COURSE GUIDE

HCM 313
RESTAURANT ENTREPRENEURSHIP

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Published by
National Open University of Nigeria

Printed 2012

ISBN:

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Introduction

Management has been practised since the dawn of human history. It will remain a basic and dominant institution perhaps as long as civilisation itself survives. Management is not only grounded in the nature and needs of modern industrial system but also in the needs of the modern business enterprise to which an industrial system must entrust its productive resources – both human and materials. It expresses the belief in the possibility of controlling man's livelihood through systematic organisation of economic resources. Management expresses the belief that economic change can be made into the most powerful engine for human betterment.

This belief that material can and should be used to advance the human spirit is not the age old human heresy called 'materialism'. In fact, it is incompatible with materialism as the term as always been understood. It is something new and distinctly modern. Resources have always been considered a limit to man's activities, a restriction on his control over his environment – rather than an opportunity and a tool of his control over nature.

Management, which is the organ of society specially charged with making resources productive, that is, with the responsibility for organised economic advancement therefore reflects the basic spirit of the modern age. It is in fact indispensable – and this explains why, once begotten, it grew so fast and with so little opposition.

Conclusively, management, its competence, its integrity and its performance will be decisive to the free world in the decades ahead. At the same time the demands on management will be rising steadily and steeply.

What you will learn in this Course

During this course, you will learn about:

- business management
- establishing a small scale business
- how to start and run small and medium scale business
- the nature of entrepreneurship
- the planning function in the hospitality industry
- restaurant and business plan
- restaurant and feasibility study
- Nigeria enterprises
- credit institutions

- choosing a form of business ownership
- sources of finance
- inventory management and supply of resources
- the start up problem
- total quality management
- quality audit and measurement

Course Aims and Objectives

When all the above aims are considered, we can conclude that the major aim of the course is to expose you to various methods and techniques and programmes of business management.

Working through this Course

For you to complete this course successfully, you are required to read the study units, reference books, and other resources that are related to the unit. Each unit of the course contains Tutor-Marked Assignment.

The Tutor-Marked Assignment (TMA) is to be done immediately and submitted to your course facilitator for assessment.

The medium to be used and the time to submit the TMA will be specified to you later. This course is a two-credit course. As such, you are expected to spend a minimum of two hours every week studying the course. You are expected to complete the entire outline within a period of 18 – 25 weeks.

Course Evaluation

Every unit of this course has an assignment attached to it. You are required to keep an assignment file. After every unit, the assignment should be done. At the end of the course, the evaluation shall be as follows:

Assessment	Marks
Assignment	30%
Examination	70%
Total	100%

Out of all the assignments you will do, each one shall be marked and converted to 30 per cent. At the end, the best 10 shall be selected so as to make up to 30 per cent. The examination at the end of the course shall cover all aspects of the course.

Course Units

In this course titled Restaurant Entrepreneurship, the following units have been designed.

Module 1

Unit 1 Business Management
Unit 2 Establishing a Small Scale Business
Unit 3 How to Start and Run Small and Medium Scale Business
Unit 4 The Nature of Entrepreneurship
Unit 5 The Planning Function in Hospitality Industry

Module 2

Unit 1 Restaurant and Business Plan
Unit 2 Restaurant and Feasibility Study
Unit 3 Nigeria Enterprises
Unit 4 Credit Institutions
Unit 5 Choosing a Form of Business Ownership

Module 3

Unit 1 Sources of Finance
Unit 2 Inventory Management and Supply of Resources
Unit 3 The Start Up Problem
Unit 4 Total Quality Management
Unit 5 Quality Audit and Measurement

These units must be treated sequentially as a logical link exists in the arrangement. Every previous unit lays a foundation for subsequent ones. A maximum period of one week is required for every unit.

Reference Materials and other Sources

As was earlier mentioned, materials relevant to the course include not only the ones below but also others that you can lay your hands on. But for now, the following references are recommended.

May-Ifeoma Nwoye. (1994). *Small Business Enterprise*. University of Benin Social Science Publication new edition.

A. M. Osoba.(ed.) Nigeria Institute of Social and Economic Research, *Towards the Development of Small Scale Industries in Nigeria*. Dalton O. Faluyi, (1986). *Principles and Practice of Hotel and Restaurant Management.*

Lena Karlsson, (1992*)*. *How to Start a Small Business. (A manual for Community Workers assisting persons with disability)*. International Labour Organisation.

Presentation Schedule

Specific dates for particular activities, such as submission of assignment, tutorial schedules and examination dates shall be made available to you on a later date. This will enable you plan your activities in the same line. The methods of submitting your assignment and receiving other course materials shall be agreed upon on a later date. You should endeavour not to fall behind the schedule whenever it is given.

Conclusion

By the time you are through with this course, you will find it useful in managing and planning of businesses.

MODULE 1

UNIT 1 BUSINESS MANAGEMENT

CONTENTS

1.0 INTRODUCTION

Management has been practised since the dawn of human history. It will remain a basic and dominant institution perhaps as long as civilisation itself survives. For management is not only grounded in the nature of the modern industrial system but also in the needs of the modern business enterprise to which an industrial system must entrust its productive resources – both human and material. It expresses the belief in the possibility of controlling man's livelihood through systematic organisation of economic resources. Management expresses the belief that economic change can be made into the most powerful engine for human betterment.

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Conclusively, management, its competence, its integrity and its performance will be decisive to the free world in the decades ahead. At the same time the demands on management will be rising steadily and steeply. (D. O. Faluyi 1986.)

2.0 OBJECTIVES

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

- define the concept of Small and Medium Scale Enterprise (SME)
- identify the fundamentals of Business Management
- distinguish hospitality business from hospitality management

3.0 MAIN CONTENT

3.1 The Concept of Small and Medium Scale Enterprise (SME)

3.1.1 What is Business?

The word 'business' means buying and selling of commodities. In actual sense, business is an all-inclusive term. It embraces all *profit-oriented* economic or commercial activities carried out by an individual or a group of persons as a means of livelihood. It includes trade, industrial operations, professions, employment, and other related areas. (Nwoye, 1994).

Small business or small scale industry; criteria for definition:

Various schools of thought have proffered varied definitions of small scale business using such parameters as:

1. total investment cost
2. size of work force
3. level of turnover
4. operational environment

3.1.2 Definition of small scale industry

Small scale industry is of numerous definitions as exist in the world and they vary from country to country within and between continents. In America for example, the Small Business Administration (SBA) defines it as a business that is independently owned and operated, is not dominant in its field and meets certain specified criteria for SBA – sponsored loan programmes. The latter requirement is on the condition that the annual receipt of the SSEs should not exceed five million dollars in special trade construction or eight million dollars in service industries.

Similarly, in the Far East (mainly China, Hong Kong, Taiwan and South Korea), manufacturing SSEs are classified as establishments whose annual turnover on the average does not exceed three million American dollars and present capital invested is generally below one million America dollars.

In Europe, particularly in the United Kingdom and Western Germany, the annual turnover of the establishments that are classified as small-scale industries does not exceed the maximum in America and the Far East. (NISER, 1987).

Within the context of Nigerian present industrial situation, a small scale industry could be defined as any business with a total capital investment of less than two million naira (2,000,000); with the number of employees not more than 50.

3.1.3 What is Management?

Management is not a mystery, but unfortunately its principles are often made obscure by verbiage. Management is the body of knowledge about managing. Managing is the process of planning and organising both human and material resources so as to secure the optimum achievement of objectives.

Managers are persons assigned to this process. They get things done through other people. With stated objectives to achieve, that is to produce certain goods or services; he directs human activities, with the help of the other resources available, towards those ends. (Faluyi, 1986)

3.1.4 What is Hospitality Business?

To answer this question, Drucker poses a series of additional questions.

1. Who is the customer?
2. What is value to customer?
3. What will hospitality business be?
4. What should hospitality business be?

We have seen how Statler and the Stouffer brothers, in different areas, thought, through the needs of the emerging American middle-class mass market of a market that really constituted a ‘new’ customer. Then they used the developing field of management to serve that market. Each saw that ‘value’ to that market was all the amenities of luxury standardised and produced so that they could be offered at popular prices.

Who are your customers and what is ‘Value’ to them? The patrons of your operation are obviously customers, and their needs and wants must be satisfied. The employer is your customer, and in an important way, especially for junior managers and supervisors. The employees you direct are also your customers. If they were not there, there would be no need for a supervisor. The balancing of the needs of all these ‘Customers’ properly done will involve creative marketing and innovation.

3.1.5 What is Hospitality Management?

When we think of the Hospitality Industry, we usually associate the term with hotels and restaurants. But the term has much broader meaning. Hospitality could mean the reception and entertainment of guests, visitors or strangers with liberality and good will. The word ‘hospitality’ is derived from *hospice*, a medieval ‘house of rest’ for travellers and pilgrims. A *hospice* was also an early form of what we now call a nursing home and the word is clearly related to hospital.

Hospitality, then, includes hotels and restaurants. But it also includes other kinds of institutions that offer shelter or food or both to people away from their homes. These institutions have more than a common historical heritage. They share the management problems of providing food and shelter, problems that include erecting a building, providing heat, light and power, cleaning and maintenance of the premises, preparing and serving food in a way that pleases the guests.

The hospitality professions are among the oldest of the humane professions and they involve making a guest, client, or resident welcome and comfortable.

3.2 A Concept of Management Cycle

The overall job of a manager is to ‘create within the enterprise the environment which will facilitate the accomplishment of its objectives’. In doing this, the manager plans the work of his subordinates and his own activity, selects and trains subordinates by staffing his operations, organises the work, and controls results by measuring performance against plan. These are the traditional functions of the manager.

The foregoing functions of management are not performed sequentially, nor is there any special time sequence involved. Planning is involved in organising, directing, and controlling. Each function affects the others and all are interrelated to form the management process. The general nature by which these processes operate can be described thus:

Planning

1. Setting objectives for the manager's area of activity.
2. Perceiving opportunities, problems and alternatives surrounding the achievement of the objectives.
3. Diagnosis of opportunities, analysis of objectives and selection of a course of action.
4. Designing a programme of action to achieve the objective.

Direction

5. Leadership is the necessary organisational action required to achieve the programme including communication and motivation of subordinates.

Organising

6. Supervision of the action plan through an organisation in which task relationships are defined and understood.

Control

7. Observation and measurement of performance against standards for achieving the plan and correction of performance deviations as and when required.
8. Observing significant trends within and without the manager's activity so that goals and programmes may be modified as necessary.

Feedback

9. Re-cycling of information concerning plans, actions, and progress at different stages of the management process to ensure that proper programming to achieve the objective is being accomplished.

4.0 CONCLUSION

In conclusion, as a manager, you are expected to plan, direct, organise, control and must be able to get feedback for effective management.

5.0 SUMMARY

Managing is the process of planning and organising both human and material resources so as to secure the optimum achievement of objectives.

Hospitality simply put, means reception, show of care, welcoming or entertaining guests, visitors or strangers with liberty and good will.

Management cycle entails planning, organising, directing, control and feedback.

6.0 TUTOR-MARKED ASSIGNMENT

1. Discuss SMEs industry in Nigeria.
2. How can you describe hospitality business in Nigeria?

7.0 REFERENCES/FURTHER READING

A.M.Osoba (Ed.) Nigerian Institute of Social and Economic Research, *Towards the Development of Small-Scale Industries in Nigeria.*

Dalton O. Faluyi, (1986). *Principles and Practice of Hotel and Restaurant Management.*

Lena Karlsson, (1992). *How to Start a Small Business. (A manual for community workers assisting persons with disability).* International Labour Organisation

UNIT 2 ESTABLISHING A SMALL SCALE BUSINESS

CONTENTS

1.0 INTRODUCTION

Many businesses fail or fold up today for several reasons or for some little things we take for granted. When establishing any business as the case may be, a restaurant, there are assessments that need to be done and some factors to consider for a successful establishment. This unit will be giving the basis of what you need to do immediately the thought comes into your mind that you want to be your own boss.

2.0 OBJECTIVES

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

- identify the factors that affect an entrepreneur's decision
- explain the model of contemporary business
- classify influences on entrepreneur's decision.

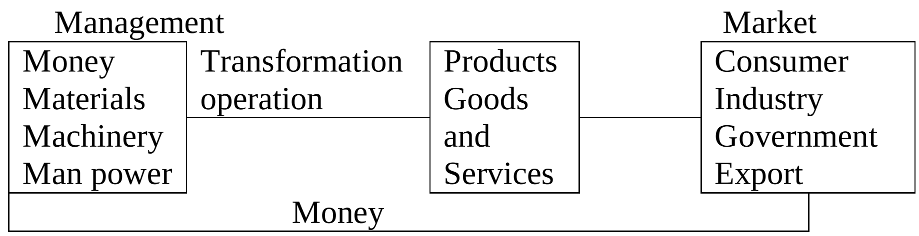
3.0 MAIN CONTENT

SELF ASSESSMENT EXERCISE

Before going into any business at all, one must consider these two basic things.

1. The reason why you are going into the business. Do not go into business because people are doing it.
2. Consider your entrepreneurial ability.

To be a successful business person, your personality as an investor, the product/market, source of finance, and the target customers must be considered.



A Model of Contemporary Business

Entrepreneurial ability must be discussed. That is, the competence as this has a long way to determine the success or failure of a business venture.

3.2 The Entrepreneur

Cooper provides the most comprehensive and useful frame work for explaining the various factors which may contribute to the 'entrepreneur's decision'. He classifies them into three groups.

1. 'The entrepreneur, including the many aspects of his background which affect his motivations, his perceptions, and his skills and knowledge.'
2. 'The organisation for which the entrepreneur had previously been working. Whose characteristics influence the location and the nature of new firms, as well as the likelihood of spin-offs'.
3. 'Various environmental factors external to the individual and his organisation, which make the climate more or less favourable to the starting of a new firm'.

Cooper defines these three groups as Antecedent Influences, the Incubator Organisation, and Environmental Factors.

Antecedent Influences

1. Genetic factors
2. Family influences
3. Educational choices
4. Previous career experiences

Incubator Organisation

1. Geographical location
2. Nature of skills and knowledge acquired
3. Contact with possible fellow founders
4. Motivation to stay with or leave organisation
5. Experience in a 'small business' setting

Environmental factors

1. Economic conditions
2. Accessibility and availability of venture capital
3. Examples of entrepreneurial action
4. Opportunities for interim consulting
5. Availability of personnel and supporting services.
6. Accessibility to customers.

Table 1.influences on entrepreneurial decision

3.2.1 Entrepreneur or Small Businessman

A small business venture is any business that is independently owned and operated, not dominant in its field, and does not engage in any marketing or innovative practices.

An entrepreneurial venture is one that engages in at least one of schumpeter's four categories of behaviour: that is, the principal goals of an entrepreneurial venture are profitability and growth and the business is characterised by innovative strategic practices.

A small business owner is an individual who establishes and manages a business for the principal goals. The business must be the primary source of income and will consume the majority of one's time and resources. The owner perceives the business as an extension of his or her personality, intricately bound with family needs and desires.

