions

3.2.5 Retention schedules: A retention schedule is a document listing all the titles of the records series, length of time each document or record will be retained as an active record, the reason for its retention (administrative, legal, fiscal, and historical) and disposition agreed by the user, receiver, and Records Director and Records Retention committee. A clearly defined plan for a record retention and disposal is a vital component of a records program.

3.2.5.1 The Scheduling Process

A retention schedule is a policy document that is created by the Records Director and the department the record is used by (owner). It is reviewed typically once a year to verify that the current retention decisions should remain in effect. The following is the information is on the retention schedule:

- Record series names
- Series description
- Retention period (based on material date)
- Disposition methods
- Approval dates for each series

Once the Department Head, Liaison, and the Records Director have reached agreement on the retention schedule for all stored material, the retention schedule is verified and signed by both parties.

3.2.5.2 Records Retention Committee

The purpose for the Records Retention Committee is to provide guidance for the Records Director for establishing and operating a retention and disposition program as a component for records management program covering:

- Periods of time for records to be maintained
- Appropriate methods for disposition of records
- Measures to be taken when a record disposition must be suspended due to litigation or audit

3.2.6 Procedures in developing records retention programme

a. Establish a records management team to develop and implement a strategic plan for the program and to provide a governance structure.

- An integrated records management steering committee consisting of an executive program sponsor (senior vice president or chief executive officer who reports to the board) and key stakeholders from records management, legal, information technology, compliance and other key business groups, will meet regularly to provide program governance, strategic guidance and support.
- The records management staff has responsibility for developing, implementing and maintaining the program.
- A network of records coordinators will serve as the liaisons between the records management staff and the departments in your organization.
- Obtain senior management support for the establishment and continual management of a records management program.
- Determine what services will be done —in-house and what services will be done by outside vendors and consultants.

b. Conduct an organization-wide inventory of the records in your office.

- The records inventory identifies what information your organization has to manage, including physical and electronic, and is essential to a good records and information management program. The inventory is the groundwork for

which you will develop your program's records retention schedule in step four below. The inventory will help you identify which materials your organization considers:

- Records (recorded information created or received by your organization in pursuance of legal obligations or in the transaction of business and has value requiring its retention)
- Non-records (reference materials, personal papers, junk mail, publications, convenience file, duplicate copies)
- Vital records (records which would be needed immediately after an emergency to continue the organisation's operation)
- Archival records (historical records of enduring value that are preserved and stored in your organisation's archives)
- Once you have identified all the departments in your organization and begin to get a feel for the scope of records to be inventoried, you will need to consider whether you have the resources to conduct the project or if you should hire a consultant to conduct the inventory.
- You can conduct the inventory via physical inventory, surveys, interviews or a combination of these methods. It is important to interview record coordinators from each department to identify and review document repositories and any systems used to create information and process transactions. Department document repositories could include network file shares, SharePoint, employee computers and file cabinets. While conducting department interviews, you should also check for closets and any unoccupied offices that may be holding stored records.
- The inventory should include whether records exist in more than one format, media, software and physical location of records.
- Review organizational repositories checking for records that are stored in:
 - Email and other messaging or collaboration servers

- Enterprise-wide SharePoint deployments
- Enterprise content management systems
- Electronic records management systems
- Back-up servers
- On-site centralized records centres
- Off-site storage areas for physical and/or electronic records
- Once a draft list of documents for each department is prepared, it should be reviewed with the department to make sure no records were overlooked.
- While conducting the inventory, create a log of all repositories in your organization. This will assist in the event of discovery. Your legal counsel will be aware of all responsive systems and repositories.

c. Establish your organization's records management policies and procedures.

- The records management policy serves as the basis for the entire program, is your program's primary governance instrument and provides employees guidance. The policy should be endorsed at the highest decision-making level, publicized throughout your organization and made readily available to all staff.
- Developing your records management policy will be dependent on your organisation's culture. Your policy should include:
 - Defining records management responsibilities assigned to employees of your organization to include the executive sponsor, steering committee, records management and information technology staff, business unit managers, system administrators, record coordinators and general users.
 - Definition of a —record whether records will be kept in a centralized area, decentralized within work areas or a combination of both.

- Records retention and disposition procedures to include: how draft documents and working papers will be handled, who will be responsible for maintaining the official record copy and litigation hold procedures.
- The records management procedures should describe in detail how to comply with the requirements outlined in the records policy and other instruments. It provides records management processes for the records staff, recordkeeping processes for the records coordinators and end users and, when applicable, specific procedures for business units.

d. Develop a records retention program.

- A records retention program consists of a method for determining retention periods, a records retention schedule and retention policies and procedures. This ensures your organisation's records are kept as long as required to meet regulatory, legal and business requirements; that records are not destroyed too early or retained too long; and that your organization follows systematic retention and defensible records destruction practices.
- The retention schedule provides your organisation's functional groups retention and disposition instructions for related records based on regulatory, legal and business requirements. Establishing a retention schedule is the single most important thing you can do to guarantee the success of your organisation's overall records management program. A retention schedule is the foundation of a records management program and applies to records in any format, i.e., paper, electronic (disk, CD, database, email, etc.). All other components of a records management program rely on the records retention schedule that facilitates your organisation's legal compliance, efficiency and risk management.
- The retention schedule should be tailored to your organisation's needs ensuring all records essential to your organization are retained only as long

as needed based on documented research of legal, fiscal, administrative and historical requirements. Retaining records longer may increase organizational liability.

e. Implement a records management training program.

- All staff, contractors and records coordinators need to be trained and know their records management responsibilities. This can be accomplished via a combination of vehicles:
 - Records management intranet site
 - New employee, records coordinator, business unit/department training
 - Handouts
 - Regular all-employee announcements related to records management policies and procedures

3.2.7 Advantages of developing a retention programme

- 1. Protect your company or organization from liability;** If your records become the subject of litigation, an established retention schedule can protect your company. Records which are disposed of following the published retention guidelines would rarely, if ever, be questioned in legal proceedings or third-party review.
- 2. Demonstrate your compliance with legal requirements:** Establishing a retention policy requires each record series to be considered on its own, and a time frame to be created, indicating how long a particular record series should be maintained. A written policy demonstrates that your organization is following established, legal procedures when destroying and retiring documents.
- 3. Improve records management efficiency/consistency;** Implementing a corporate-wide retention schedule will require the records manager to identify all of the organization's record series. This process will provide the opportunity to identify and eliminate duplicated documentation and

redundant records. This process will make the records management program more efficient and less costly.

- 4. More efficient use of expensive office space;** A well implemented record retention schedule can identify records which are eligible for destruction as well as records which can be sent to less expensive, offsite storage. The return on investment from destroying unneeded records and transferring semi-active and inactive records to offsite storage can produce immediate and significant cost savings.

Implementation of a comprehensive record retention schedule will reduce costs, improve efficiency, and may assist in avoiding legal liability. With a reduced volume of records, identifying and retrieving important documents will be easier when they are needed. Be sure to have your legal counsel or corporate attorney review the schedule before it becomes official policy within your organization.

4.0 Conclusion

In this unit, the concept of Information System and its elements was treated. We also discussed the advantages and procedures of developing records retention programme. We also further highlighted how small businesses can use information tools.