An entrepreneur is an individual who establishes and manages a business for the principal purpose of profit and growth. The entrepreneur is characterised principally by innovative behaviour and will employ strategic management practices in the business.

It is clear from the above that the study of entrepreneur is not tidy, and that there are no easy formulas available to help in the task of picking the winners - those entrepreneurs who can, and wish to, start the large firms of the future.

In summary, before going into business as an investor, here is the checklist for going into business:

a. Personality of the potential investor

1. He must be a self-starter with strong self-confidence.
2 He has to have the attributes of a leader and be good at getting along well with others.
3 He must have vision.
4 He must be a good organiser and hard working, willing to put in long hours.
5 He must be able to take timely decisions and take responsibility for the outcome.
6 He must be in good health.
7 He must be able to cope with failure.

Many Nigerians believe that success or failure in business depends on luck, faith or witchcraft. The would-be entrepreneur must believe that successes and set-backs are within his control and he must be ready to deal with them.

b. The Product/Market

1. Look for products whose markets have already been developed, and with high demand
2. Concentrate on products with minimal import duties and foreign exchange content. Emphasise the use of local raw materials
3. A pre-feasibility study is needed in identifying a suitable product.
4 An ideal product would be such that would ensure high turnover at regular intervals

With regards to this, the Federal Government’s Industrial Development Centres exist to offer guidance to potential investors on the most profitable production lines, for small scale operation.

c. Finance

1. How much money will be needed to get the particular business started?
2. How much is the potential investor willing and ready to put into the business?
3. Does the investor know where to borrow or how to get the required capital?
4. Has he discussed with any Banker about his plans?
5. Is he aware of the Federal Government's incentive schemes for small scale industries?

d. Partners/Human Resources

1. These have to be people you can get along with
2. Do not hire employee just because they are relatives

e. Customers

1. Find out if people like to live or visit the areas in which you plan to open the business.
2. Are there similar businesses in the area?

Now that you have seen the true picture of yourself, you can go into setting up of business. Here are the trends to follow:

1. Conception of idea
2. Feasibility study (investigation)
3. If not feasible drop it, if feasible continue to the next step
4. Further investigation if necessary
5. Plan
6. Operation

Feasibility study will give an insight into the potential outcome of the business.

4.0 CONCLUSION

In conclusion we can deduce that going into a new business encompassed various conditions and factors as well as methods through which any potential entrepreneur can be successful. Self assessment is of paramount importance.

5.0 SUMMARY

Factors that affect the decisions of an entrepreneur are classified into three: the background, where the entrepreneur had previously worked and environmental factors. Before going into business, the personality, product/market, finance, customers, human resource must all be considered.

6.0 TUTOR-MARKED ASSIGNMENT

Discuss the basic things to be considered before going into business.

7.0 REFERENCES/FURTHER READING

Lena Karlsson,(1992). *How to Start a Small Business. (A Manual for Community Workers Assisting Persons with Disability).* International Labour Organisation

.UNIT 3 HOW TO START AND RUN SMALL AND MEDIUM SCALE BUSINESS *(RESTAURANT)*

CONTENTS

1.0 INTRODUCTION

The socio-economic imperatives of the Nigeria economy of today are systematically shifting in favour to the growth of small and medium scale business. Among the reasons for this trend is the sudden realisation of the economy.

For a long time government had taken centre stage hoping to carefully and centrally plan the economy. At the core of this approach is the presumption that it is better to centrally manage the scarce resources than manage it in fragments. In so doing, government hopes to redistribute income, reduce unemployment, provide infrastructure and facilitate the growth of Gross National Product (GNP).

Unfortunately, after a period of four decades, they are several miles behind the initial expectations. At the last count, our public corporations have turned out to be a conduit pipe to entrench mediocrity, inefficiency and enrichment of few at the expense of the struggling masses.

Riding on the strength of monopoly coupled with its legal immunity, they have given and continue to give sub-optimal and epileptic services at high rate. In some cases of petroleum products, the products are not even readily available.

It is against this backdrop that successive governments have taken a major rethink to this public sector domination of the economy. Consequently, it has embarked on systematic deregulation of the economy. The first step was to carefully privatise some of the corporation, while other were commercialised. The ultimate goal is to make the sector amenable for others to come and compete. This is what is called liberalisation or deregulation.

The bottom line is that deregulation in its wake will see the shift in emphasis from public to private sector domination of the economy. Expectedly, many small and medium scale businesses will come on stream.

This unit, in anticipation of this scenario, seeks to acquaint entrepreneurs and would-be entrepreneurs with the basic ingredients on how to set up and run small and medium scale businesses.

2.0 OBJECTIVES

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

- explain the concept of small and medium scale enterprise
- identify strategic planning

3.0 MAIN CONTENT

3.1 What is Small and Medium Scale Enterprise (SME)?

The concept of SME has enjoyed some measures of controversy in the attempt at defining it. Consequently, there are as many definitions of SME as there are scholars and institutions defining it. Scholars are to use parameters such as number of employees, sales volume or turnover, capital small, medium and/or big scale.

At one point some people, rightly contended that these parameters do not provide uniform benchmark for all industries and for all time. For instance, what could pass for a big capital in food and beverage industry will certainly be small when compared to that in steel or aviation industry. Further, what is a big capital today may become small in five years to come. (Ezeife, 1998).

The above discrepancies, notwithstanding, we are constrained to use these measures, mainly for want of any other parameter to define SME. For the purpose of this study, we shall adopt the definition by the National Council on Industry (NCI). The reason for this is its currency and simplicity. NCI, at its thirteen meeting in July 2001 adopted the following as the reclassification of industrial enterprises in Nigeria.

a. **Micro/cottage industry:** An industry with a total capital employed of not more than N1.50 million, including working capital but excluding cost of land, and/ or, a workforce of not more than 10 workers.

b. **Small-scale industry:** An industry with a total capital employed of over N1.50 million, but not more than N50 million including working capital but excluding cost of land and/or a workforce of 11- 100 workers.

c. **Medium-scale industry:** An industry with a total capital employed of over N50 million, but not more than N200 million, including cost of land, and/or, a workforce of 101-300 workers.

Following the above classification, SME consist of all business organisations whose total capital employed is above N1.5 million, but not more than N200 million including the cost of land and workforce capacity of between 11-300.

Available statistics show that 95% of establishments in the organised manufacturing sector fall into SME category. More disheartening is the fact that at least three out of every four SME fail every year (Nzelibe 1996, Tinubu 2002). What is more, over 90% of those who wished to go into business do not eventually get to start. (Ezeh, 1999).

3.1.1 Preliminary consideration before venturing into SME

Most SMEs fail as soon as they are started because those who start them do not properly appraise themselves and their business idea before embarking on the venture. The Holy writ even counseled that one needs to appraise himself and the business so that one does not stop midway. (Luke 14: 28-30). Consequently, the following should be done before starting a small or medium scale business.

a. Self analysis

Those who break the frontiers of business to start new ventures, even at the risk or failure, are called entrepreneurs. It is pertinent to note that not all prospective SME owners have the requisite personality trait and skills to succeed as entrepreneurs. Consequently, one must objectively appraise himself to ascertain whether one has all it takes to set up small or medium scale enterprise. David Maclelland, discovered through research findings that successful business owners must have high “Need for Power and Achievement” (Onodugo, 2000). They are generally aggressive, confident, upwardly mobile, positive towards risk, hardworking and dogged.

A checklist of the characteristics of would-be entrepreneurs provided by small business management, Honolulu (1977) has the following traits.

Characteristics		*Traits*
Self confidence	-	Independence, individuality, optimism.
Task/result-oriented	-	Need for achievement, profit-oriented, persistence, Perseverance, determination, hard work, drive, energy, initiative.
Risk-taker	-	Risk-taking ability, likes challenges.
Leadership	-	Leadership behaviour gets along well with others, responsive to suggestions and criticism.
Originality	-	Innovative, creative, flexible (openness of mind), resourceful, versatile, knowledgeable.
Future-oriented	-	Foresight, perceptive.

It is unrealistic to expect one to have all these traits to qualify to own a business; it is equally true to note that the more you have these traits the higher the chances of success. Again, even the ones you do not presently have, one needs to have the in-built flexibility to acquire them overtime.

In assessing oneself, one needs to take resources, to ones aptitudes, the things one has done in the past, opinion of close and yet objective friends and confidants, spouses and professional business consultants.

If in the end, one discovers that he is bereft of most of these traits, he should think twice before starting a business venture. If the person must, he can partner with another person who scores high on these traits.

b. Proper examination of the business idea (feasibility study)

Next to self-diagnosis, is a careful and yet systematic examination of the business idea. This is what is generally called feasibility study. Several people start business because their friends are doing the same business. Others are advised by their folks to join and yet some get into business on the presumption that it will succeed. It is some of these tendencies that account for the preponderance of the failure of most SMEs. To avoid this, it is important to carry out feasibility studies before going into business. The detail of feasibility studies will be discussed in the next unit.

3.1.2 Strategic Business Planning

Once the preliminary considerations are done with, the next most important activity in starting up SME is planning. It is often said that when one fails to plan then such a person has planned to fail. Nzelibe (1996) rightly observed that one of the most serious operational problems of SME is lack of effective and formal planning.

Planning is the process of determining what to do in the future and how it is going to be done. It takes discipline and mental hard work to plan. At the end of the planning process the following outcomes would be arrived at:

a. Ends-in-view

The first major outcome of planning is a clear statement of objectives. They reveal what the owners of the business entity want to achieve. The difference amongst vision, mission statement and objectives is a matter of scope and specification. Vision and mission are broader; cover a longer time span and less specific. Objectives are specific, measurable, realistic and time bound. They are derived from and are a stepwise means of attaining visions and missions.

b. Strategy

This is the means of realising these objectives. It also encompasses how one would compete. This strategy even starts with what legal forms of business ownership that one chooses. Is it going to be a sole proprietorship kind of business or a partnership? Again one may consider starting a new business entirely, buy an existing one and/or merge with another organisation.

Under strategy, one needs to consider the particular market to go for and what special offer to give them. Depending on the organisation's strength and weaknesses one may offer unique, high value products or penetrate the market with low prices.

Another important consideration under strategy is on how to grow. A forecast of the business environment needs to be made and careful decision of how to enable the business to grow.

Growth can be undertaken by expanding the current business operations. In this case, what is required is to operate at full capacity or integrate either forward by taking on the activities of distributors or backward by doing what your supplier used to do. Growth can be undertaken by outright diversification into entirely new field. This happens when growth prospects in the current business are limited or not very rewarding. Growth can be attained by either merger or amalgamation. Both forms entail fusing two existing organisations into one. It is called merger when the identity of one of the old firms is retained. It is amalgamation if a new identity is entirely given.

c. Financing options

It is during planning that one determines how to finance a business. Major determinants of the choice of financing option are the willingness or otherwise to dilute ownership, the size of the business and its profitability. Meanwhile, the spectrum of financing options available to a prospective SME owner is personal savings and contributions from family members, equity financing from partners and other stakeholders and debt financing. The latter, which is debt financing, entails seeking credit in commercial banks, finance houses and government financial institutions. All of them require some processes and technicalities, which for the most part and for a long time, have not been met by SMEs leading to poor flow of fund from such sources.

A new scheme however has been invented by the Bankers' Committee supervised by CBN to help the funding problem of SMEs. It is called Small and Medium Industries Equity Investment Scheme (SMIEIS). This scheme came to fill the gaps which debt financing created.

d. Personnel requirements

The wheel that moves organisations forward are the human resources therein. During planning, a careful design of how to attract and retain requisite personnel to run the firm will be undertaken. An organisation may shop for one or two experienced hands and use them to train other personnel. Another may go for experienced people immediately and get trainees later. The approach used is a reflection of the nature of the organisation and the strategies with which they want to invade the market with. Personnel policies are designed to guide the implementation of personnel decisions.

3.1.3 Running of Small and Medium Enterprises

To effectively run SME after inception entails these three related activities:

- design and implement actions of systems and structures
- motivation
- controlling

a. Design and implementation of systems

Hindsight in consulting for SMEs has shown that most business concerns that fail do not have systematised procedures of doing things. Those who overtime and through rigorous effort were able to systematise the way they recruit, dissolve authority and responsibility, manage inventory, train, discipline, record and disburse funds, etc, hardly ever do badly.

Essentially there is need to have the following systems for effective running of SMEs. They are:

Administrative system: this comprises organogram and job description manual. It shows at a glance who occupies what positions, who reports to whom, and their authority relationships. With this, vacancies can be declared and training of new entrants proceeds systematically.

Accounting system: this shows in a nutshell how money comes and moves within and outside the organisation. It entails the design of requisition forms and payment vouchers. This system defines authority limits in terms of finances. Imprest for various offices and its retirement procedures are identified.

Inventory system: This simply details what happens to raw materials from the point of purchase till it is turned into a finished product. It says something about the required quantities of both finished product and raw materials that should be held at any point in time. Issues as to when to order for more discard the ones held and the like will be handled by it.

Personnel policies record: it is important for every staff on entry to be acquainted with the code of conduct expected of him/her. It defines what the dos and donts. This is important. Most SMEs carry out these things retroactively. Sometimes, punishment is determined only when the offense is committed. This does not augur well for the smooth running of the organisation.

There are other systems such as MIS or record keeping systems, internal control systems, etc. the ones discussed are the most basic ones. It is pertinent to submit that success in running a small or medium scale business cannot proceed effectively without designing and implementing these systems.

b. Motivation

Motivation constitutes those things which when out in place propels a worker to behave in desired manner in the work environment. (Onodugo, 2000). It is what explains why people behave in certain ways in an organisation.

This is very important, as the bane of most SMEs is their inability to retain staff. High staff turnover makes succession and continuity difficult and throws overboard the benefits of training. To overcome these, one need to motivate staff to make them put in their best. Below are basic guidelines that underlie effective motivation.

Adequate reward for labour: workers respond to their work the same way they are treated. Often time entrepreneurs and business managers think that they are doing themselves a favour by paying pittance to their workers. Once a worker is not well paid, not only will he not put in his best but he will be looking for job elsewhere.

Participation in decision making: there is nothing as motivating as a feeling of sense of belonging. When workers are allowed to know what is happening in an organisation to the point of being allowed to make an input, they will naturally own the outcome of such decisions. Feeling of sense of belonging and camaraderie will pervade the environment leading to increase in productivity.

Reinforcement: staff members can be prodded to put in their best by acknowledging their efforts in the work place. It is not always money that motivates. Acknowledgements such as praise, certificate of merit and/or promotion can equally serve as a positive reinforcement to such worker to do more.

Job environment and growth path: one thing that makes inward drive to dampen is a job schedule that is monotonous. One worker can readily predict what he/she is required to do most of the time, boredom starts setting in. If on the other hand, the job is challenging and presenting varying phases and fronts, it draws out the best from the workers. This is more so, if such a staff member knows the clear growth path such a hard work will earn him.