5.0 Summary

For information technology systems, there are two general categories of records: those records that are associated with the actual creation, maintenance and retirement of the information technology system itself and those records that comprise the data content of the system. Each of these sets of records must be managed in concert with the other. The records management requirements for the data content of the system are the same as if the records were kept in a non-

electronic medium with the additional requirement that technologies must be maintained that enable the records to be accessible, accurate, authentic, reliable, legible, and readable throughout the life of the data record. Records required for the creation and maintenance of the information technology system itself include implementation project documents such as procurement proposals and system support documentation. The records management requirements and retention schedules will likely vary between these two categories of records.

6.0 Tutor-marked assignment

- a) State the advantages of developing a retention programme
- b) Procedures in developing records retention programme

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UNIT 14: BUDGETING AND RATIO ANALYSIS

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1.0 INTRODUCTION

This unit is focused on budgeting and financial ratio. Budgeting is a subset of the planning and control functions of management. Budget is the master plan which explains in detail or the x-ray of financial requirements, the policies behind the requirements and the methods for financing the proposed expenditures .The purpose of every organisation is to make profit, thus, the relevance of financial ratio analysis is also expatiated, the nature of financial ratios, the sources of data analysed, its purposes and types.

2.0 OBJECTIVES

At the end of this unit, you will be able to:

- define budget and budgetary control
- explain the purpose of budgeting
- types of budgetary system
- discuss financial ratio and types

3.0 MAIN CONTENT

3.1 Budgeting and budgetary Control

It is a detailed plan, expressed in quantitative terms, specifying how resource will be acquired and used during a specified period of time. It is a financial proposal which could be for a short or long-term plan. It is a systematic approach for achieving management performance. It is an integral part of management. It is noteworthy to mention that a budget is more than a financial instrument, for it relates to quantities of product and to operations, and consequently serves as a complete programme of business activities in the period to which it relates. It is the plan of the business expectations in the future usually for twelve months. It should be noted that an overall organization budget for one fiscal year with each department in the organization submitting her inputs to aid a comprehensive budget, Besides, the

department later breakdown into weekly or monthly their budgets depending on the nature and size of business.

According to the Institute of Chartered Marketing Association (ICMA), England, a "budget is a financial and quantitative statement, prepared and approved prior to a defined period of time of the policy to be pursued during a given period, for the purpose of attaining a given objective. e.g. profit or sales volume". The budget provides a guidepost to point the way, and the actual steering of the vehicle is in the hands of the driver-manager.

Planning involves the control and manipulation of relevant variables, and reduces the impact of uncertainty and risk.

A budget should not be rigid and difficult to understand. It should be capable of differentiating between fixed costs or revenues, explaining schedules, showing expected revenue and expenses at given levels of activities. Planning should not only be done for revenue and expenses, but must include planning for assets and the sources and uses of funds. The sources and uses of funds statements shows the new wealth that has become available to a business in the year and how it has been invested in the organization. They can be constructed to highlight changes in the firm's cash position, as they tend to emphasize different aspects of management of finance.

The success of a budget depends greatly on the control instruments or mechanisms put in place, hence, the need for budgetary control.

Budgetary control

Budgetary control is a system which uses budget as a means of planning and controlling, It is the establishment of budgets relating to the responsibilities of executive to the required policy and the continuing comparison of actual with the budgeted results, either to secure by individual or collective action of the objective of that policy, or to provide basis for revision.

The realization of an organisation's goals in terms of comprehensive profit planning and controlling or budgeting is a systematic and formalized approach for stating and communicating the firm's expectations and accomplishing the planning, coordination, and control responsibilities of management in such a way as to maximize the use of given resources all rest on effective budgetary control system. It is a management technique.

3.1.1 Purposes of budgeting

The main reasons for budgeting are:

1. To state a firm's expectation categorically to avoid possible confusion and facilitate their attainability. With this, individuals are motivated and performance can be evaluated. A number of both endogenous and exogenous variables affects such expectations, such as, socio-economic factors, political factors, supply and demand conditions, competitive environment, technological dynamism etc.
2. It is used to reduce inherent risks and uncertainty that characterizes every business and to ensure proper direction of individual and group efforts to achieve goals. This is the impact of planning.
3. To provide a parameter to measure and control the performance of individuals and units in the organisation and recommend corrective steps that will guarantee the achievement of the organisation's goal. It serves as a feed-back mechanism.
4. To provide a means to effectively communicate organisational expectation to all parties involved in managing the business. A clear and written communication of objectives through budgets will help employees to understand, support and accomplish goals.
5. To help employees in coordinating resources and projects. This entails the harmonization of the activities of all departments for the realization of the organisation's common goal.

6. A budget expresses the plan in formal terms and helps to realize the firm's expectations. A budget is thus, a mechanism to plan for the organization 's overall operations. The most important aspects of every operation are: revenues and expenses. It is a tool by which management plans can be realized in term of revenue and expenditure.

3.1.2 Types of Budgetary System

The size of an average business organization determines the type of budgetary system to be adopted. Most businesses are too large to permit the detailed planning of the total business in a single budget. It is thus necessary to use a master budget that encompasses all the plans and shows how they affect the business as a whole. With this details being left for various specialized budgets. The following are the major types or classifications of budgets:

i. Sales Budget

It forms the fundamental basis on which all other budgets are based. In most organizations, it is the starting point of the budgeting plan; therefore, it is the level of sales that determine the budgeting plan in the organization. As sales are the primary source of cash receipts, such sales estimates is the foundation of financial planning. It can be asserted that a budget is a forecast of sales to be achieved in a budget period, as production cost is based on all activities, most of which again depends on predicted sales level. The sales prediction is the foundation for the qualification of the entire business plan.

In preparing sales budget, the following must be taken into consideration:

- i yearly break-down;
- ii. product break-down
- iii. territory break-own
- v. sales-man estimate

- vi. plant capacity
- vii. pricing policy and strategy
- viii. government control
- ix. competition
- x. political situation.

Table 2

Ajons & Co. Ltd. Sales Budget				
Area and products	Months			
	May	June	July	Total
	N	N	N	N
Sales Area A				
Product X	900	1,050	1,200	3,150
Product Y	<u>15.750</u>	<u>16.800</u>	<u>17.850</u>	<u>50.400</u>
Total	<u>16.650</u>	<u>17.850</u>	<u>19.050</u>	<u>53.550</u>
Sales Area B				
Product X	1,800	2,100	2,400	6,300
Product Y	<u>9.450</u>	<u>10.080</u>	<u>10.710</u>	<u>30.240</u>
Total	<u>11,250</u>	<u>12.180</u>	<u>13.110</u>	<u>36.540</u>
Sales Area C				
Product X	6,300	7,350	8,400	22,050
Product Y	<u>6.300</u>	<u>6.720</u>	<u>7.140</u>	<u>20.160</u>
Total	<u>12.600</u>	<u>14.070</u>	<u>15.540</u>	<u>42.210</u>
Total of all assets	<u>40.500</u>	<u>45.100</u>	<u>47.700</u>	<u>33.300</u>

Limitations

1. Plant capacity may not be enough
2. Non-availability of required personnel
3. Non-availability of the needed raw materials
4. Inadequate capital
5. Since sales is mostly on credit the cash position is a determinant factor.

ii. Cash Budget

It represents the cash requirements of the business during a budget period. It is an attempt to compare the estimated cash receipt and cash disbursement of the

company over the budget period and designed to show the periodical cash balancing position. Cash balance must be kept at optimum level, that is, too little cash can lead to illiquidity or insolvency, whereas, too much cash tends to affect profitability negatively. It is a special type of budget which reveals the happenings or the likelihood of how other sub-budgets succeed in view of the levels of cash in the organization. Hence, it relates to other budgets because all other plans have to be tested and reviewed in relation to how they affect the cash position.