Training: training does two functions. It empowers the staff to do work better. It also meets the intrinsic desire of staff members who crave for improvement. This is motivation.

c. Controlling

This is the managerial function which ensures that the goals and objectives of any organisation are realised. It is not enough to plan and start up businesses, it is equally important that close monitoring of the activities are embarked upon to ensure that it conforms to the initial plan. This is where controlling comes in.

SMEs by their very nature are prone to fraud and waste. In order to ensure proper running of the firm, adequate control measures must be deployed to guard the conduct of organisation members. The following are the techniques that will help business organisations facilitate control.

Careful adherence to plan and policies: the results of planning are enshrined in a document called plan. It is important that the targets contained in the plan and policies initiated to facilitate it are all closely adhered to. In other words, a sine-qua-non for good control starts with good planning.

Periodic evaluation of the financials: one way of controlling of the financial activities of SMEs is by looking at their financial statement (Fs). Financial statement consists mainly of income statement and balance sheet. The former reveals the difference between operating income and expenses. The balance is either profit or loss. While the latter shows the net worth of the organisation. It shows in sum the profile of organisation’s assets and liabilities. With this information, managers of SME would make the necessary adjustments to ensure that the organisation is financially healthy.

Budgetary control technique: budgets are action plans expressed in quantitative terms. It is a statement of future expected income and expenditure. Budgeting is the process of preparing a budget, while budgetary control is the process of controlling organisation's activities through the instrumentality of a budget. As a medium of control, budgets are very effective. Once a budget is prepared, every operative will align its activities to conform to the budget items. Deviations from the budget estimate must be done with prior knowledge of the appropriate authorities. With this, financial recklessness is reduced to the barest minimum.

Inspection and quality control: this is mostly used in manufacturing concerns. It proposes periodic check of the manufacturing process to ensure that the output conforms to initial design specification and level of performance. In the process, sub-standard and defective products are isolated for rework or discard. This helps to ensure that the products that reach the consumers are top value products that are intended for them.

Benchmarking: this is one way by which SMEs can ensure control and attain improvement. This is the process by which organisation's products and processes are matched with prevailing standard of the "best practice". The closer a firm's activities are to the best practice the better the chances of it realising corporate goals.

Designing accounting system and having qualified personnel to run it: as has been mentioned earlier, it is good for every organisation that is control conscious to design accounting manuals and ensures compliance by staff members. Central to the effective implementation of accounting manuals are qualified personnel. A well paid chartered accountant would not easily commit fraud since he knows that he will not only lose his job, but his license may be withdrawn. People who are not so qualified may not exercise such restraint. This also presupposes that staff members should be paid comparatively competitive salaries. Anything short of this could make them not to value the job as to wanting to retain it.

4.0 CONCLUSION

The central thrust of this unit is that in the wake of the deregulation of the Nigerian economy, we shall witness the birth of many SMEs. These firms, well managed, will bring about the required turn-around of our economy.

This unit had deliberated on how to set up and run small or medium scale business concerns. While one cannot claim that it is exhaustive, it certainly has the basic ingredients that will help those who genuinely want to start and run one.

5.0 SUMMARY

To be an entrepreneur, you must be able to control, motivate, direct and take risk.

6.0 TUTOR-MARKED ASSIGNMENT

Explain some of the attributes of an entrepreneur

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UNIT 4 THE NATURE OF ENTREPRENEURSHIP

CONTENTS

1.0 INTRODUCTION

Today's dynamic environment demands that organisations and their managers adapt and review themselves continually to succeed over time. People and organisations not only must change, they must change frequently and at a rapidly accelerating pace. Success in the highly competitive business environments, in particular, depends on *entrepreneurship*, a term used to describe strategic thinking and risk-taking behaviour that results in the creation of new opportunities for individuals and/or organisations. These opportunities frequently appear in the form of new business ventures-such as the now familiar Domino's Pizza and Federal Express overnight package delivery, or as new goods or services, such as the popular 3M Post-it note.

2.0 OBJECTIVES

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

- define the concept of entrepreneur
- explain entrepreneurship and small business
- distinguish entrepreneurship from large enterprise

3.0 MAIN CONTENT

3.1 Entrepreneurs

An entrepreneur is a risk-taking individual who takes action to pursue opportunities in situations others may fail to recognise, or may even view as problems or threats. Characteristics typically associated with entrepreneurs include:

1. *internal locus of control*: entrepreneurs believe that they are in control of their own destiny.
2. *high energy level*: entrepreneurs are persistent, hard-working, and working, and willing to exert extraordinary efforts to succeed.
3. *high need of achievement*: entrepreneurs are motivated to act individually to accomplish challenging goals.
4. *tolerance for ambiguity*: entrepreneurs are able to tolerate situations with high degrees of uncertainty.
5. *self-confidence*: entrepreneurs feel competent, believe in themselves, and are willing to make decisions.
6. *action oriented*: entrepreneurs want to get things done quickly and do not want to waste valuable time.

A common image of an entrepreneur is as the founder of a new business enterprise that achieves large scale success. Anita Roddick's Body Shop, Bill Gates' Microsoft, and Sam Walton's Wal-Mart are but a few dramatic examples of this type of entrepreneurship. But entrepreneurs also operate on a smaller scale. Those who take the risk of buying a local McDonald's or Subway Sandwich franchise, opening a small retail shop, or going into self-employed service business are also entrepreneurs. Similarly, anyone who assumes responsibility for introducing a new product or operations change within an organisation is also demonstrating the qualities of entrepreneurship.

3.2 Entrepreneurship and Small Business

Entrepreneurship plays an important role in the formation of smaller enterprises. A small business is commonly defined as one with 500 or fewer employees. The United States Small Business Administration, or SBA, also states that a small business is one that is independently owned and operated. Almost 99 percent of American businesses meet this definition, and the small business sector is very important in most nations of the world. Among other things, small businesses offer two major economic advantages.

1. They create many job opportunities
2. They are the source of many new goods and services.

Three of the most common ways to get involved in a small business are to start one, buy an existing one, or buy and run a franchise.
Small businesses have a high failure rate-as many as 60-80 percent fall in their first 5 years of operation. Although many factors affect such outcomes, an important foundation for such success is the *business plan* – a written document that describes the nature of the business as well as

exactly how an entrepreneur intends to start and operate it. Writing such a business plan helps the entrepreneur ‘think’ through the various details of setting up a business. Typically, this plan will be shared with banks, venture capitalists, and other potential investors in order to attract any additional funds that may be needed to make the startup possible. Small business success will always be based also on the entrepreneur’s ability to implement the management process - planning, organising, leading, and controlling.

3.3 Entrepreneurship and Large Enterprises

In today’s dynamic and competitive environment, larger organisations also depend on entrepreneurial managers willing to assume risk and encourage the creativity and innovation so important to continued success. Yet, this task is especially challenging in very large and complex systems organisations whose natural tendencies may be toward stability, rigidity, and avoidance of risk. Because of this, the concept of entrepreneurial behaviour on the part of people and subunits operating within the confines of large organisation to act like small ones. To do this, some large organisations create small subunits, often called *skunk works*, in which groups of people are allowed to work together in a small group of enthusiastic employees that was once sent off to separate facility in Cupertino, California. Their mandate was straightforward - to create a state of the art, user-friendly personal computer. The group operated free from the firm’s normal product development bureaucracy, set their own norms, and worked together without outside interference. The ‘jolly roger’ was raised over their building as symbol of independence. It worked: this is the team that brought the now famous MacIintosh Computer into being. The success of the Maclntosh and its offspring at Apple is a fitting reminder of the importance of this chapter’s focus on strategic management and entrepreneurship in organisation.

4.0 CONCLUSION

In conclusion, it can be stated that the entrepreneur is not motivated by money itself but rather by his high motivational needs, especially his need to achieve. Money is a by-product for accomplishing some nobler goals. The entrepreneur has an idea and a dream. His awareness of people and their needs, and his technical training, enable him to perceive profitable marketing opportunities that others have neglected. We know from past studies, that in the more advanced countries, entrepreneurial characteristics are related to certain sociological factors in the entrepreneur’s childhood and to personal experiences in later adult life. Further research should reveal additional parameters that will help to explain the complex individual we call an entrepreneur.

Governments have always sought to find and develop entrepreneurs. In underdeveloped nations, these individuals often hold the key to economic growth for a whole society.

5.0 SUMMARY

In summary, an entrepreneur is dynamic, result driven and always believes in himself.

6.0 TUTOR-MARKED ASSIGNMENT

Discuss the nature of an entrepreneur

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7.0 REFERENCE/FURTHER READING

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UNIT 5 THE PLANNING FUNCTION IN HOSPITALITY INDUSTRY

CONTENTS

1.0 INTRODUCTION

Planning involves the development and selection from among alternatives of the necessary course of action to achieve an objective. This definition is one of many. However planning is defined, it is inevitably described in terms of the actions necessary to achieve an objective. The objective is therefore the essential pre-requisite to planning and planning can commence and be useful only when objectives are properly selected.

Planning is a necessary everyday activity both in life and in management. Planning should go on at every level of an organisation, from dishwasher to the chairman of the board of directors. Planning for one's life work is as essential as an active process related to long-range organisational goals and day-to-day work as well.

Planning is something everybody agrees is important. But planning often gets neglected, probably because it requires hard thinking and involves the uncomfortable work of dealing with uncertainty.

Failure to plan invites trouble. Three different kinds of examples illustrate why planning is necessary at all levels of the organisation. Consider, first of all, the waitress who does not plan her next trip to the dining room in the light of needs of her entire station. She will probably have to run back and forth to get one or two items that she could have brought all at once. She wastes, in this way, two of her precious resources: time and energy. At the end of the day she has worked harder than her co-workers and probably earned less in tips from customers who had to wait for her to complete those extra trips.

If you have ever been in a restaurant that has run out of eggs at breakfast or bread during a rush on the sandwich station, you have seen a second example - the results of poor operational planning. And you know its cost: dissatisfied guests, upset employees, the loss of some of those inconvenienced customers and perhaps some of the people they talk to. In general, the organisation's reputation suffers.

Failure to plan entails serious risks at any level. Your own plans are most important to you. Just as the waitress that wastes time and the restaurant that runs out of eggs lose profit opportunities so you may waste a good deal of effort and miss opportunities if you fail to plan in the following two ways.

1. You need to plan for yourself at general levels.

a. Whatever work you do (desk, clerical, college home work, or motel housekeeping) your work will be easier and quicker if you can plan it.

b. As a supervisor or manager, you must learn to plan the work of others.

c. In addition to planning the work you do for others, you must come to think of your own career as a form of business since you sell services to your employer. Thus your career development involves planning for the kinds of services you want to be selling at some future point – banquet manager, sales representative, food production supervisor, etc. – and then planning how to achieve that position within a reasonable period.

- You will probably have to accept the fact that, as a member of an organisation, you are part of somebody else's plans. The point is that understanding the planning process helps you to understand the need of a well-managed company which has carefully developed plans. As an understanding participant in planning, you should be a more effective employee and find greater meaning in your work.

2.0 OBJECTIVES

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

- identify planning as regards organisation
- describe how to strategise in an organisation
- explain various operational issues in an organisation .

3.0 MAIN CONTENT

3.1 Planning Organisation

We may define planning as the work managers (and workers) do to visualise the future in a concrete way and to determine course of action that will achieve the organisation's goal over a definite period.

ORGANISATIONAL LEVEL

Top Management
|
Middle Management
|

Supervisors

|

Workers

The term "planning" denotes anticipating several different sets of circumstances for different purposes. Several key terms will help you grasp the idea of the planning process. Policies are general guides for dealing with the future. They do not tell what to do; they indicate how to reach a decision. Policies leave much to the discretion of the decision maker and they provide a predetermined, agreed-upon basis for decisions.

A plan is a reasoned means of moving towards some selected goals. A plan reflects policy and may include rules, methods, procedures standards, and budgets. A plan may have both strategic and tactical elements. Plan describes future events of whatever complexity in a way that shows how they will be ordered to achieve the organisation's goals.

3.1.1 Methods and Procedures

These resemble rules (rules state what must be done and what must not be done). Methods indicate how a standard job is to be done. Procedures are really a sequential set of rules.

The method for stripping a turkey carcass has been determined by a food service operator with the help of industrial engineers. As a result of these studies, waste motions are minimised and the time required is reduced to a minimum.

Most hotels have a procedure that specifies the process a guest's records should go through during his or her stay just as most health care institutions have a similar procedure for patient records.

Standards specify not procedures but outcomes. Some standards pertain to cost control and many related to quality control.

A budget is a numerical plan, generally expressed in naira, although sometimes units of weight or time may be used, as well. The budget specifies the naira results expected from plan of operation.

Most well-run operations prepare budgets that express the results they expect in naira. Those budgets may be supported (in their estimates for housekeeping payroll, for instance) with a statement about house budget at various levels of occupancy as a base for housekeeping payroll projections.

3.1.2 Strategies and Tactics

These are terms borrowed from the military to denote level of importance and time dimensions in plans. Strategy implies large scale, high level and long-term time commitment.

A hotel chain may develop a marketing strategy that relates the hotel's services to the guests it seeks to serve and prescribes, in general, how their patronage will be sought. Each of the units of that chain must develop the tactics that best fit the individual property and its market. Strategies are concerned with overall goals and the general means of achieving them. Tactics are specific, relating methods to individual circumstances.

3.1.3 Operation Planning

When management establishes goals and thinks out policies, its planning work has only begun. It needs a plan of action to specify how the policy will be implemented. Those two terms borrowed from the military, strategy and tactics, distinguish between levels of plans.

Strategic Issues

Strategy, as you remember, concerns long-term, general plans. The discussion that follows will focus on three strategic areas out of many that could be chosen.

a. Product and service strategy
b. Personnel strategy
c. Community relations.

These three areas conveniently illustrate how policy guide decision is implemented by both planning and action.

a. Product and Service Strategies

In food service, a menu is planned, the general pattern of an operation's menu represents a strategy; and the customers you intend to reach indicate the strategy you will develop. Consider a steak house such as "Steak and Ale". The menu reflects a policy of limited selection. This limited selection simplifies production and service. A strategy of self-service for salads represents a decision to give up portion control in return for advantage of having the guests serve themselves.

The advantages of self-service are:

1. the waitress has one less course to serve and
2. the guests get and eat salad while their steaks are being cooked.

A waitress can carry large portions, so fewer waitresses are needed. Moreover, when the guests begin to eat, the wait between courses is less; consequently, table turns are more rapid. With fast turns like this, a restaurant can serve more guests during peak meal periods. The "trade-off" of portion control on salads is more than worth the advantages gained.

b. Personnel Strategies

Many companies wishing to avoid unionism use a compensation strategy that offers pay and fringe benefits well above union scale. In other cases, an aggressive compensation strategy may be adopted by a company not because of unionism but simply to help it employ the cream of the crop in its labour market.