Table 3

Ajons & Co. Ltd. Sales Budget			
	Months		
	May	June	July
	N	N	N
Beginning cash balance Add.	12,000	13,080	13,944
Cash Collections:			
50% of sales	20,250	22,050	23,850
Collection from debtors	<u>15,000</u>	<u>20,250</u>	<u>22,050</u>
Total Cash receipts	<u>47,250</u>	<u>55,380</u>	<u>59,844</u>
Less: Cash disbursements			
Raw materials purchases	12,300	13,050	13,770
Salaries	1,500	1,500	1,500
Wages	20,340	22,140	23,940
Sales commission	2,025	2,205	2,385
Rent	600	600	600
Miscellaneous	405	441	477
Purchase of equipment	-	1,500	-
Dividends	3,000	-	-
Total Cash disbursement	<u>40,170</u>	<u>41,436</u>	<u>42,672</u>
Cash surplus or deficit	7,080	13,944	17,172
Minimum Cash balance (ending) Borrowing (repayment)	<u>12,000</u>	<u>12,000</u>	<u>12,000</u>
Interest	6,000		(3,000)
Cash balance ending	-	-	(45)
	<u>13,080</u>	<u>13,944</u>	<u>14,127</u>

Advantages

- It ensures sufficient cash position
- It reveals shortage or surplus and suggests necessary actions to be taken.

- c. It shows whether or not required expenditure could be internally financed or not
- d. It shows the availability of cash, so that the advantages of cash discount may be exploited.

iii. Production Budget

The sales estimate shows the volume of each line of product which is expected to be required, periodically. The production budget is aimed at assuring that finished goods meet the demands of the sales management. The budget determines the quantity of such goods on hand which must be maintained at the proper size in relation to sales. If the stock on hand is too large, a financial loss may result due to deterioration, changes in style, spoilage, cost of storage, maintenance expenses etc. If the stock becomes too small, there is the fear of losing sales and customers due to non-availability or inadequate supply of goods. The production budget is prepared after the sales budget as it is based on sales forecast. A meaningful production budget requires the need to combine the sales forecasts for each product with information about the beginning level and the expected level of ending inventories of the finished products. Budgeted production unit is calculated thus:

Sales estimate + expected ending inventory - Beginning inventory.

Table 4

Ajons & Co. Ltd. Sales Budget			
	Months		
	May	June	July
	N	N	N

Estimated sales of X	900	1,050	1,200
+ Desired ending inventory	<u>840</u>	<u>960</u>	<u>1,080</u>
	1,740	2,010	2,280
- Beginning inventory	720	840	960
Units of X to be produced	<u>1,020</u>	<u>1,170</u>	<u>1,320</u>
Estimated sales of Y	2,250	2,400	2,550
+ Desired ending inventory	<u>1,920</u>	<u>2,040</u>	<u>2,160</u>
	4,170	4,440	4,710
- Beginning inventory	<u>1,800</u>	<u>1,920</u>	<u>2,040</u>
Units of Y to be produced	<u>2,370</u>	<u>2,520</u>	<u>2,674</u>

iv. Raw Material Budget

Having prepared the production budget, the materials usage and the purchasing budget will have to be estimated and constructed. The raw materials are the items from which the product is made. Their costs are direct or prime costs. The direct cost of working capital which these stocks represent and the indirect burden of deterioration, provision of storage space, maintenance and supervision all must be taking into cognizance. These problems must be solved along with when, how much and where to buy. The materials budget is a tool that enables the purchasing department to plan and secure materials timely. The material usage depends upon the level of production and the level of beginning inventory and desired ending inventories. The units of material to be purchased are thus, determined as:

Purchases (units) = Budgeted usage + Desired ending inventory (material) - Beginning inventory (material)

Table 5

Ajons & Co. Ltd. Sales Budget			
	Months		
	May	June	July
	N	N	N

Material needed to produce X (1 unit of X x 2 units of material)	2,040	2,340	2,640
Material needed to produce Y (1 unit of Y x 4 units of materials)	<u>9,480</u>	<u>10,080</u>	<u>10,680</u>
Total production needed	11,520	12,420	13,320
+ Desired ending balance	<u>17,280</u>	<u>18,630</u>	<u>19,980</u>
Total needs	28,800	31,050	33,300
- Beginning balance	<u>15,750</u>	<u>17,280</u>	<u>18,630</u>
Purchases (units)	<u>13,050</u>	<u>13,770</u>	<u>13,770</u>
Cost of purchases (N)	<u>13,050</u>	<u>13,770</u>	<u>13,770</u>

v. Labour Budget

A business organization must have adequate work force who must be available whenever their services are required to aid in achieving the realization of the organization's objectives. The problem with the preparation of labour budget is that sometimes labour may be idle (as there may not be work) yet the organization cannot afford to dismiss them, and their presence requires that management provides services like good working environment - canteens, Wash rooms etc.; in order to keep the workforce irrespective of the volume of work done. The budget helps in the comparison of relative costs of productive and idle-time of labour.

A direct labour schedule is presented below from the data given in the production budget; the direct labour hours required to be produced and the labour hours required per unit of output.

Table 6

Ajons & Co. Ltd.			
Sales Budget			
	Months		
	May	June	July
	N	N	N

Units of X to be produced	1,020	1,170	1,320
Units of Y to be produced	<u>2,370</u>	<u>2,520</u>	<u>2,670</u>
Total Units	<u>3,390</u>	<u>3,690</u>	<u>3,990</u>
Total hours at 1 hr per unit	<u>3,390</u>	<u>3,690</u>	<u>3,990</u>
Total labour cost N6, per unit	<u>20,340</u>	<u>22,140</u>	<u>23,940</u>

v. Physical Property Budget

This is the need to budget for physical properties like building, machinery and equipment that constitute a relatively permanent investment, which though depreciate over time. The proposed programme as based upon the sales estimate may call for the installation of additional equipment.

Anything in form of permanent equipment can be justified only in the light of long term considerations. An increase in demand of permanent nature may justify further installation; but a temporary demand may have to be met by putting out work to sub-contractors during the peak period, or by overtime or double shift working or by the accumulation of stocks in slack period against the time of peak demand.

vii. Fixed Budget

It is a budget designed to remain unchanged regardless of the level of activity actually attained. It is prepared on the basis of standard cost.

However, because of its unrealistic nature, essentially due to changing purchasing power of money, particularly, during inflation, it has suffered the following drawbacks:

- a. it is difficult for management to assess performance at different departmental levels;
- b. it may not conform with actual production level; and
- c. it is often difficult to revise; in case the business condition undergoes basic change.

Fixed budget has limited application and also ineffective as a tool for cost control. Many organizations try to give up the concept as it does not provide for automatic adjustment with changing volume. It is however, advantageous as it ensures judicious and prudent disbursement of limited financial resources. It does not encourage extra-budgetary budgeting. There is financial discipline.

viii. Flexible Budget

It is a budget designed to accommodate changes in the level of activities that is experienced in an organization. It is thus, a more dynamic concept, but its flexibility gives room for easy manipulation and provides for extra-budgetary allocations. It is advantageous in the following ways:

- a) desirable when business (sales) conditions are unpredictable e.g. luxurious goods or new products;
- b) it is necessary for control of operating condition;
- c) it is easily adaptable, elastic and more practical;
- d) it is useful when external factors such as weather variation, exporting activities, new products etc. are common in an economic environment.