Such a strategy dictates the rule that whenever the wage level in the local labour market rises, the company raises its wages. To follow this strategy, the company must probably initiate a procedure of regular wage surveys in the area.

c. Community Relations Strategies

The traditional way to offer the goals and services of a fast food business is to advertise in the various media. While a hotel, high-quality restaurant often purchases advertising, many of these kinds of operations place heavier reliance on their public relations activities. These institutions – fast food, restaurant, hotel, hospital and school lunch – need financial support from the community in the form of sales, donations or appropriations. Each has a policy of seeking community support, but their strategies differ according to the operational circumstances of each and the guests or clients they serve.

Tactical Issues

These are generally concerned more with short-run and localised actions. But like strategies, tactics are plans, the means of implementing policy. In a high occupancy chain hotel in a busy city, the property's marketing strategy was dictated by its franchise affiliation.

The manager realised that a very large number of hotel rooms were being built in Ikeja area. It became apparent that when all the properties under construction opened, the Ikeja area would have an oversupply of rooms for several years to come. To prepare for this future marketing problem, the manager developed what was dubbed "FIRM Service". This tactic cost practically nothing, and it dealt with the problem of heavy future competition by gaining an advantage in that local market the franchise group's strategy identified as most promising.

3.1.4 Long-Range Planning

You can often plan today and tomorrow "in your head". The situation may be simple enough for you to grasp intuitively. But when you make decisions that will have an effect for months or years, you need more sophisticated planning tools. We provide a few related illustrations to familiarise you with this kind of analysis.

a. Return of capital

When an organisation makes an investment, it generally expects to earn that investment back within some definite period. Take this simple situation: A new vacuum sweeper for use in public area costs N400.00. The larger machine is more efficient, and it reduces the hours required to vacuum the area from 100 a month to 90. If the operator's time costs N4 per hour, we can calculate two crude measures of value, and these measurements are common, simple decision aids. They are called the PAYBACK period and the rate of return.

A useful formula follows:

P = Payback period
OS = Operating savings P = N1/05
NI = Net investment
For our problem
OS = 10 HOURS × N4 = N40
And
P = N400/N40 = 10 months

Notice that we have specified the monthly savings, so the payback period is also expressed in months. The new machine will pay for itself in just under a year.

Another way of analysing this problem is to determine the rate of return (ROR). Here we just invent our formula, but the results are usually expressed in annual terms. So, the monthly savings in the previous problem are multiplied by 12

ROR = OS/NI = 40/400 = .010 or 1%

Such a short payback period indicates a very favourable rate of return. In a business where money to invest is at a premium and many departments require funds for new equipment, these techniques give us the means to establish investment priorities.

In more complex cases, *a time adjusted* rate of return may be used. Another common tool is the BREAK-EVEN POINT computation. This technique is similar to the payback period method. Suppose a new banquet room is proposed. Management expects the banquet check average to be N40.50 and the banquet check food costs to be 33 percent. All other costs of the proposed banquet department are fixed. If these fixed costs (the monthly payroll, heat, light and power, depreciation, etc.) for this room are N7, 500.00 how many banquet check foods must be sold per month to cover the cost of the banquet room (in other words to break-even)?

Our new formula follows:

BEP = Break Even Point
MR = Marginal Revenue (revenue less variable cost)
FC = Fixed costs (these are costs which will occur regardless of volume of sales if the decision is made to go ahead)
S = Sales
VC = Variable cost
MR = S – VC = N4.50 – N1.50 = N3.00
BEP = FC/MR = N7500/N3 = 2500 meals.
Thus, 2500 meals per month will cover all costs for this room or not on the basis of its judgment about the number of meals it will probably serve.

b. Cost-Benefit Analysis

In business, the measure of naira profit earned is not just useful; it is the principal decision-making guide. In school lunch or congregate feeding, such a measure is not enough. To begin with, revenue from guests is not always a significant factor because the cost of the programme is covered by government funds. The programme purpose is not to earn profit. Moreover, the decisions cannot always be measured in naira.

Goals and policies provide the basis for developing plans, both strategic and tactical. As the goals addressed relate to longer periods, however, those responsible for planning cannot rely on intuition. They must use more formal and often complex means analysis.

c. The Individual as a Planner

If an operation is to be successful, individual workers must begin to consider themselves as planners. Notice the planning a waitress automatically engages in as she moves from kitchen to dining room and back. As she steps out of the kitchen she quickly sums up the situation on her station: one of her three tables (table A) has just been seated. A second party has finished its main course (table B) since she left the dining room. A third party (table C) is waiting for the dessert she is carrying. She plans her next moves in order of priority.

1. Serve dessert = table C
2. Greetings and assurance of return while serving water = table A
3. Take dessert = table B
4. Take appetiser and main course orders = table A
5. Return to kitchen

As she carries out this plan and heads back to the kitchen, she realises she must plan her movements in the pantry to minimise wasted time and effort. On the way out of the dining room she asks the busboy if he can clear table B. with his assurance on that she plans her moves in the kitchen.

1. Call dinner order for table A
2. Pick up appetiser for table A
3. Pick up dessert for table B
4. Return to dining room

Her pattern is not necessarily the right way to handle three-table station and any actual situation would certainly not be thus neat. The point is, a waitress relies heavily on planning whether or not she is conscious of it.

When the head cook arrives at work at 8a.m. she realises that three meals confront her with immediate problems. Breakfast is now in progress and usually busy. The short order cook is in trouble because he is running out of his set up (raw food stored in a nearby refrigerator). The turkey on the menu for dinner needs to come out of the freezer right away. A roast round has to go in the oven immediately to be ready for an early banquet.

Planning obviously pervades the well-run hospitality operation at all levels, from the maid who checks the stock on her cart to the general manager, who orchestrates all the planners he or she works with.

3.2 Planning as a Personal Process

Someone interested in a hospitality career must begin to accumulate useful learning experiences in the earliest, least skilled jobs. Now it is time to reinforce that concept with conviction that personal career goals need to be identified as early as possible (without an artificial forcing).

These goals may well dictate a policy of putting skill learning first and income second in choosing jobs while in college, institution and perhaps, for those first years out of college, as well. This "learn first earn second" strategy ensures "practice". But if income is more important or essential you may have to alter your strategy.
The point is, of course, that planning, policy and strategy are not something somebody else does. No plan is more important to you than your own plan for yourself.

4.0 CONCLUSION

To start a business is not easy. There are lots of planning and research that have to be done. The individual starting the business needs to be very motivated, committed and determined to succeed.

To start business is being seen among many organisations and governments as an easy way to solve problems of unemployment. People should set up their own small businesses in their communities and thereby be able to make a living and to provide the communities with goods and services which are needed.

Failure will not always mean that people give up the idea of starting a business entirely. They will be able to learn from the mistakes made and the chance of succeeding at the second attempt will be greater.

Research has also shown that there is a greater chance for individuals than for groups to succeed in business. If a group starts a business, conflicts will often arise. Many big businesses started small but were later able to expand.

There is also a bigger chance of success if loan is given as opposed to grant. A loan will make people more committed to succeed.

5.0 SUMMARY

In the course of this discussion we were able to understand planning activities of an organisation, operational, tactical and strategic issues applicable to individual organisation.

6.0 TUTOR-MARKED ASSIGNMENT

1. Differentiate between operational and strategic issues in an organisation.
2. Describe tactical issues in an organisation.
3. What do you understand by planning in hospitability industry?

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MODULE 2

UNIT 1 RESTAURANT AND BUSINESS PLAN

CONTENTS

1.0 INTRODUCTION

An individual who wants to start a business should first try to write a business plan.

A business plan is a written description of the planned business. It is a very useful description because it can be given to a bank or to an organisation when we ask for start-up capital. When we approach a bank or a business organisation we might also have to fill in loan application form.

It is very important to write a convincing business plan. The business plan should be written very carefully. It is not difficult to see why. We are trying to convince the bank or the organisation that our idea is a good one and that it will get good value for any money it lends or donates.

2.0 OBJECTIVES

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

- explain in simple form what business plan is all about
- write a convincing business plan.

3.0 MAIN CONTENT

3.1 Writing a Business Plan

Business plans are required whenever money is to be raised, whether from a bank, a finance house, or a provider of equity capital. To you, your business is of supreme interest and importance; to the bank or fund manager, your plan is but one of many that is received. So you must win this person's approval and keep his or her interest. To do this:

1. be clear
2. be brief
3. be logical
4. be truthful
5. back up words with figures wherever possible

3.1.1 Clarity

The person reading your business plan is busy, often has other issues to deal with, and is consciously or unconsciously judging you by the way in which you express yourself. Therefore:

1. Keep your language simple.
2. Avoid trying to get too many ideas into one sentence.
3. Let one sentence follow on logically from the last.
4. Go easy on the adjectives.
5. Tabulate wherever appropriate.

3.1.2 Brevity

If the banker or manager gets bored while reading your stuff, you are unlikely to get the sympathetic hearing you deserve. So, try to summarise as much as posssible, leaving only the essentials of what your reader ought to be told. In-depth descriptions are out.

3.1.3 Logic

The facts and ideas you present will be easier to take in and make more impact if they follow one another in a logical sequence. Avoid a series of inconsequential paragraphs, however well phrased. Also, make sure that what you say under one heading is in line with all you have said elsewhere.

3.1.4 Truth

Do not overstate your case.

3.1.5 Figures

The banker or investor reading your plan is numerate, thinking in terms of numbers. Words will not impress a banker unless they are backed by figures that you have made as precise as possible. So try to quantify wherever you can.

3.2 Designing the Business Plan

The layout of your business plan can help greatly in keeping the reader interested. Above all, the information you give must follow a logical pattern. You could present your material in the sequence shown here, using headings, so that the reader can survey your plan and navigate without difficulty.

1. A brief statement of your objectives.
2. Your assessment of the market you plan to enter.
3. The skill, experience and finance you will bring to it.
4. The particular benefits of the product or service to your customers.
5. How you will set up the business.
6. Your financial targets.
7. The money you are asking for and how it will be used.
8. The longer-term view.
9. Appendices to back up previous statements, including especially the cash flow and other financial projections.

10. History of the business (where applicable).

The above list can be added to, of course, if the people who will read your business plan have a special interest to which you should address yourself. For instance, public authorities are concerned to know the effect on local unemployment: write a special and prominent section to tell them about it.

3.3 Deciding how much to Write

In all business plans something, however brief, should be noted on each of the items listed above. How much you put into each section should be in proportion to the size and scope of your project as the reader of your plan will see it. A busy bank official will not want to read through pages of material if he is being asked for no more than a few hundred pounds. On the other hand, he will not be impressed if, when asked to lend £100,000, he is given only a sentence or two on the aspect that is of interest most.

3.4 Getting down to it

Careful writing of your business plan will give you a better insight into your own business.

You have a marvelous project; you have a shrewd idea that there is a market for it; you have obtained a good deal of advice from experts and have done sums to calculate your hoped-for profits, your cash flow and the money you need to raise. So, when you get the finance, you will be ready to go. Or so you believe! But it may not entirely be in your favour. You still have some work to do. Now is the time to do it.

‘Writing’, said Sir Francis Bacon, ‘makes an exact man’. There is nothing so effective in testing the logic and coherence of your ideas as writing them out in full. As the future of your business depends in large part on your ideas working in a logical and coherent way, now is the time to subject them to test

3.5 How do I set about it?

Taking the sections numbered opposite one by one, make notes under each heading of all you have done or expect to do. For example, regarding Section 2, what do you really know about the market you want to enter? Have you done enough market research? Who will be your customers? How many will there be? How will you contact them? How will you get your goods to them? Or, when it comes to Section 5, have

you a clear, concrete picture of what you will actually do to 'get the show on the road'?
Write it all out! Perhaps you would like to adopt the following method: taking a large sheet of paper for each of the above sections, note down the facts relevant to each of them; then sort them, test for truth and coherence and arrange into a logical pattern.

You will prune down hard when you come to write the document itself. In the meantime, you would have organised your ideas, you would have noticed the gaps and weaknesses, and the business is bound to be the better for it.

3.6 Tackling each section

a. The brief statement

This should be to the point. Just write something to show the reader what your plan is all about. Say what you want to do in one sentence. In a second sentence, state how much money you want and what you want it for.

b. The market

When you come to the main body of your document, start with the section that is most likely to impress your reader. The majority of people lending money believe that what makes for success in business is finding and exploiting a large enough market. So, as a rule, the 'market section' should be the one with which you lead off.

Though your product may be the best since the invention of the motor car and you may have the talents of a Henry Ford, you will get nowhere if there is no call for your brainchild or you lack the means of projecting your product into the market. The person reading your plan will know this only too well and will want to find out whether you are aware of these facts and how well you have done your home work. Your market research is crucial.

Note that where figures are given, and they should be given freely, the authority for the figures should be quoted. If your figures can be checked, this will promote confidence.

c. The skills, experience and resources of the persons involved

A lender or investor will want to know the track record of the person to whom his or her own or clients' money is to be entrusted. Therefore, you must give a fairly full account of your own business career and those of your coordinators or partners. School and academic histories are hardly relevant. Past achievements and technical qualifications, on the other hand, are. Of almost equal importance is the degree of your financial investment. You cannot expect others to risk money in an enterprise to which the founders themselves are not financially committed in a big way.

d. The benefits of your product

This is the most difficult part about which to comment because it is the section in which you are likely to wax most enthusiastically. Human progress depends on new ideas and people with good ones need all the support they can get. You must face the fact that only a minority of innovations can be made commercially viable. Your banker or financier has probably seen hundreds of absolutely brilliant ideas come to naught, and for all kinds of reasons. So, this is the section you will have to write most soberly.

A famous American writer – a writer, not a businessman – once said that if you made a better mousetrap, the entire world would beat a path to your door. This is just not true. Any successful business person could have told him that simply making a better product is only one step on the way to success, and not even the first or the most important step.

Do not get too disheartened. You have, you believe, a first-class product and, as you demonstrated (under number 2, above), the market for it is there. What you must do now is to persuade your reader that the product is a good one and that it will have the edge to help you exploit the opportunities set out under number 2.

Stick firmly to hard fact! ‘Puff’ sentences, such as ‘This is the best widget-grinder on the market and will be the cheapest too’, cut very little ice. Show with figures, why it is the best and why it is not the most expensive. If you have some independent test results, say so, and give at least a summary of them in an appendix. A few genuine figures are worth a page of adjectives, on which, as was stated earlier, you must go easy.

The following pieces of information could be included in this section:

1. A brief description of the product or idea
2. How it works
3. Why it is better than the rivals
4. Any independent appraisal (with details in an appendix)

e. The method

By this time your reader will have a clear idea of your market, your skills and the customer benefits of your product. What he or she wants to know is whether you are going to set about things in a sensible and workmanlike manner. Tell your reader what he or she should know in terms that are as concrete as possible.

First of all, how do you propose to market the product or service? Will you have your own sales force? What will you do about publicity and advertisement? How will you 'target' your sales drive? Under what terms will you sell? When will you be starting on all this? Give a firm time schedule, if possible.