Its defects are observed as follows:

- a. it is very costly;
- b. it depends on accuracy of data collected; and
- c. it is incapable of replacing good management.

It can be asserted from the foregoing that every organization has a basket of budgetary systems and uses that which is relevant to it at different times. The budget is a solution to all problems, hence, those who administer it and those that are influenced directly by it must understand and actively support it to ensure it success.

3.1.3 Budget Preparation

The preparation of a comprehensive budget will include: a.

- a. Sales budget
- b. a production budget
- c. a purchasing budget
- d. labour budget
- e. cash budget.

The illustration given below is used to demonstrate what the preparation of budget is like.

Illustration

Ajons and Co. Ltd. is contemplating the preparation of budget for May, June, and July. It sells its two products in three different sales areas. The company's balance sheet for the year just ended is shown in Table 1 below Sales areas A, B and C respectively produce 10 percent, 20 per cent and 70 per cent of product X sales and 50 per cent, 30 per cent, and 20 per cent of product Y sales. The selling price for product X is ₦ 10 and ₦14 for product Y.

Sales are made on 50 per cent cash and 50 per cent credit basis. The credit sales are collected in the following month.

Table 1

Ajons & Co. Ltd		
Balance Sheet, 31st December, 1999		
	₦	₦
Creditors for December purchases		12,300
Dividend payable (due on Jan. Y2K)		3,000
Share Capital		
Total		<u>3,06,510</u>
Cash		2,91,210
Debtors (for December Sales)		
Stock:		12,000
Raw materials (15,750 at N1 each)		15,000
Product X(720 at N8)	15,750	
Product Y (1800 at N10)	5,760	
Plant and Machinery	<u>18,000</u>	
Less: Accumulated depreciation	3,00,000	39,510
Total	<u>60,000</u>	
		<u>2,40,000</u>

		<u>3,06.510</u>
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Finished goods are valued at the cost of direct labour and direct materials. Sales for December 1999 were N30,000. The monthly forecast of sales (units) are:

Units	May	June	July	August
X	900	1,050	1,200	1,350
Y	2,250	2,400	2,550	2,70

The production of products X and Y uses one common material which costs NI per unit. Two units of material are required to produce one unit of product X while product Y requires four units of the same material. Wages are paid at the rate of N6 per hour during which it can produce one unit of X or Y. Ajons & Co. Ltd has a policy of maintaining a basic finished products inventory equal to 80 per cent of next month's sales and a raw material inventory equal to 150 per cent of current month's production needs.

The payments to creditors are made during the month of the following purchase. Salaries and wages are paid during the month they accrue. Sales commission is 5 per cent of sales and is paid during the month earned. An equipment costing ₦1,500 will be purchased in June and the payment will be made in the same month. A minimum cash balance of ₦12,000 at the end of each month is intended to be maintained by Ajons & Co. Ltd. Money can be borrowed or repaid in multiples of ₦3,000. Interest rate on loans is 6 per cent per year. Loans are

initiated on the first day of the month, and repaid on the last day of the month. Interest is paid when the principal is repaid. The following are other estimated monthly expenses:

Salaries	₦1,500	paid as incurred
Rent	₦600	paid as incurred
Depreciation	₦1,800	
Miscellaneous	1% of Sales	paid as incurred.

Note

(The above illustration shall be used as we progress on the types/classifications of budgetary system).

3.2 Definition of Financial Ratios

Financial ratios are mathematical comparisons of financial statement accounts or categories. These relationships between the financial statement accounts help investors, creditors, and internal company management understand how well a business is performing and of areas needing improvement.

Financial ratios are the most common and widespread tools used to analyze a business' financial standing. Ratios are easy to understand and simple to compute. They can also be used to compare different companies in different industries. Since a ratio is simply a mathematical comparison based on proportions that large and small companies can use ratios to compare their financial information. In a sense, financial ratios do not take into consideration the size of a company or the industry. Ratios are just a raw computation of financial position and performance.

Values used in calculating financial ratios are taken from the balance sheet, income statement, statement of cash flows or (sometimes) the statement of changes in equity. These comprise the firm's "accounting statements" or financial statements. The statements' data is based on the accounting method and

accounting standards used by the organization. Financial ratios are categorized according to the financial aspect of the business which the ratio measures.

3.2.1 Types of Financial Ratios

Financial ratios can be broadly classified into liquidity ratios, solvency ratios, profitability ratios and efficiency ratios (also called activity ratios or asset utilization ratios). Other categories include cash flow ratios, market valuation ratios, coverage ratios, etc.

i. Liquidity Ratios

Liquidity ratios assess a business's liquidity, i.e. it is the ability to convert its assets to cash for paying off its debt obligations without any significant difficulty (i.e. delay or loss of value). Liquidity ratios are particularly useful for suppliers, employees, banks, etc. Important liquidity ratios are:

- Current ratio
- Quick ratio (also called acid-test ratio)
- Cash ratio
- Cash conversion cycle

ii. Solvency Ratios

Solvency ratios assess the long-term financial viability of a business i.e. its ability to pay off its long-term obligations such as bank loans, bonds payable, etc. Information about solvency is critical for banks, employees, owners, bond holders, institutional investors, government, etc. Key solvency ratios are:

- Debt ratio
- Debt to equity ratio
- Debt to capital ratio

- Times interest earned ratio
- Fixed charge coverage ratio
- Equity multiplier

iii. Profitability Ratios

Profitability ratios measure the ability of a business to earn profit for its owners. While liquidity ratios and solvency ratios explain the financial position of a business, profitability ratios and efficiency ratios communicate the financial performance of a business. Important profitability ratios include:

- net profit margin
- gross profit margin
- operating profit margin
- return on assets
- return on capital employed
- return on equity
- earnings per share

Other ratios related to profitability that are used by investors to assess the stock market performance of a business include:

- price to earnings (P/E) ratio
- price to book (P/B) ratio
- Dividend payout ratio
- Dividend yield ratio
- Retention ratio

iv. Activity Ratios

Activity ratios assess the efficiency of operations of a business. For example, these ratios attempt to find out how effectively the business is converting

inventories into sales and sales into cash, or how it is utilizing its fixed assets and working capital, etc. Key activity ratios are:

- inventory turnover ratio
- days sales in inventory
- receivables turnover ratio
- days sales outstanding
- payables turnover ratio
- days payable outstanding
- fixed asset turnover ratio
- working capital turnover ratio

v.Cash flow ratios

Cash flow ratios are mainly used to assess the quality of earnings of a business. Since net income information is based on accrual concept, which is subject to significant management judgment, cash flows ratios (also called performance ratios) provide a more unbiased assessment. Example include cash flow per share.

vi.Coverage Ratios

Coverage ratios are supplementary to solvency and liquidity ratios and measure the risk inherent in lending to the business in long-term. They include EBIDTA coverage ratio, debt coverage ratio, interest coverage ratio (also known as times interest earned), fixed charge coverage ratio, etc.