It will promote confidence if you outline your 'management structure'. If you have partners, you need to know who will be responsible for what? How do you intend to keep the various sections in touch with one another? Will you have management meeting once in a week? Will you have it once a month? Will you have it only when there is a desperate crisis? What about keeping employees abreast of what is going on and what is expected of them?

Outline the production methods you will adopt at the start of the project. Write something, briefly, about the premises you will use. A sentence, or possibly two, will tell of the plant and machinery. You may need a workforce. State how many people you will need at the beginning and later, as sales increase. What will be the capacity of the initial set up?

The office is your next concern. As a skill engineer or a keen sales person, you may be impatient of all the paper work. However, to convince your reader that your business will not descend into chaos or grind to a halt, tell him or her who will see to it that it does not. Who will make sure that the letters are answered in your absence? Who will look after the books? Who will answer the phone? Who will process orders? Who will look into invoices? Who will chase up debtors? Have you assessed the amount of work which will need to be done in this department?

Your reader will also want to know how you will control and monitor the business financially. The smallest business needs to know at all times what its cash position is. As soon as there are those who owe you money, or to whom you owe money, it will be necessary to keep regular check. Your banker or your investor will know that many an otherwise good business has come to grief through lack of elementary financial controls. Ensure not only that you have made the necessary arrangements, but that your investor knows you have given this aspect proper thought. Any good accountant should be happy to advise you.

f. The long-term view

So far, so good, you have explained how you will get your project off the ground and how it will run during the start up period. Now, the banker or the investor will want to know how he or she stands for the future.
Some enterprises are essentially short term. Some should continue to be very profitable over a longer period. Some will be slow-growing and their financial needs can be met out of profits. Others will have to accelerate fast and they will need further injections of capital on a pre-planned basis. Your financial banker will want to know your thoughts on all these points.

If yours is a project to exploit some ‘trendy’ idea, the banker will expect some assurance that, if the fashion were to change, he or she could be paid out of ready money and not be locked into unamortised fixed assets, i.e., fixed assets whose cost has not yet been recovered out of profits and which would be difficult to sell. In general, the banker should be told how you see the market over five years and in the long term. Also, what you propose to do about potential competition.

g. Use of the funds

Now that your reader knows that you have a good product, that there is a market for it, and that you know how to run the business in an efficient way, you should explain, in fair detail, why you need his or her money and how you will spend it. Emphasise how much money you and your colleagues are investing. No one is going to risk money on your project if you are not substantially committed.

Having added up the sums you are putting in and all that you are hoping to raise, list the items you will be spending the money on, such as:

1. patents
2. land and buildings (give some details)
3. plant and equipment (specify major items)
4. cost of publicity for the initial launch
5. working capital (reference to cash flow forecasts)
6. reserve for contingencies

h. Financial targets

Although your hopes and plans for financing your business will be set out in all the cash flow forecast, etc, which you will attach as appendices, it will be helpful if you give a brief summary now of the important points. No matter how small the business, you will be expected to show the following.

1. The expected turnover for the first year
2. The expected net profit for the first year
3. How much of the loan will be paid off in one year
4. When you expect to pay off the loan entirely
5. What you hope for in the second year (when payments from the business start-up allowance, if any, will no longer be coming in).

You do not have to show that the business will make a profit in the first year. Your banker knows that many businesses make a loss initially and still go on to succeed. If you show that you can expect to achieve profit in the long term, your banker should be prepared to go along with this. However, if you are raising equity capital, there are other considerations. Most equity investors expect to be with you a long time. They are interested in capital gain and, if available, dividends. The additional pieces of information they will want are the following.

1. The rate at which you expect profit to grow
2. What your dividend policy will be
3. What you and the other directors will be taking out of the business before the equity holders' share in the profits
4. What plan or ambition you have (if any) to sell out, to buy them out, or to go on the AIM (Alternative Investment Market), a junior branch of the Stock Exchange

i. The appendices

What you have said so far should have told the reader all about your project. You have now to add documentation to convince him or her that you have done your homework properly and that you can show good evidence for what you have said. Last and most important will be the detailed financial forecast. This will vary from the relatively simple cash flow forecast on a form supplied by your bank to an elaborate 'business model' prepared by a professional accountant.

The financial projections are the real meat of the whole business plan. A great deal of information should be given, especially in the cash flow forecast. Other appendices could be copies of any documents that will support what you have said previously. They might include:

1. accurate summaries of any market research, either your own or research that has been professionally carried out
2. photocopies of local newspaper articles describing a need for a service you propose to provide
3. picture of your product or products
4. copies of your leaflets or other promotional literature
5. the results of any testing of your product, especially if it has been done by an independent organisation

The general outlines so far given are intended to guide you, for those seeking funds for a new enterprise. If you want finance to expand an existing business or to take over an existing shop, the principles will remain the same, but you will need to write an additional paragraph or pages, preferably at the beginning of your business plan, to do with:

j. The History of the Business

This section should be brief, factual, and based on the audited trading results. At least three years' results should be shown, if possible, as well as the last balance sheet. Reference may be made to such fuller comment, explanation and plans for change as may be given in later pages, e.g. under 'Marketing' or 'Management'.

The history should also tell of any major changes in ownership or management of significant market alterations trends –in other words, it should mention any important happening that has affected the business over the past few years.

It is possible to write a business plan in many different ways. Some banks or organisations have their own rules for writing it. In such cases, we must find out what they require.

We will describe the product or service and the reasons why we think it is viable. We can refer to the community survey and feasibility study. It is important that the bank or organisation gets a good picture of the product or service. It should also get a good idea as to why the product or service is feasible in this area, taking account of demand, competition, raw materials, skills and other relevant points. We should also make a budget to show what the monthly profit will be.

In most cases, we will find that a business plan usually includes the following parts:

- cover page

- the business (description of the business)
- the market
- production
- business income
- business expenses
- start-up capital
- training
- business benefits and risk
- cash flow budget

The Cover Page: The cover page should show the name, address and the aim of the business. It should also give a description of the business, (what kind of product will be produced or service will be provided, location of the business, etc,) and the amount of money required from the bank or organisation. It will also show who made the application and to whom it will be given. The cover page is a short summary of the information which follows in the business plan.

The Business: We should also explain the legal form of our activity (cooperative, sole proprietorship, etc.), what product we will produce or service we will provide, and describe the persons who will be involved in the business (give names, past experience, etc.) we should also say when we plan to start the business, who will manage the business and mention what organisations will be able to give management support, etc. it is good to include a work plan, a constitution and job descriptions.

The Market: In this section we describe who the customers and the competitors will be, how we will promote our products or services, as well as why we think the customers will prefer to buy from us rather than from our competitors. It is very important for us to convince the bank or the organisation that we have a good market.

Production: From this section we will provide information about the production process, how much we will be able to produce, how the production skills will be obtained, where we will be able to find raw materials, tools, pieces of equipment and the need for transportation, a description of our workplace, etc.

Business Income: We should describe the product or service, saying how many we think we can sell and the price we will charge. We should also say what the size of the profit and the income for the members will be. Our figures should be realistic. The prices and profits must not be higher than those we can expect to receive.

Business Expenses: Under this heading we make a detailed budget describing the raw materials, rent, wages and other inputs which we will need and the monthly cost of each.

Start-Up Capital: We need to describe the start-up capital we will need to be able to start our business. We should show if any of the inputs will have to be imported from outside our country (this will cost foreign currency). It is necessary to say which of the inputs has already been secured (either obtained or promised), from where it has been secured and which inputs we require from the bank or organisation.

Training: We should describe the kind of training that is needed by people working in the business. This will probably be of two kinds:

Pre-production training (training in planning to start a business, where to buy raw materials or machines, etc.), will be needed before the business starts.

Production training (how to operate machines, etc,) and *management training* will be needed when the business starts. We should give the number of persons for whom training is required, where it could take place, who would do the training and the time required. It is important to show that everybody will receive adequate training for their future tasks.

Business risk and benefits: Here, we will describe the problems we might encounter when running the business as well as the advantages we have in this business, for example over the competitors.

Cash flow budget: A cash flow budget should always be included in our business plan. The cash flow budget will show how much cash we think will come in and go out from our business during the first six months.

3.7 Budgeting

A budget is a financial and/or quantitative statement prepared and approved prior to a defined period of time for the purpose of attaining a given objective. A budget is normally for a year. It is therefore a short-term plan. One of the primary objectives of budget is to measure the profit earnings of an organisation. However, in the case of government, non-profit making budgets are used:

- as a guide for the present and future
- to plan, control and estimate the amount to be received and spent during a specified period
- to distribute limited resources

- to motivate managers towards the achievement of corporate goals.
- as a means of evaluating performance
- to inform managers about the results and operations of their responsibility domains.
- as a standard of measurement for the purpose of controlling on-going economic endeavours.

Government units that obtain revenues from taxes and other sources use such for current operations by means of budgets. A government budget shows authorised appropriations and estimated revenues. Many however, perceive the term 'budget' as a restraining or impeding factor. Hence, people seem to develop a negative attitude to budgeting.

3.7.1 The Purposes of Budget

Budget serves as a basis for the activities of an organisation which the budget serves. These may be enumerated thus:

1. A budget is an economic and financial document. It highlights organisation's policies which are designed to promote economic growth, efficiency and enhance the quality of life of the workers.
2. It is a useful guide for the allocation of available resources.
3. The budget serves as a means of accountability for the money earlier entrusted and the appropriations of newly approved ones.

3.7.2 Uses of Budgets

Budgets are used for the following:

Planning: Budgets are used to plan. Budgets are plans to which monetary values are assigned, of what are to be achieved in a determinable future time, for example, a year.

Communication: Budgets assist in communicating horizontally and vertically. When budgets are being prepared, individuals, groups, communities and associations will inform Government about their areas of interests. This is 'upward communication'. When the budget is approved, Government reads it to the members of the public and publishes it in the newspapers. This is 'communicating downwards'.

Motivation: Budget is a target to be achieved. Government motivates the staff through promotions and improved conditions of service, for assisting in the full and successful implementation of the budget.

Standard for Management of Performance: Since a budget is a target, it is a measure of performance. What is achieved is recorded and compared with the target of performance set. The process of implementation draws management attention to problematic areas.

Evaluation of Economic and Social Policy: Budgets are used to solve the social problems of inflation and unemployment.

Cost Reduction Technique: Evaluation of operations and procedures may result in cost savings. Double or triple promotion is allowed if the staff performs extra-ordinarily well or he has acquired additional qualification. A newly employed staff will be on step 1 of the grade; if otherwise, the letter of appointment of the officer will state the step to which his salary has been placed. Promotion is supposed to be given every four years, but it is not automatic.

3.8 Management

3.8.1 What is management?

Management is the task of planning, organising, supervising and evaluating so that the aim of the business can be met.

Planning: This means to plan all the activities in advance and to make a work plan. In the work plan we state the tasks which need to be done, when they must be done and who will do them. Planning also include making a budget.

Organising and supervising: This means instructing people who work in the business so that they know what they have to do. It also involves encouraging them to work hard. A good manager tries to inspire workers with a deep sense of the importance of what they are doing.

Evaluation: This means to judge the value or worth of something. In the case of our business, we are especially interested in judging the value of the performance/actual results in comparison with the plans which we have made. We want to know if things are going as planned. To do this, we compare the work plan with performance. We also compare the budget with the bookkeeping. If we judge that things are not going as planned, we must look for the reason why and correct mistakes which have been made.

Management also involves setting up the business and doing bookkeeping and accounting. Every business transaction has to be recorded. We have to record the selling and buying of goods, the payment of wages, etc. to decide the price to sell our product or service is also important. We call this *pricing*. Pricing must be done in relation to c*osting*, a calculation of how much it costs to produce the product or service.

Marketing: This is another important part of management. Marketing involves finding out who our customers are likely to be, what they want to buy and how they can be attracted to buy our product or service. We need to spread information about our product or service. There are different ways of doing this, such as putting up posters, advertisements in newspapers and talking to people in the community. Management should always be looking for a new way to tell people about the advantages of buying their products or services.
There are two types of management which are closely linked together, *financial management* and *overall management***.** Overall management is mainly concerned with setting up a business, making a work plan, supervising, organising, marketing and evaluating. It also involves settling conflicts in the business and encouraging and inspiring the members. Financial management involves everything to do with the control of money: budgeting, bookkeeping, accounting, costing and pricing.

4.0 CONCLUSION

In conclusion, a business plan that is convincingly written places us in the best position of getting loans from our banks or financial organisation. With the guidelines given in this unit, you are on the best track to write a convincing business plan.

5.0 SUMMARY

In the course of this discussion, we were able to discuss various aspects of business plan and the management of business in terms of planning, organising, staffing, coordinating, controlling and budgeting.

6.0 TUTOR-MARKED ASSIGNMENT

1. Business plan is a must to any effective business. Discuss.
2. What do you understand by feasibility studies as an integral part of business?

7.0 REFERENCES/FURTHER READING

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UNIT 2 RESTAURANT AND FEASIBILITY STUDY

CONTENTS

1.0 INTRODUCTION

A woman with disabilities, Dorothy, wanted to make some money. She decided to make baskets and sell them at the market in the local community. She managed to get a loan to start-up the business and she found the raw materials near her home. Yet, after she started production, she was not able to sell many baskets? Why? People in the community preferred to buy plastic bowls, which were being sold for a lower price at the other end of the market. Dorothy wondered if she should lower the price so that she would sell more baskets, but with lower price she would not make profit. (Lena Karlsson, 1992. 'International Labour Organisation').

Another group of persons with disabilities, living in the same community, decided to start a grinding mill. A donor organisation gave them an imported grinding mill, on loan. The group was able to make a large profit from the mill. After sometime, however, part of the mill was worn out and needed to be replaced. It was not possible to find spare parts in the country where the group lived, Zambia. They asked the donor organisation for spare parts. The donor organisation told them that the type of mill was no longer produced and that its spare parts were no longer available. (Lena Karlsson, 1992. 'International Labour Organisation').

Many businesses fail because there are circumstances which prevent them from succeeding. In other words, *they are not feasible.* People in business might have unhelpful circumstances in:

- selling their products (marked problems)
- production (for example, they might not be able to find the right raw materials or spare parts)

- management (they might not be able to learn the necessary skills for planning and organising their work)

It might seem to be a good idea to start a restaurant, a bakery, a soap making business. Yet it would be unwise to start any of these activities right away. We must first test the ideas, to find out if they really can work successfully in the community.

What is a Feasibility Study?

A feasibility study is a way of testing proposed activities to see if they can work successfully. When we are testing the feasibility of a proposed business idea, we want to find out if we will be able to make a profit if we start this type of business. We test each business idea by asking questions about it.

What Kind of Questions Do We Ask in a Feasibility Study?

We usually need to know the answers to the following questions.

1. Will the people in the community buy our product or service rather than a similar product or service from our competitors?
2. Can the individual or persons in the group learn how to make the product or provide the service?
3. Can we obtain the raw materials, tools, and equipment which are needed?
4. Can we find a suitable place to work in?
5. Can we find a suitable place to sell from?
6. Can we transport raw materials to our workplace and finished products to our selling place?
7. Can we manage or learn how to manage our business?
8. Can we sell our products or service at a profitable price?
9. Can we provide enough, in good time?
10. Do we know where we can obtain capital to start-up the business?

What should we do with the Information that is collected in the Feasibility Study?

The answers to these questions tell us which business activities are likely to be feasible. We must help the individual or the group who wants to start a business to choose the idea which is most feasible. We should explain that we want them to get the largest possible profit for their work. But we must also be sure that each person in a group is keen on starting the business.

2.0 OBJECTIVES

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

- conduct a meaningful feasibility study
- describe how to select the most suitable business.

3.0 MAIN CONTENT

3.1 How to Conduct a Feasibility Study

The Feasibility Study has ten sections. Each section begins with a question. For most of the questions it is difficult to answer ‘yes’ or ‘no’ right away. For this reason, under each question, there are others about particular details. Once we have answered the more detailed questions, we should be able to say ‘yes’ or ‘no’ to each big question. It is important to let persons who want to go into business first try to answer these questions, we should do it together.

To answer some of the questions, we will need to find out a lot of information. For example, we may have to go to the different shops in the community to find the price of goods similar to those we are planning to produce.

For other questions, we may need help from business people. They should be able to help us to calculate the price of goods or services. From the community survey, part 2, and from the occupational survey, we may obtain information about people who have been working in businesses similar to those which we will want to start. They may be willing to help with answers to some questions. From the community survey, part 2, and from the occupational survey, we will also see if these people have had problems in any of the matters covered by the questions. They may have had problems about raw materials, transport or other matters, if they have had such problems, we must naturally ask ourselves if similar difficulties are likely to occur in our business.

1. Demand/Competition

Many businesses fail because they cannot sell their products or services. They have marketing problems. People may not want to buy the products or services because they do not need them. Or they may not want to buy because competitors can offer the same products or services at a better price or with a higher quality.

The first question we must therefore ask is:

Q1. Will people in the community buy our product or service rather than a similar product or service from our competitors?

To answer it, we must study the instructions and answer all the questions below:

a. The Need for a Different Product or Service

Suppose we want to start a bakery. We may have reason to think that people in the community will prefer to buy bread from other shops rather than from us. What can be done to change this? We must offer the people a product or service which is different (and better) than any they are already buying. This is the only way to give them a reason to start buying from us.

How can we make our product or service different from others? We may try to make it cheaper, of higher quality, on sale more often, on sale in different quantities, sold in a place where more customers would come, make it more attractive, or completely new in some other way.

b. The Competitors

To find out if our idea for a product or service is different enough to make people start buying it, we must first get some information about our competitors. A competitor is a person or business selling the same or similar product or services as we are planning to sell. From the community survey, it will be known if similar products or services are sold in the area.

It is important to visit competitors in the same town or community where we want to sell. We need to visit at least five businesses. If there are many businesses, we should visit some large ones and some small ones. Some people whom we visit may not want to give much information. They may be afraid of competition. If we start selling the same product or service, customers may prefer to buy from us rather than from them. It will sometimes be helpful to ask someone in another kind of business (not a future competitor) to answer some of the questions.

c. Our Product or Service

After completing as much of the chart as possible we must think about what we want to sell. How will it be different from what our competitors are selling? (It must be different from what all our competitors are selling). Note; if we say 'cheaper', we should be careful! Some organisations try to sell their products or services very cheaply, and then they find out they do not have enough income to buy raw materials or pay the workers. The price we are planning to charge must cover all our costs.

If our product or service is a completely new idea, something that no one else is selling in the community, we must be able to say why we think people will start buying it. We should check which reasons apply to our product or service.

- We know that people buy this product or service when they travel outside the community and they have told us that they would buy it locally if it was available.
- What we want to sell is a cheaper substitute (or alternative) for something else that people already buy.

d. The Market Survey

We should try to know which products or services the people in the community would like to buy. After visiting our competitors, we may think that people will buy from us rather than from them. It is now time to find out from our possible customers if they would like to buy the product or service we are planning to sell. For this purpose we must do a market survey.

It is possible that government organisations or private companies may be among our customers. If, for example, we are planning to start a chicken cooperative we can ask schools, hospitals or hotels if they are willing to make a contract with us to buy chickens on a regular basis.

For the market survey we choose people in the community who buy in shops that sell the same (or similar) product or service as the one we are planning to sell. We must ask 15 to 20 persons at least.

e. Our Ability to Compete

We must now answer feasibility Q1. Will people in the community buy our product or service rather than a similar product or service from our competitors?

We should answer 'yes' if:

- Our product or service is different from others sold in the community and most of the customers interviewed say they would like to buy it because of this difference.
- We are planning to sell something that is sold in the community but most people interviewed say they cannot usually find it when they would like to buy it.
- We are planning to sell something that has not been sold in the community the people say they would like to buy it if available.
- We have made contacts with an institution, school or private company which has promised to make a contract with us to buy our product or service on a regular basis.

We have now collected quite a lot of information about our customers. We will need this information later when it is time to promote our product or service. To promote means to inform customers about a product or service, and try to persuade them to buy it.

2. Skills Training

If answers showed that people in the community are interested in buying the product or service we are planning to sell, then, it is time to find out if the individual or group has the skills needed to produce the product or provide the service or if skills can be learnt. Other questions are; what types of skills are required to work in this business? Does the individual or the group have the physical ability to do the tasks required? Is the individual or the group interested in learning these skills? Does someone in the group or a person in the local community already have the necessary skill and would he or she teach others? Is there a local school or institute that could teach this skill to the group or the individual? These are the questions you need to answer appropriately before going to the next step.

3. Materials, Tools and Equipment

The next step is to ask if we can obtain the raw materials and equipment which will be used in the business.

It will be a good idea to get help in answering the questions from somebody who is already in a similar business. He or she can help us to make a list of all materials, tools and equipment needed. This business person can also give advice on where to find these items. We should always first try to get materials, tools, and equipment in the local community. It is especially important that the materials we need can be obtained in the community as often as we need them.

If we have to import equipment from outside the country it might be very difficult to obtain foreign currency and an import license. There will also be problem in getting spare parts. To get spare parts from another country can take a long time and may be very expensive. We should try to buy tools and equipment made within the home country.

4. Workplace

When running a business, it is important to have a good place to work in. There are some essential things we will need to consider when looking for such a place; the location that customers can get to, space to work in, space to store raw materials in, space to store finished products in, office/meeting space, doors and windows that lock, enough daylight to work by, electricity, running water, telephone, selling place that many customers will come to and other needs we can think of. The location you need depends on the type of business we are planning to start. An oil pressing business using a manual machine does not need electricity and vegetable growing business might not need a building.

In looking for a suitable workplace we might get help from the government, the district council or people in business. It is necessary to visit possible work places that we are able to rent or use free which have the conditions needed. It is important that the rent you have to pay is not very high, since the cost of the rent together with all other costs must be lower than the income from selling the product or service.

5. Selling Place

The next question now is can we find a suitable place to sell from?

We may want to sell the product in a local area only, or in both a local area and in a wider area, such as a region of the country or the whole country. Most businesses find it best to start selling in a local area only and later think about expanding outside their community when their business is running well.

Here are some possible places to sell. We may think of others also.

- At a town market
- On a road where many people pass by.
- In a store where the owner agrees to give or rent the space to us. Directly to a store which will pay us directly and sell the products to its customers. Some stores have branches throughout a region or a country.

- To a business person, called a dealer or wholesaler, who will pay us directly and will then sell the products to other people or stores.
- In our own store or in a store which we own jointly with other organisations.
- From our workplace.

6. Transport

In every business it is important to have satisfactory arrangements for the transportation of raw materials and/or finished products.

In many parts of the world transport is a big problem. Some businesses fail because of transportation problems. Therefore it is a big advantage if we can find the material and sell our product or service within the community. Transport also cost a lot of money and is part of our production costs. If we have to spend on transport our profit will be lower. We have to be sure that we are able to transport our raw materials to our workplace and our finished goods to the selling place. We must also make sure that the persons working in the business can reach the workplace every day.

7. Management

It is very important that our business should be well managed. There must be people who know how to keep the business running smoothly and who can make wise decisions when problems occur.

Management is what we do to make sure that the aim or goal of the business can be achieved. This includes planning, organising, supervising and evaluating the activities of the business. For example, the aim of a sunflower pressing business might be to produce sunflower oil to sell to local community and create income for the people working in the business.

In this case, planning will probably mean preparing a work plan in advance, saying what work must be done, who will do what and when. Planning also includes making a budget, in which we estimate how much income we will receive during the year and how much we will pay out in expenses. If our planning is carefully done, we are much less likely to make mistakes. We can often foresee opportunities and difficulties before they happen.

The people working in the business must be organised and supervised so that they know exactly what has to be done. Good organisation and supervision also means encouraging people to work.

Managers have to plan and supervise the arrangements to set up the business. They have to keep a careful watch on the bookkeeping and accounting. All business matters must be recorded. When, for example, we buy materials, sell goods or pay wages, these must be recorded. If we do not keep proper accounts, it will be impossible to see how the business is doing and mistakes will easily occur. It is also important that a costing of all our goods is made so that we know what price we should sell our goods for.

Evaluation is an estimate of value or worth. We estimate the value of what has been achieved in comparison with the plans. We compare the work plan with the work that has been done. We compare the budget with bookkeeping and accounts. If things have not been going as planned, we must ask the reason why and correct any mistake which have been made.

Another important part of management is *marketing*. This means trying to get the largest possible sales of our product or service. Marketing involves finding out who our customers are likely to be, what they want to buy and how they might be attracted to buy our product or service. It also involves selling, delivering and getting paid for the product or service. It also involves selling, delivering and getting paid for the product or service.

Many businesses fail because their management is poor. We must make sure that the group or individual is educated in management before the business starts. People must learn the general management skills needed to set up a business, make a work plan, organise and supervise the workers, evaluate performance and market the product or service. They must also learn the skill of financial management such as budgeting, bookkeeping, accounting, costing and pricing.

It is important that we should get as much advice as possible about managing our business. There are probably government and business organisations which can advise and help us.

Financial Management - keeping financial records using those records to make business decisions (such as ‘how much should we produce next month?’ or ‘should we raise our selling prices?’) can be difficult. It may be wise to ask a financial expert to help us in the beginning. The best person will probably be an experience bookkeeper or accountant.

The financial expert can help by:

- checking our financial records once a month.
- meeting the committee or the individual once a month to make financial decisions for the next month.

- making an audit of our records once a year. An audit is a thorough examination and checking of accounts by someone qualified to do this. We will have to send an auditor's report to any agency that donates or lends us money. We may also have to send it to the income tax department.

8. Pricing

If we think that we will be able to manage our business, it is necessary to ask this question; 'can we sell our products or service at a profitable price?' To answer the question, we must first study the instructions below.

It may be difficult to do calculations about prices if none of the members or the individual has run a business before. There are many different things to consider. It is therefore a good idea to ask a business person or a business organisation to help with these questions.

Remember the money that we receive from selling the product or service must pay for three things.

- All our production expenses. (For example the cost of raw materials, rent and transport).
- Income for the workers.
- Replacement costs for tools, equipment, etc. and for unexpected expenses.

When added together these three things are called the recurrent expenses. Every year our sales must at least equal the recurrent expenses. Otherwise, we will lose money and the business will fail.

When starting the business we will also have start-up costs. These are the costs we will have before we are able to sell any goods. The start-up costs usually include cost for equipment, tools and furniture as well as rent, salaries and cost of raw materials for the first months when we are not able to sell any goods. It usually takes about six months from the time we start the business until we are able to make a profit.

9. Production

It is important to satisfy the consumers who will buy our goods or services. We must produce enough of the goods/ services and on time, so that they will be ready when the customers need them. We must be able to produce enough in good time.

10. Capital

The last question in the feasibility study is concerned with capital. Capital is the money which we invest or put into our business. We will need a lot of money in the beginning to cover the start-up costs. When the business is running successfully, the income from sales should cover all the recurrent costs. Now the question is how to obtain capital to start-up the business? Is it from local business people, government, and community development agencies, embassies of other countries which have self-help funds, small business development organisations, or banks?

3.1.1 How to Select the Most Suitable Business

We have now completed the feasibility study for all the business ideas which we need to test. It should be possible to choose the most suitable one. To make our choice, we must go through the following steps.

1. List the suitable businesses
2. Choose the best business
3. Call for a meeting

It is advisable to call the community leaders and the representatives of the women and the youth groups for a meeting to inform them about the business chosen.

4.0 CONCLUSION

In conclusion, it is now necessary for us to start planning for the business chosen. It is time to do a work plan and to look in more detail at the sources of finance available to start the business.

5.0 SUMMARY

In the course of our discussion in this unit, we were able to study how we can conduct an objective feasibility study leading to a well established business organisation.

6.0 TUTOR-MARKED ASSIGNMENT

What do you understand by feasibility study and can you use it to conduct a successful feasibility for any business?

7.0 REFERENCES/FURTHER READING

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UNIT 3 NIGERIAN ENTERPRISES

CONTENTS

1.0 INTRODUCTION

Many people think about running businesses of their own at some times in their lives. With some, this is no more than day-dreaming. Others are more serious. This unit will give you the basis of business forms, how to source for capital, evaluation of credit and many more that will help you start your small business as a way of contributing to the development of your community.

2.0 OBJECTIVES

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

- recognise the business forms existing in Nigeria, goals of profit oriented business and financial requirements of various types of business.
- discover how to source for capital for business operations
- identify the concept of capitalisation
- recognise the types of financial market in Nigeria, financial institutions
- distinguish the time value of money, capital budgeting, analysis of financial statements
- explain small-scale businesses in Nigeria
  describe how to prepare a feasibility study.

3.0 MAIN CONTENT

3.1 Business Forms in Nigeria

There are four different legal forms of business organisation:

- Cooperative
- Sole proprietorship
- Partnership
- Limited company/Joint Stock Company.

A cooperative is a group of people who come together voluntarily to produce goods or to provide a service. Usually all members contribute some funds to start the cooperative. In many countries there must be at least ten people to form a cooperative, one person-one vote, and the members have to share the profits either equally or according to how much each member works. The liability for debts in the cooperative is limited to the amount of capital invested.

There are different regulations in different countries on how to form a cooperative. Usually there is a Ministry of Cooperatives or Department of Cooperatives within the government which helps groups who want to form a cooperative. They give advice, provide training in management skills and sometimes assist with start-up capital.

Those who want to form a cooperative should write an application letter to the ministry or department saying they want to become a cooperative. They should submit a membership list and a list of the committee.