3.2.2 Calculating financial ratios

When trying to decide which ratios to work on, there are some standard ones that most business firms use. The problem with ratios is that they are useless unless

they are compared to something. For example, if you calculate your firm's debt ratio for one-time period (for instance, a year) and it's 50%. What does that really mean? All you can take from that is a debt ratio that shows total liabilities/total assets, and that 50% of your firm's assets are financed by debt. You do not know if that is good or bad unless you have something to compare it with.

i. Trend Analysis

Presumably, you have other years of balance sheet data for your small business. It is very helpful to calculate the financial ratios for several years (or quarters if you have that data) so you can track the trends in your ratio. You can compare your firm's ratios to trend data. To complete this comparison, you want to take data from the past (e.g. same time last year), and compare it to the present to see how your firm is doing over a series of time periods.

ii. Industry Analysis

Just as important as trend analysis is industry analysis. It is very important, particularly in today's economic climate, to know what your industry is doing as compared to your company. For example, if your industry's ratios are much different than your firm's, you want to examine why and perhaps take action.

You can also compare your firm's ratios to industry data. You can gather data from similar firms in the same industry, calculate their financial ratios, and see how your firm is doing in comparison to the industry at large. Ideally, to get a good financial picture of your firm, you should do both.

4.0 CONCLUSION

It is obvious that no business will survive without profit planning which must be based on certain budget or estimation of both income and expenditure to determine whether or not the business opportunity available is worthwhile. The definition of financial ratios, the sources of data used, purpose and types of financial ratios were elaborated. Financial ratios can be broadly classified into liquidity ratios, solvency ratios, profitability ratios and efficiency ratios (also called activity ratios or asset utilization ratios). Other categories include cash flow ratios, market valuation ratios, coverage ratios, etc.

5.0 SUMMARY

Budgeting plans future activities of a business organization and in this unit we were able to define budget, the purpose of budgeting, how to prepare a budget and types of budgetary systems. Financial ratios are mathematical comparisons of financial statement accounts or categories. These relationships between the financial statement accounts help investors, creditors, and internal company management understand how well a business is performing and of areas needing improvement.

6.0 TUTOR MARKED ASSIGNMENT

1. What are the limitations of sales budget?
2. Define budgeting and budgetary control.
3. State 5 merits of budgeting
4. Highlight the differences between Cash flow ratios and Coverage ratios

7.0 REFERENCES/FURTHER READING

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UNIT 16: BREAK-EVEN ANALYSIS AND CHART

CONTENT

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3.1.2 Formula for Break-Even Analysis	
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3.2.1 Construction of a Break-Even Chart	
3.2.2 Types of Break-Even Chart	
3.2.3 Multi-Product of Break-Even Chart	
3.2.4 Advantages and Limitations of Break-Even Chart	
4.0 Conclusion	
5.0 Summary	
6.0 Tutor-marked Assignment	
7.0 References/Further Reading	

1.0 Introduction

In this unit, we are going to discuss the concept of Break-Even analysis and Break-Even Chart will be explored. The construction of this chart, the types, method of preparation, advantages and limitations and lastly the multi-products of the break-even chart.

2.0 Objectives

At the end of this unit, students should be able to;

- Explain the Break-Even analysis concept.
- Understand the of Break-Even chart
- Know the types and construct the Break-Even chart
- Identify the advantages and limitations of the break-even chart

3.0 Main Content

3.1 What is a 'Break-Even Analysis

Break-even analysis entails the calculation and examination of the margin of safety for an entity based on the revenues collected and associated costs.

Analysing different price levels relating to various levels of demand, an entity uses break-even analysis to determine what level of sales are needed to cover total fixed costs. A demand-side analysis would give a seller greater insight regarding selling capabilities.

Break-even analysis is useful in the determination of the level of production or in a targeted desired sales mix at what point the business will become profitable. The analysis is for management's use only as the metric and calculations are often not required to be disclosed to external sources such as investors, regulators or financial institutions. Break-even analysis looks at the level of fixed costs relative to the profit earned by each additional unit produced and sold. In general, a company with lower fixed costs will have a lower break-even point of sale. For example, a company with \$0 of fixed costs will automatically have broken even upon the sale of the first product assuming variable costs do not exceed sales revenue. However, the accumulation of variable costs will limit the leverage of the company as these expenses are incurred for each item sold.

Furthermore, the concept of break-even analysis deals with the contribution margin of a product. The contribution margin is the excess between the selling price of the good and total variable costs. For example, if a product sells for \$100, total fixed costs are \$25 per product and total variable costs are \$60 per product, the product has a contribution margin of the product is \$40 ($\$100 - \60). This \$40 reflects the amount of revenue collected to cover fixed costs and be retained as net profit. Fixed costs are not considered in calculating the contribution margin.

3.1.1. Formulas for Calculating Break-Even Analysis

The calculation of break-even analysis may be performed using two formulas. First, the total fixed costs are divided the unit contribution margin. In the example above, assume total company fixed costs are \$20,000. With a contribution margin of \$40, the break-even point is 500 units (\$20,000 divided by \$40). Upon the sale of 500 units, all fixed costs will be paid for, and the company will report a net profit or loss of \$0.

Alternatively, the break-even point in sales dollars is calculated by dividing total fixed costs by the contribution margin ratio. The contribution margin ratio is the contribution margin per unit divided by the sale price. Using the example above, the contribution margin ratio is 40% (\$40 contribution margin per unit divided by \$100 sale price per unit). Therefore, the break-even point in sales dollars is \$50,000 (\$20,000 total fixed costs divided by 40%). This figured may be confirmed as the break-even in units (500) multiplied by the sale price (\$100) equals \$50,000.

3.2 Meaning of Break-Even Chart

The Break-Even Chart (BEC) is a graphical representation between cost, volume and profits. No doubt, it is an important tool which helps to make profit planning. It has been defined as, **“a chart which shows the profitability or otherwise of an undertaking at various levels of activity and as a result indicates the point at which neither profit nor loss is made.”**

Since it shows the effects of cost and revenue at varying level of sales it has been rightly called Cost-Volume-Profit graph (CVP graph).

BEC depicts the following information:

(a) Cost (i.e. Fixed, Variable and Total);

(b) Sales value and Profit/Loss;

(c) Break-Even Point;

(d) Margin of Safety.

Certain Assumption about the CVP Graph:

(a) Fixed Cost, will remain constant during the relevant period;

(b) Semi-Variable Cost can be bifurcated into variable and fixed components. (c) Variable cost per unit also will not make any change during the relevant period.

(d) Selling price also will not make any change during the relevant period irrespective of the quantity sold.

(e) Operating efficiency also will remain constant.

(f) Product mix will remain unchangeable.

(g) Volume of production and sales are equal.

3.2.1 Construction of a Break-Even Chart:

A Break-Even Chart is constructed on a graph paper. Activity or volume of production is plotted on the X axis whereas, cost and revenue are plotted on the Y axis.

Again, „X“ axis may be represented in the following manner, such as:

(i) Volume in units;

(ii) Sales value;

(iii) Standard Hours; and

(iv) Percentage level of activity.

The following illustration will help to understand the whole principal:

Units	Fixed Costs	Variable Cost	Total Cost	Sales
	Rs.	Rs.	Rs.	Rs.
—	40,000	—	40,000	—
1,250	40,000	5,000	45,000	25,000
3,750	40,000	15,000	55,000	75,000
5,000	40,000	20,000	60,000	1,00,000

Source; Jeswani (2017)

(a) Draw fixed Cost of Rs 40,000-line parallel to $_X'$ axis. Then plot the variable cost line over fixed cost level at various level of activity and join the variable cost line with fixed cost line at zero level of activity which will indicate total cost line — variable cost being over fixed cost line.