Sole proprietorship means that an individual person decides to start a business and he/she becomes the sole owner of the business. The success or failure of the business depends only on the individual him/herself. He/she is responsible for running the business and he/she must be willing to pay losses/debts him/herself. The income produced in the business will be taxed as personal income. A person who plans to start a business should ask the local council office for license. The cost of the license usually depends on the kind of business being planned.

Partnership is a joint ownership business together with one or more people. The partners will share the control of the business and they will have joint responsibility for any decision made. They will share the profits and debts and they will be taxed separately on each individual's share of the business.

Limited company/Joint Stock Company this form of business is not recommended for a small business because it involves complicated legal procedures and heavy taxation. A limited or joint stock company is owned by its shareholders. People invest money by buying shares. Those with more shares have more control of the company. The shareholders are responsible for debts of the company but their responsibilities for debts are limited to the amount of capital invested in the company. The shareholders elect directors who run the company.

3.2 Capital for Business Operation

To finance your business there are many things to it but for the scope of this course you will be given the basics of what it takes to source for money.

Good management is the key to small business success. A firm's profitability is directly related to the ability of its management. Lenders and investors know this. Consequently, they'll want to know the following:

1. *The character of the businessman.* Is he considered a responsible member of the community? Does he have a reputation for honesty? What's his performance record?
2. *Competence of the businessman.* Does he have the necessary background and experience required for successful business operation? Is he a "go-getter" with lots of initiative?
3. *How will the money be used?* Start-up? Expansion? Working capital? Cover up a mistake?
4. *How much money is needed?* Is the amount enough for the purpose? Is it too much? Too little? In the case of a loan: what will be the source and method of repayment? Can the businessman really afford it? What does he own that can serve as collateral or security?
5. *Type of business or industry*. Is it a growing industry, steady industry, or is it on the decline? Is it a "fad" type of business?

In the case of an already established business, a lender or investor will want to know these seven points.

1. The type of business; manufacturing, contracting, wholesale, service, retail.
2. Major products or services.
3. When was the business started and by whom?
4. Education and experience of principals in the business.
5. What is the legal organisation of the business - proprietorship, partnership, or corporation? Why was this form chosen?
6. Some details on how and where the business operates.
7. Major suppliers and customers.

Also needed are financial data on the business, such as the followings.

1. Initial capitalisation: how much money was invested to start the business originally?
2. Where did this money come from?
3. Financial statements for the last two years.
4. Credit rating.
5. Previous financing: How much? When? From whom?
6. Operating ratios of the business compared to industry standards, where available.

Regardless of whether the business is new or already in operation, the lender or investor will want to know the answers to these questions.

1. Does the business have a plan of operation stating goals and objectives for the next four years?
2. What are the short-term and long-term money needs to reach these objectives?

He may also ask the following additional questions.

1. In the event of accident or death of the owner/manager, is there someone who can carry on the business successfully?
2. Is there "key man" insurance?
3. Is the owner insured against losses and liabilities that might occur in the business?
4. How much competition does the business face in its area of operation?

To get financing, a businessman must be able to produce evidence that proves a loan to, or investment in the business will not result in a loss. The provider of financing must be satisfied that the funds are required for sound reasons and that the business can:

1. pay back the money according to terms in the case of a loan
2. generate a profitable return in the case of an investment

The soundness of a loan or investment is best illustrated by clearly mapping out the anticipated future growth of the business. There are four basic forms to prepare:

1. A comparative profit and loss statement.
2. A projected cash budget.
3. Financial statements for the past couple of years.
4. "Growth Plan" for the future of the business.

Where to get help in preparing the information needed for a complete financial picture of the business:

1. Attorneys can often handle both the accounting and tax problems of the smaller business. In addition, they are in good position to advise the businessman if and when he should consider changing his form of business (proprietorship, partnership, or corporation) for legal or tax purposes.
2. An accountant or bookkeeper is the best source of information if the business can afford it.
3. Income tax returns for previous years can supply the basic information necessary for financial records.
4. Banks and small business administration can provide assistance, as well as recommend others in the business community who can help prepare the necessary information.

In planning the growth of your business over, for example, a four year period, you will want to consider the following kind of questions:

1. By how much do I hope to increase my sales?
2. How much more inventory will I have to buy to meet these sales?
3. Will I need a new building or leasehold improvements? How much will they cost?
4. What new fixtures and equipment will I need? How much will they cost?
5. Will I have to hire more people? What will that cost me in wages, etc.?
6. What other expenses will be increased? By how much? (rent, utilities, supplies, insurance, advertising, taxes, other expenses)
7. How much more cash will be tied up in receivables-money other people owe me?
8. Will the increase in sales adequately cover the increase in expenses?
9. How much money will be left over as business profits?
10. Will the increase in sales also cover interest and loan payments?
11. Is this figure worth the time and expense required?

Steps in Obtaining and Maintaining a Credit Rating

1. Contact a mercantile credit agency.
2. Make available to the credit reporter whatever information is requested.
3. Keep the credit agency records current by submitting an annual report.

Four basic ways of getting more money for your business:

1. Trade Credit: purchasing merchandise, supplies and equipment on credit extended by suppliers. The larger portion of small business financing comes from trade sources.
2. Loans: borrowing money from banks, other financial institutions or individuals.
3. Equity Financing: selling part of the ownership of your business to someone else, by taking in a partner or selling stock.
4. Business Profits: Reinvestment in the business from profits.

Types of Financing:

1. Accounts receivable financing
2. Bank credit cards
3. Commercial loans
4. Commodity loans
5. Convertible debentures
6. Equipment financing
7. Equipment leasing
8. Factoring
9. Flooring
10. Improvement loans
11. Indirect collection financing
12. Installment loans (time plan)
13. Inventory distribution financing
14. Inventory financing
15. Passbook loans
16. Professional term loans
17. Real estate loans
18. Secured loans
19. Term loans
20. Trade credit
21. ‘Other’ loans
22. Small business administrative loans:
    - bank participation loans
    - direct loans
    - displaced business loans
    - economic opportunity loans
    - guaranteed loans

These sources can be grouped into two which are:

1. Informal credit institution or traditional institution.
2. Formal credit institution.

However, the large proportion of farmers’ loan comes from the formal credit institution. It is however pertinent to know that majority of the farmers in developing countries still rely on traditional money lender because:

1. their approach to farming is as a hobby not business.
2. the farmer value his time so much that he has no time for bureaucratic procedures.
3. the credit need might be too small. Therefore the production objective is not to make profit but farming is mostly done as a hobby.

4.0 CONCLUSION

Success in raising outside finance can be crucial if your new business is to get off the ground. There is, therefore, no excuse for presenting a poorly thought-out application. Indeed, the rejection of a bad application is probably the best favour an investor could do for you!
There are more sources of start-up finance than many people believe but they all tend to have slightly different preferences and approaches. So, if you believe you have an idea, you have planned properly and are asking for a reasonable amount of money, do not be unduly disheartened by one rejection. Try somewhere else instead. (Richard B. H., 1983.)
The next unit will be providing you some guides to the use of credit.

5.0 SUMMARY

This unit discussed various forms of business organisations. The unit also looked into the basis of credit evaluation, and finally discussed cash flow and techniques of project evaluation.

6.0 TUTOR-MARKED ASSIGNMENT

Discuss various forms of business organisations in Nigeria.

7.0 REFERENCES/FURTHER READING

Ernest W. Walker, (1975). *The Dynamic Small Firm*
Lena Karlsson, (1992). *How to Start a Small Business. (A Manual for Community Workers Assisting Persons with Disability).* International Labour Organisation.
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UNIT 4 CREDIT INSTITUTIONS

CONTENTS

1.0 INTRODUCTION

Credit institutions give loans and are of different types. This shall be discussed in this unit. We shall also discuss some guides that will help you when you want to obtain a loan.

2.0 OBJECTIVES

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

- differentiate between formal and informal credit institution
- describe the basis of credit evaluation and techniques of project evaluation.

3.0 MAIN CONTENT

3.1 Institutional Credit

Credit institutions can be grouped into two namely, formal and informal.

Formal Institutional Credit

Attempts made by credit institutions to make loans easier for farmers to obtain have proved futile. The average small scale farmers in other developing countries still rely on the traditional institutions such as money lenders, traders and shopkeepers. The formal credit institutions tend to take the rate of interest as a prime consideration and it is also highly impersonal. The present interest is as follows:

Bank loan: Approved regime is about 19-22%. For the preferred sector, it is 1-9%. To the average farmer, it is usually more important that loan is adequate and that it is granted without delay. Selecting a proper lender becomes a very important consideration to the farmer if the farmer must succeed.

3.2 Guide to the Use of Credit/Evaluating Credit Capacitor

This guide is important to both the lenders and the borrowers in the interest of stability.

3.2.1 Feasibility Study

A typical feasibility report has an introduction of a clear objective of the business. The second section is the technical aspect of it, this includes the technical knowhow of the business. Technical relationship should be put into current assessment. There should also be an estimation of the cost of farm assets and operating expenses including depreciation. Note the technical relationship in terms of output.

The third section is the market output or consideration which answers questions such as; is there a market for the output? Look at the specific location . The price regime is also considered. What is the current price of the product?

3.2.2 Cash Flow Analysis

Some documents are necessary such as: income statement, what to produce, and what to generate, operating cost i.e. we want to see your margin between income and expenditure. It is also expected to show how money goes into the business and how it is expended. *Cash in cash out*. The cash flow is determined at the end of each year.

Ratio Ration

Your estimation of net present value of a project is the summation of the discounted revenue and discounted cost.

Benefit Cost Ratio

BCR= BENEFIT/COST. For a project to be feasible, BCR must be greater than one.

Internal Rate of Return

IRR (Internal Rate of Return) is the rate of interest that equates the future streams of income to the present rate. Normally a project is feasible if the IRR > the present rate of interest.
The main guides in credit activities are usually referred to as *3Rs* i.e. Returns, Repayment, and Risk bearing capacity.

Returns to the Business

Simply put “this is what the business would have yielded at the end of the loan”

Repayment Capacity

This is a question of illiquidity i.e. has the borrower the capacity to repay the loan when due?

Risk Bearing Capacity

The relevant question here is whether the borrower has the capacity or ability to take the risk of acquiring the loan and investing it in the unknown.

Debt Equity Ratio

This provides an indication of a higher risk bearing ability since more equity is available to cover potential loss that might occur.

Returns

This refers to the most profitable amount of credit which can be used in the business for ascertaining the level of returns. The instruments used for determining returns include the balance sheet, profit and loss account or income statement. These provide the main source of information to the lender. It is on this basis that the credit worthiness of the borrower is ascertained. Returns are however, not sufficient indicator for measuring the success of a business. Some enterprises may be profitable while others are hopelessly unprofitable. It is therefore important to look at the performance of individual enterprise within the frame work.

In the context of the less developed countries like Nigeria, this will involve analysing both the household and the business aspects of the borrower. In other words, there will be a need to analyse the consumption and production.

Repayment Capacity

As a guide to credit utilisation, repayment capacity analysis deserves more consideration. The key question is when the borrower will be able to pay the loan as entrenched in the contract or note or mortgage terms. A loan may be profitable but the borrower may not be able to meet the repayment as it is due. The major reason to this may be the consumption pattern of the borrower. The situation may limit the use of borrowed funds. This is influenced by the amount of indebtedness of the borrower. For example, assets, which are paid out of gross income, are self liquidating assets i.e. they pay for themselves.

Investment Appraisal (Capital Budgeting)

This deals with cash flow - *Cash inflows cash outflows*. Cash in flows are your returns while cash out flows represent your expenses, your payments, and the money that goes out. The uses to which funds are applied can also be identified e.g. initial investment, capital investment, working capital, operating capital, salary etc.

Time Value of Money

This is important in cash flow analysis since money commands higher value in the present than in the future. This is due to cash flow problems, uncertainty in cash flow and inflation.

Various techniques are used in determining this time value of money in cash flow analysis:

1. accounting rate of return
2. payback period
3. internal rate of return
4. Net present value

The first two are non discounting method while the latter two are discounting method.

1. Accounting Rate of Return

This takes average returns over the whole year and expresses it as a percentage of initial investment. For example:

Projects	A	B	C
Investment cost in yr 0	10,000	15,000	15,000

Net flow	Yr1	2,000	9,000	1,000
	Yr2	3,000	8,000	2,000
	Yr3	4,000	2,000	8,000
	Yr4	5,000	1,000	9,000
AR =		14,000/4	20,000/4	20,000/4
		3,500	5,000	5,000

Rate of return on initial investment:

A 3500/10000 ×100 = 35%
B 5000/15000 ×100 = 33.3%
C 5000/15000 ×100 = 33.3%

In a nutshell, those three projects have been ranked in terms of returns to the project. However, this method is not often used in project appraisal, it does not bring into account risk and uncertainty.

2. Payback Method

This deals with the time taken for project to pay back the initial investment.

Project		D	E	F
Yr 0		10,000	10,000	15,000
Net cash flow	Yr1	3,500	3,500	5,000
	Yr2	3,500	3,500	4,000
	Yr3	3,000	3,000	3,000
	Yr4	-------	3,000	2,000
	Yr5	-------	3,000	1,000
	Yr6	-------	3,000	3,000
Payback in years	3		3	5

Payback method does not take account of the value of the initial investment and does not also take into account the problem of discounting. (The present value of money is not also considered).

3. Internal Rate of Return

This method ascertains the true rate of interest a project generates. Suppose a project costs N9, 608 and generates the following cash flow:

Year 1	4,000	0.893	3572
Year 2	4,000	0.797	3188
Year 3	4,000	0.712	2448

The rate of interest is normally given. Assuming r is 12%. Check the annuity table to get the discounting factor 10 – 12%, look at year 1 to get discounting factor = 0.893. Do the same for other years 2^{nd} = 0.797, 3^{rd} = 0.712.

If you are discounting your future stream of income to present value, your discount factor must be < 1.

The implication of our calculation is that the rate of interest is lower than the present lending rate.

4. Net Present Value

This is commonly used in project appraisal. It also looks at prevailing interest rate and takes out a discount. The cost of a project is referred to as cash out flow and hence it is a negative value.

Project cost	Project	Present value factor	Present value
Cash (cash flow)	-10,000	1	-10,000
Year 1	3,000	0.893	2679
Year 2	3,000	0.797	2391
Year 3	3,000	0.712	2136
Year 4	4,000	0.636	2244
Year 5	4,000	0.567	2268
Year 6	4,000	0.507	2028
			14,046

Cash Inflow – Cash Outflow

The Net Present Value [NPV] is a summation of cash flow. This method is used in assessment. The NPV deals with the present value of an amount to be received in the future and if the amount is to be invested today at designated interest rate, the summation indicates whether or not the project will be feasible. Positive NPV indicates that the project is capable of earning enough income to off-set the initial investment within a given period.

4.0 CONCLUSION

This unit discussed various forms of business organisations, given the basis of credit evaluation, and finally discussed cash flow and techniques of project evaluation.

5.0 SUMMARY

Formal/institutional credit is mainly from bank loans. Informal credit is from friends, money lenders and relatives which most business starters prefer to avoid long time protocols involved in the formal/institutional credit.