(b) At the same time, ascertain sales value at various activity level and plot them on the graph paper and then to zero which line indicates the volume of sales.

(c) It is interesting to note that where the sales line intersects the total cost line, that is known as Break-Even point. Needless to mention here that BEP will be ascertained by drawing a perpendicular to $_X'$ axis from the point of intersection which measures the horizontal distance from the zero point from where the perpendicular is drawn.

Similarly, in order to find out BES value, another perpendicular to the $_Y'$ axis from the point of intersection is drawn.

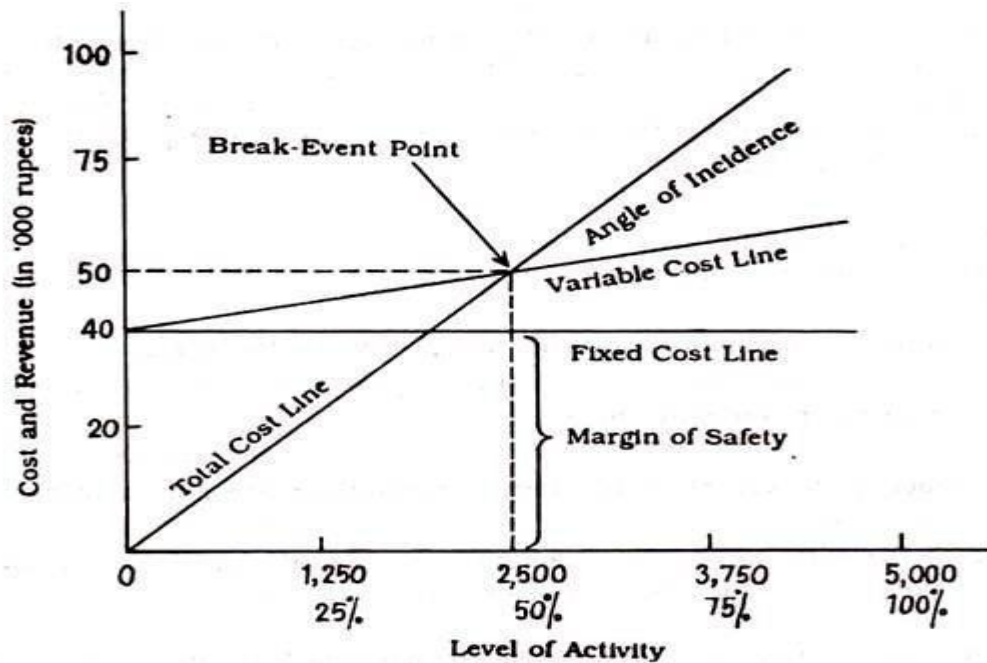


Fig 4.2 Break-Even Chart.

Source; Jeswani (2017) Comments:

From the above BEC, it becomes clear that profit/loss at different levels of activity can be understood from this chart. For example, if we find the sales line is above the total cost line, there will be profit and vice-versa. Similarly, if total cost is equal to total sales, there is no profit or no loss i.e., break-even point. In Fig. 4.2 diagram, 50% level of activity brings break-even level.

3.2.2 Types of Break-Even Chart:

The BECs we have discussed so far are the common type. There are certain types of Break-Even Charts which are yet to be discussed and which are used for various purposes.

Some of them are discussed here under:

- (a) Detailed Break-Even Chart
- (b) Control Break-Even Chart
- (c) Cash Break-Even Chart
- (d) Break-Even Chart to ascertain the optimum volume.

(a) Detailed Break-Even Chart: Under this type of BEC, the total variable costs, i.e. direct materials, direct labour, variable overhead are represented in this graph together with the appropriation items, like dividend on equity shares, dividend on preference shares, income-tax and retentions are plotted. In this respect it may be mentioned that if this chart contains only the details of appropriation of profit it may be called profit-appropriations BEC.

The following illustration with help to understand the principle:

Illustration:

From the following particulars, draw up a detailed BEC:

Total Fixed Cost	Rs. 10,000
Dividend	Rs. 4,000
Income-Tax	@ 40% of profit
Maximum Sales	8,000 unit @ Rs. 20
<u>Cost Structure</u>	<u>Rs. (per unit)</u>
Direct Material .	4
Direct Labour	2
Variable : Factory Overhead	2
Selling Distribution	2
TC	<u>10</u>

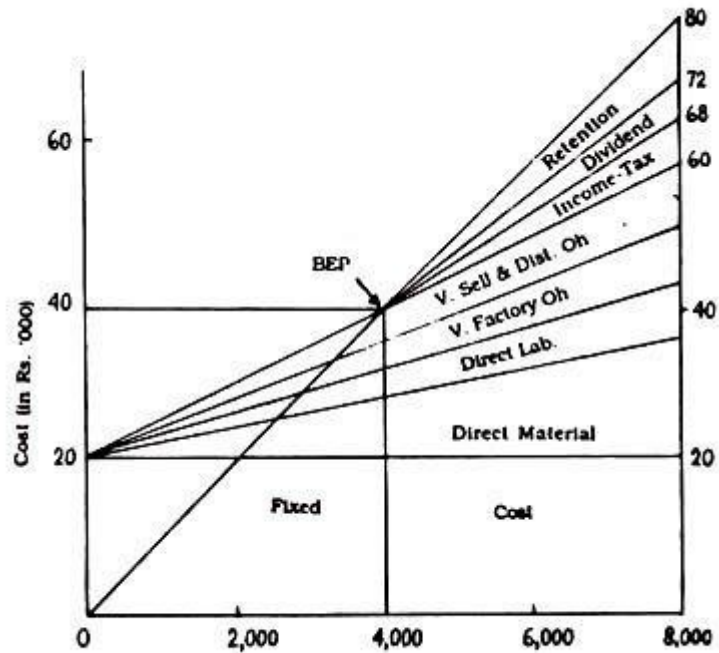


Fig. 4.7. Detailed Break-Even Chart

Source: Jeswani (2017)

(b) Control Break-Even Chart:

Control Break-Even Chart is prepared in order to make a comparison between budgeted/standard and actual cost, sales and profits, particularly when the Budgetary Control Systems and Marginal Costing system are combined, after analysing the deviations between budgeted/standard and actual figures.

Control Break-Even Chart proves itself a very useful method which directly helps the management in taking decisions. It is to be remembered that the detailed information about deviations between budgeted figures and actual figures is not possible graphically.

(c) Cash Break-Even Chart:

Before preparing a Cash Break-Even Chart we are to divide the amount of fixed cost into two following groups:

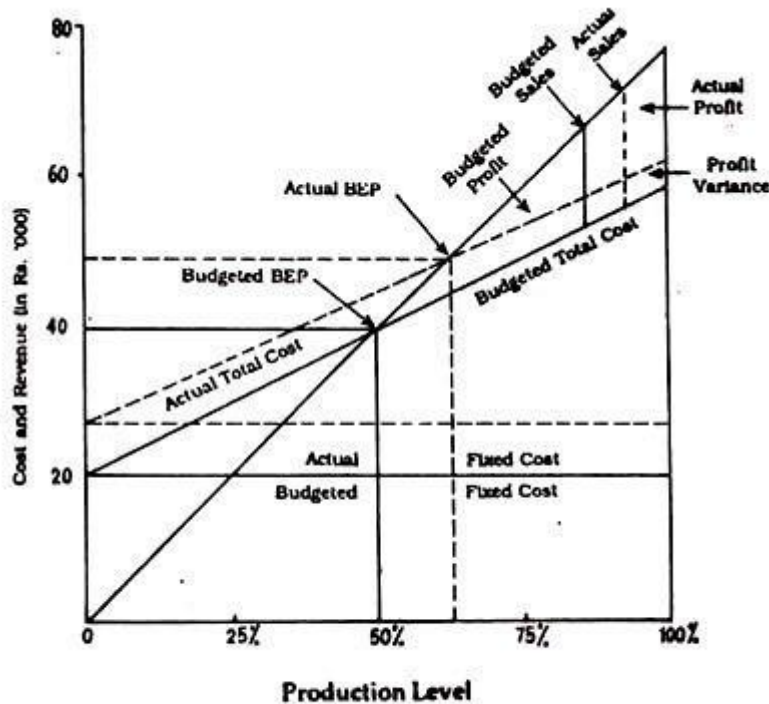


Fig. 4.8 Control Break-Even Chart.

Source; Jeswani (2017)

- (i) Fixed Cost which require cost outlay (like, Rent, Salary etc.);
- (ii) Fixed Cost which do not require immediate cost (like, deferred expenditure, Depreciation etc.).

In this chart, item

- (i) Is treated as base like ordinary BEP whereas item
 - (ii) Is shown last i.e., after variable cost, so that a comparison can be made easily.
- Similarly variable costs which need immediate payment, are plotted as usual. But care should be taken if any credit transaction is included in the variable cost.

If that be so the ' same is to be treated as no. (ii) stated above. This Chart is very useful to those firms which suffer from short-term liquidity and solvency position as well. It is primarily used in cash flow analysis.

Illustration:

From the following information prepare a Cash-Break-Even Chart:

	Rs.
Fixed Cost :	
For immediate Cash Payment	10,000
Non-Cash item (Depreciation)	6,000
Variable Cost	10 per unit
Sales 4,000 units	@ 20 per unit
Tax @ 50%	
Pref. Dividend	Rs. 4,000

Solution:

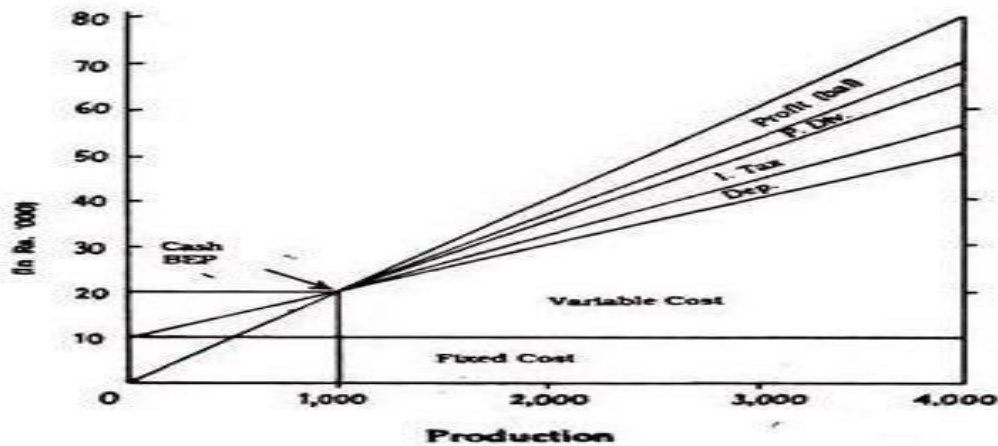


Fig. 4.9 Cash Break-Even Chart.

Source; Jeswani (2017)

(d) BEC to ascertain the Optimum Volume:

This is particularly useful where the demand for a product is elastic. Because in case of perfect competition selling price of a product is to be reduced in order to earn more profit by increasing the volume of sales which ultimately gives a highest contribution. Now, the problem arises before us is that at what stage the amount of profit will be maximised since the volume of sales are fluctuating. This can be solved with the help of a BEC which is shown below. In this regard, it may be said that if amount of sales and costs at different stages are plotted on a graph paper, it becomes possible for us to know at which point the profit will be maximized. Needless to mention that, point will be the optimum level and that selling price of the products will be the optimum selling price of the products of the firm. All this information can be had with the help of a BEC which is presented below: **Illustration:**

X Ltd. gives you the following particulars for which you are requested to ascertain the volume of sales and selling price at which the company can maximise profits with the help of a graph.

Expected Sales	Selling price (per unit)
	Rs.
1,000	20
2,000	19
3,000	18
4,000	17
5,000	16
6,000	15
6,500	14

Expected Sales	Selling price (per unit)
	Rs.
7,000	13
7,500	12
8,000	11

Source; Jeswani (2017)

The fixed costs amount to N24,000 and the same is to increase by N 8,000 if the output exceeds 4,000 units.

Solution:

Before preparing the graph the following table is prepared:

Unit	Sales	Fixed Cost	Variable Cost	Total Cost
	Rs.	Rs.	Rs.	Rs.
1,000	20,000	24,000	5,000	29,000
2,000	38,000	24,000	10,000	34,000
3,000	54,000	24,000	15,000	39,000
4,000	68,000	24,000	20,000	44,000
5,000	80,000	32,000	25,000	57,000
6,000	90,000	32,000	30,000	62,000
6,500	91,000	32,000	32,000	64,500
7,000	91,000	32,000	35,000	67,000
7,500	90,000	32,000	37,500	69,500
8,000	88,000	32,000	40,000	72,000

Now taking the above data, we can plot the same on a graph which is depicted as under:

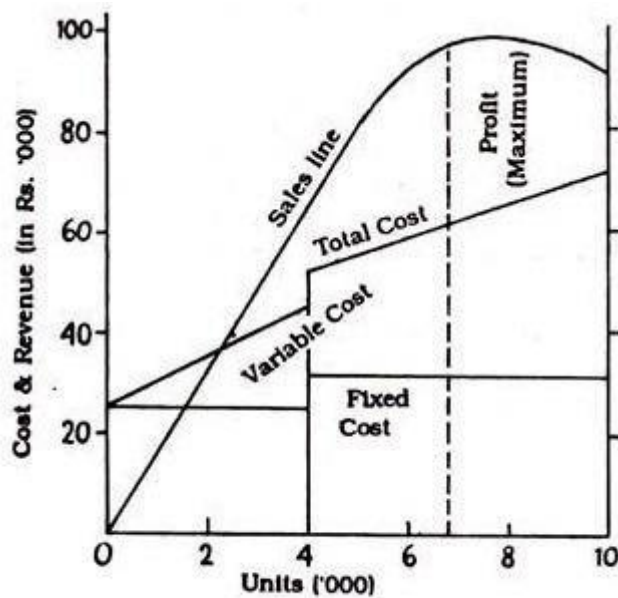


Fig. 4.10. Showing Optimum Volume.

Source; Jeswani (2017)

From the above, it becomes clear that at 6,500 units, the profit can be maximized. In other words, at this level the sales value/line is higher than the total cost line resulting the highest margin. As such, this will be the optimum level of output at the prevailing selling price which will yield the maximum profit.

3.2.3 Multi-Product of Break-Even Chart:

It is quite possible to produce different types of products for a firm and in that case, a Multi-Product Break-Even Chart may be constructed for the firm as a whole. Naturally, in that case, BEP will be that point where the Average contribution line will intersect the fixed cost line assuming that there will be no change in sales-mix.

Method of Construction of Multi- Product Break-Even Chart:

- (a) Complete P/V ratio and arrange the products in descending order according to P/V ratios.
- (b) Y axis represents contribution and fixed cost while X axis represents sales value;

- (c) Then plot the total fixed cost line;
- (d) And then take the product which has highest P/V ratio, plot its contribution against sales and so on;
- (e) Now, get the average contribution line after joining the origin to the end of the last line so plotted.
- (f) The BEP will be that point where average contribution will cut fixed cost line of the products.

Illustration:

X Ltd products three types of products, viz. A, B and C.

Construct a BEC in order to determine their BEP from the following particulars:

	Total Rs.	A Rs.	B Rs.	C Rs.
Sales 50,000	20,000	12,500	17,500	—
Fixed Cost	9,250	—	—	—
Variable Cost	31,500	10,000	7,500	14,000

Solution:

Before constructing the BEC, let us calculate the P/V ratio of each product first. Then according to the importance of P/V ratio, a table showing cumulative sales should also be prepared. At last, complete the graph.

$$P/V \text{ Ratio} = \frac{C}{S}$$

∴ For Products :

$$\begin{aligned}
 A &= \frac{\text{Rs. } 20,000 - \text{Rs. } 10,000}{\text{Rs. } 20,000} = \frac{\text{Rs. } 10,000}{\text{Rs. } 20,000} = \frac{1}{2} \text{ or } 50\% \\
 B &= \frac{\text{Rs. } 12,500 - \text{Rs. } 7,500}{\text{Rs. } 12,500} = \frac{\text{Rs. } 5,000}{\text{Rs. } 12,500} = \frac{2}{5} \text{ or } 40\% \\
 C &= \frac{\text{Rs. } 17,500 - \text{Rs. } 14,000}{\text{Rs. } 17,500} = \frac{\text{Rs. } 3,500}{\text{Rs. } 17,500} = \frac{1}{5} \text{ or } 20\%
 \end{aligned}$$

Now we are to prepare the following table:

Product	P/V Ratio	Sales		Contribution	
		Product wise	Cumulative	Product wise	Cumulative
A	50%	20,000	20,000	10,000	10,000
B	40%	12,500	32,500	5,000	15,000
C	20%	17,500	50,000	3,500	18,500

$$\begin{aligned}
 \therefore \text{BES will be} &= \frac{\text{Fixed Cost}}{\text{Total Contribution}} \times \text{Total Sales} \\
 &= \frac{\text{Rs. 9,250}}{\text{Rs. 18,500}} \times \text{Rs. 50,000} \\
 &= \text{Rs. 25,000}
 \end{aligned}$$

Source; Jeswani (2017)

The same result can also be depicted by the following Multi-Product Break-Even Chart (BEC)

as under:

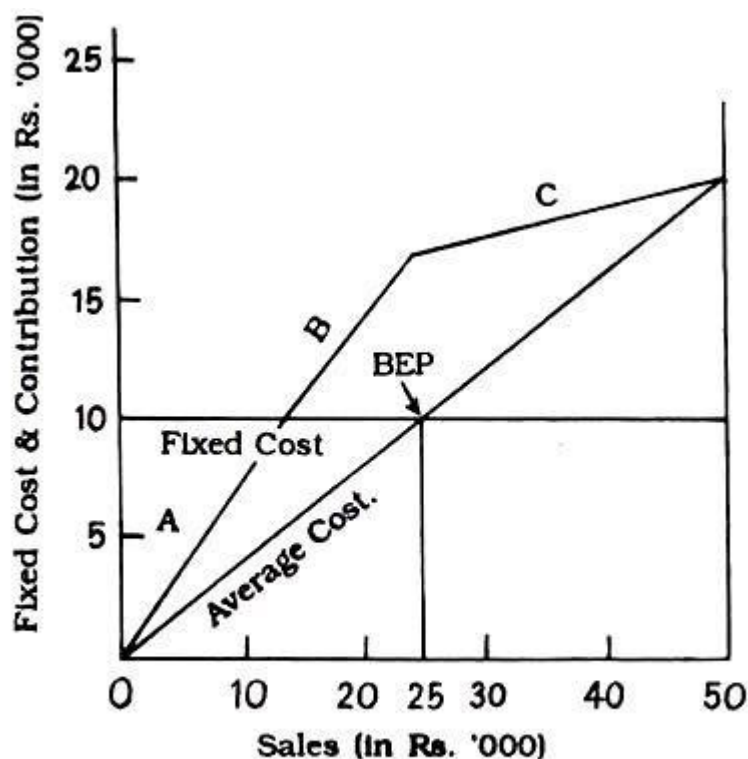


Fig. 4.6 Multi-Product BEC

Source; Jeswani (2017)

3.2.4 Advantages and Limitations of Break-Even Chart:

The following advantages may be offered by a BEC:

(i) Easy to Construct and Easy to Understand:

A Break-Even Chart gives us very clear-cut information which helps the management to take correct decisions as it depicts a detailed picture of the entire undertaking.

(ii) Useful Tool to Help Management:

It has already been pointed out that a BEC gives us the relationship between Cost, Volume and Profit. Thus, the same may present the effect of changes in cost and selling price due to the change in variable cost and fixed cost.

(iii) Helps to Select the most Profitable Product Mix:

No doubt a BEC helps us to select the most profitable product mix or sales mix for earning more profits.

(iv) Helps to Ascertain the Strength of the Business:

This chart helps us to determine profit earning capacity after analysing together Angle of incidence and Margin of Safety.

Therefore, the Management obtains some important information relating to:

- (i) Increase the selling price,
- (ii) To reduce the cost;
- (iii) To substitute the less profitable product by more profitable products,
- and (iv) To increase the volume of production

Limitations of Break-Even Chart

The BEC is not free from snags. They are:

(i) Based on Unrealistic Assumptions some of them are:

- (a) Selling price remains constant irrespective of the volume of sales;
- (b) Production and sales are equal (i.e., without considering value of stock);
- (c) Variable cost remains same;

(d) All indirect cost can be segregated into fixed and variable. In actual practice, however, all the above assumptions are not correct **(ii) Ignore the Concept and Effect of Capital Employed:**

BEC ignores the basic accounting elements i.e., capital employed which is very significant for calculating the rate of profitability or earnings, **(iii) Construction of Multiple BEC Chart:**

If different variety of products are produced, separate BEC should be drawn up which creates a problem of fixed overhead allocation.

4.0 Conclusion

The nitty- gritty of the break-even analysis and chart has been explained with practical illustrations to ease the construction. the break-even analysis as assisting in determining the number of units or amount of revenue that will cover the business total costs. While the break-even chart is a graphical display of similar information.

Summary

The concept of Break-Even analysis and the Chart were discussed in details. the construction of this chart, the types, method of preparation, advantages and limitations and lastly the multi-products of the break-even chart.

6.0 Tutor-marked Assignment

X Ltd. gives you the following particulars for which you are requested to ascertain the volume of sales and selling price at which the company can maximise profits with the help of a graph.

Expected Sales	Selling price (per unit)
	Rs.
1,000	20
2,000	19
3,000	18
4,000	17
5,000	16
6,000	15
6,500	14

Expected Sales	Selling price (per unit)
	Rs.
7,000	13
7,500	12
8,000	11

The fixed costs amount to N25,000 and the same is to increase by N9,000 if the output exceeds 5,000 units.

7.0 References/Further Reading

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