6.0 TUTOR-MARKED ASSIGNMENT

Compare and contrast discounting and non-discounting techniques of project used in evaluating time value of money.

7.0 REFERENCES/FURTHER READING

Ernest W. Walker, (1975). *The Dynamic Small Firm.*

Lena Karlsson, (1992). *How to Start a Small Business. (A Manual for Community Workers Assisting Persons with Disability).* International Labour Organisation.

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UNIT 5 CHOOSING A FORM OF BUSINESS OWNERSHIP

CONTENTS

1.0 INTRODUCTION

Like Donald and Susan Sutherland, hundreds of thousands of people have started new businesses in the United States. In fact, more than 500,000 new U.S. businesses are started each year. Chances are, you have thought of owning your own business or know someone who has. One key to success in starting a new business is understanding how to get the resources you need. You may have to take on partners or find other ways of obtaining money. To stay in business, you may need help from someone with more expertise than you have in certain areas, or you may need to raise more money to expand. How you form your business can make a tremendous difference in your long-term success. You can form a business in one of several ways. The three major forms of business ownership are:

1. sole proprietorships
2. partnerships
3. corporations.

It can be easy to get started in your own business. You can begin a word processing service out of your home, open a car repair center, start a restaurant, develop a web site, or go about meeting other wants and needs of your community. A business that is owned, and usually managed, by one person is called a *sole proprietorship*. That is the most common form of business ownership.

Many people do not have the money, time, or desire to run a business on their own. They prefer to have someone else or some group of people get together to form a business. When two or more people legally agree to become co-owners of a business, the organisation is called a *partnership.*

There are advantages to creating a business that is separate and distinct from the owners. A legal entity with authority to act and have liability separate from its owners is called a *corporation.*

As you will learn in this unit, each form of business ownership has its advantages and disadvantages. It is important to understand these advantages and disadvantages before attempting to start a business. Keep in mind that just because a business starts in one form of ownership, it doesn’t have to stay in that form. Many companies start out in one form, then add (or drop) a partner or two, and eventually become corporations, limited liability companies, or franchisors.

2.0 OBJECTIVES

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

- compare the advantages and disadvantages of sole proprietorships.
- describe the differences between general and limited partners, and compare the advantages and disadvantages of partnerships.
- state the advantages and disadvantages of corporations, and explain what is meant by the term Limited Liability (Ltd).

3.0 MAIN CONTENT

3.1 Sole proprietorships

Sole proprietorship has been explained in the introductory part of this unit, without wasting time we shall be considering the advantages and disadvantages in some few lines.

Advantages of Sole Proprietorships

Sole proprietorships are the easiest kind of businesses for you to explore in your quest for an interesting career. Every town has sole proprietors you can visit. Talk with some of these business people about the joys and frustrations of being on their own. Most will mention the benefits of being their own boss and setting their own hours. Other advantages they mention may include the following:

1. *Ease of starting and ending the business.* All you have to do to start a sole proprietorship is to buy or lease the needed equipment (e.g., a saw, a word processor, a tractor, a lawn mower) and put up some announcements saying you are in business. It is just as easy to get out of business; you simply stop. There is no one to consult or to disagree with about such decisions. You may have to get a permit or license from the local government, but often that is no problem.

2. *Being your own boss.* Working for others simply does not have the same excitement as working for yourself At least that is the way sole proprietors feel. You may make mistakes, but they are your mistakes and so are the many small victories each day.

3. *Pride of ownership.* People who own and manage their own businesses are rightfully proud of their work. They deserve all the credits for taking the risks and providing needed goods or services.

4. *Leaving a legacy.* Business owners have something to leave behind for future generations.

5. *Retention of company profit.* Other than the joy of being your own boss, there is nothing like the pleasure of knowing that you can earn as much as possible and not have to share that money with anyone else (except the government, in taxes).

6. *No special taxes.* All profits of a sole proprietorship are taxed as the personal income of the owner, and the owner pays the normal income tax on that money. (However, owners do have to estimate their taxes and make quarterly payments to the government or suffer penalties for nonpayment.)

Disadvantages of Sole Proprietorships

Not everyone is equipped to own and manage a business. Often, it is difficult to save enough money to start a business and keep it going. The costs of inventory, supplies, insurance, advertising, rent, computers, utilities, and so on may be too much to cover alone. There are other disadvantages of owning your own business:

1. *Unlimited liability-the risk of personal losses.* When you work for others, it is their problem if the business is not profitable. When you own your own business, you and the business are considered one. You have unlimited liability; that is, any debts or damages incurred by the business are your debts and you must pay them, even if it means selling your home, your car, or whatever else you own. This is a serious risk, and one that requires not only thought but also discussion with a lawyer; an insurance agent, an accountant, and others.

2. *Limited financial resources.* Funds available to the business are limited to the funds that the one (sole) owner can gather. Since there are serious limits to how much money one person can raise, partnerships and corporations have a greater probability of obtaining the needed financial backing to start a business and keeps it going.

3. *Management difficulties.* All businesses need management; that is, someone must keep inventory records, accounting records, tax records, and so forth. Many people who are skilled at selling things or providing a service are not so skilled in keeping records. Sole proprietors often find it difficult to attract good, qualified employees to help run the business because they cannot compete with the salary and fringe benefits offered by larger companies.

4. *Overwhelming time commitment.* Though sole proprietors may say they set their own hours. It’s hard to own a business, manage it, train people, and have time for anything else in life. This is true of any business, but a sole proprietor has no one with whom to share the burden. The owner often must spend long hours working. The owner of a store, for example, may put in 12 hours a day, at least six days a week-almost twice the hours worked by a non-supervisory employee in a large company. Imagine how this time commitment affects the sole proprietor’s family life. Tim DeMello, founder of the successful company Wall Street Games Inc., echoes countless other sole proprietors when he says, “It’s not a job, it’s not a career, it’s a way of life.”

5. *Few fringe benefits*. If you are your own boss, you lose the fringe benefits that often come from working for others. You have no paid health insurance, no paid disability insurance, no sick leave, and no vacation pay. These and other benefits may add up to approximately 30 percent of a worker's income.

6. *Limited growth.* Expansion is often slow since a sole proprietorship relies on its owner for most of its creativity, business know-how, and funding.

7. *Limited life span.* If the sole proprietor dies, is anticipated, or retires, the business no longer exists (unless it is sold or taken over by the sole proprietor's heirs).

3.2 Partnerships

A partnership is a legal form of business with two or more owners. There are several types of partnerships.

1. General partnerships
2. Limited partnerships
3. Master limited partnerships.

A **general partnership** is a partnership in which all owners share in operating the business and in assuming liability for the business's debts.

A **limited partnership** is a partnership with one or more general partners and one or more limited partners.

A **general partner** is an owner (partner) who has unlimited liability and is active in managing the firm.

A **limited partner** is an owner who invests money in the business but does not have any management responsibility or liability for losses beyond the investment.

Limited liability means that limited partners are not responsible for the debt of the business beyond the amount of their investment. Their liability is limited to the amount they put into the company; their personal assets are not at risk.

A newer form of partnership, the master limited partnership (MLP), looks much like a corporation (which we discuss next) in that it acts like a corporation and is traded on the stock exchanges like a corporation, but it is taxed like a partnership and thus avoids the corporate income tax. For example, Sunoco Inc. formed MLP Sunoco Logistics (SXL) to acquire, own, and operate a group of crude oil and refined-product pipelines and storage facilities. SXL began trading on the New York Stock Exchange in 2002. Income received by SXL is not taxed before it is passed on to investors in the form of dividends as it would have been if SXL were a corporation.

Another newer type of partnership was created to limit the disadvantage of unlimited liability. All states are now allowing partners to form what is called a *limited liability partnership (LLP).* LLP limit partners' risk of losing their personal assets to only their own acts and omissions of people under their supervision. This means that the LLP allows you to operate without the fear that one of your partners might commit an act of malpractice that would result in a judgment that takes away your house, car or retirement plan, as would be the case in a general partnership. However, in many states, this personal protection does not extend to contract liability protections for LLP. The LLP is in many ways similar to an LLC.

All states, except Louisiana, have adopted the Uniform Partnership Act (UPA) to replace laws relating to partnerships. The UPA defines the three key elements of any general partnership as:

1. common ownership,
2. shared profits and losses, and
3. the right to participate in managing the operations of the business.

Advantages of partnerships

There are many advantages to having one or more partners in a business. Often, it is much easier to own and manage a business with one or more partners. Your partner can cover for you when you are sick or go on vacation. Your partner may be skilled at inventory control and accounting, while you do the selling or servicing. A partner can also provide additional money, support, and expertise. Partnerships usually have the following advantages:

1. *More financial resources.* When two or more people pool their money and credit, it is easier to pay the rent, utilities, and other bills incurred by a business. A limited partnership is specially designed to help raise money. As mentioned earlier, a limited partner invests money in the business but cannot legally have any management responsibility and has limited liability.

2. *Shared management and pooled/complementary skills and knowledge.* It is simply much easier to manage the day-to-day activities of a business with carefully chosen partners. Partners give each other free time from the business and provide different

skills and perspectives. Some people find that the best partner is a spouse. That is why you see so many husband-and-wife teams managing restaurants, service shops, and other businesses.

3. *Longer survival.* One study that examined 2,000 businesses started since 1960 reported that partnerships were four times as likely to succeed as sole proprietorships. Being watched by a partner can help a business person become more disciplined.

4. *No special taxes.* As with sole proprietorship, all profits of partnerships are taxed as the personal income of the owners, and the owners pay the normal income tax on that money. Similarly, partners must estimate their taxes and make quarterly payments or suffer penalties for nonpayment.

Disadvantages of partnerships

Any time two people must agree, there is the possibility of conflict and tension. Partnerships have caused splits among families, friends and marriages. Let's explore the disadvantages of partnerships:

1. *Unlimited liability.* Each general partner is liable for the debts of the firm, no matter who was responsible for causing those debts. You are liable for your partners' mistakes as well as your own. Like sole proprietors, general partners can lose their homes, cars, and everything else they own if the business loses a lawsuit or goes bankrupt.

2. *Division of profits.* Sharing risk means sharing profits, and that can cause conflicts. There is no set system for dividing profits in partnership, so profits are not always divided evenly. For example, two people form a partnership in which one puts in more money and the other puts in more hours working the business. Each may feel justified in asking for a bigger share of the profits. Imagine the resulting conflicts.

3. *Disagreements among partners.* Disagreement over money is just one example of potential conflicts in a partnership. Who has final authority over employees? Who hires and fires employees? Who works what hours? What if one partner wants to buy expensive equipment for the firm and the other partner disagrees? Potential conflicts are many.

4. *Difficulty of termination.* Once you have committed yourself to a partnership, it is not easy to get out of it (other than death, which

immediately terminates the partnership). Sure, you can end a partnership just by quitting. However, questions about who gets what and what happens next are often very difficult to solve when the partnership ends.

3.2.1 How to form a partnership

It is not hard to form a partnership, but it is wise for each prospective partner to get the counsel of a lawyer experienced in such agreements. Lawyers' services are usually expensive, so would-be partners should read all about partnerships and reach some basic agreements before calling a lawyer.

For your protection, be sure to put your partnership agreement into writing. The model business corporation act recommends the following in a written partnership agreement.

1. The name of the business. Many states require the firm's name to be registered with state and/or county officials if the firm's name is different from the name of any of the partners.
2. The names and addresses of all partners.
3. The purpose and nature of the business, the location of the principal offices, and any other locations where business will be conducted.
4. The date the partnership will start and how long it will last. Will it exist for a specific length of time, or will it stop when one of the partners dies or when the partners agree to discontinue?
5. The contributions made by each partner. Will some partners contribute money, while others provide real estate, personal property, expertise, or labour? When are the contributions due?
6. The management responsibilities. Will all partners have equal voices in management, or will there be senior and junior partners?
7. The duties of each partner.
8. The salaries and drawing accounts of each partner.
9. Provision for sharing of profits or losses.
10. Provision for accounting procedures. Who'll keep the accounts? What bookkeeping and accounting methods will be used? Where will the books be kept?
11. The requirements for taking in new partner.
12. Any special restrictions, rights, or duties of any partner.
13. Provision for a retiring partner.
14. Provision for the purchase of a deceased or retiring partner's share of the business.
15. Provision for how grievances will be handled.

16. Provision for how to dissolve the partnership and distribute the assets to the partners.

3.3 Corporations

Although the word corporation makes people think of big businesses like General Motors, IBM, Ford, Exxon, General Electric, Microsoft, and Wal-Mart, it is not necessary to be big in order to incorporate. However, many corporations are big in order to incorporate. Obviously, many corporations are big and contribute substantially to the U.S. economy. In any case, incorporating may be beneficial for small businesses as well.

A **conventional corporation** is a state-chartered legal entity with authority to act and have liability separate from its owners (the corporation's stockholders are its owners). What this means for the owners is that they are not liable for the debts or any other problems of the corporation beyond the money they invest. Owners no longer have to worry about losing personal belongings such as their house, car, or other property because of some business problem. This is a significant benefit. A corporation not only limits the liability of owners but often enables many people to share in the ownership (and profits) of a business without working there or having other commitments to it. Corporations can choose whether to offer such ownership to outside investors or whether to remain privately held.

Advantages of corporations

Most people are not willing to risk everything to go into business. Yet for a business to grow and prosper and create economic opportunity, many people would have to be willing to invest their money in it. One way to solve this problem is to create an artificial being, an entity that exists only in the eyes of the law - a corporation. Let's explore some of the advantages of corporations:

1. *Limited liability.* A major advantage of corporations is the limited liability of owners. Corporations in England and Canada have the letters *Ltd*. after their name, as in British Motors Ltd. The *Ltd.* stands for "limited liability," probably the most significant advantage of corporations. Remember, limited liability means that the owners of a business are responsible for losses only up to the amount they invest.

2. *More money for investment.* To raise money, a corporation can sell ownership (stock) to anyone who is interested. This means that millions of people can own part of major companies like

IBM, Xerox, and General Motors and smaller companies as well. Corporations can also borrow money from individual investors through issuing bonds. Corporations may also find it easier to obtain loans from financial institutions, since lenders find it easier to place a value on the company when they can review how the stock is trading.

3. *Size.* That one word summarises many of the advantages of some corporations. Because they have the ability to raise large amounts of money to work with, corporations can build modern factories or software development facilities with the latest equipment.

4. *Perpetual life.* Because corporations are separate from those who own them, the death of one or more owners does not terminate the corporation.

5. *Ease of ownership change.* It is easy to change the owners of a corporation. All that is necessary is to sell the stock to someone else.

6. *Ease of drawing talented employees.* Corporations can attract skilled employees by offering such benefits as stock options (the right to purchase shares of the corporation for a fixed price).

7. *Separation of ownership from management.* Corporations are able to raise money from many different investors without getting them involved in management.

Disadvantages of corporations

1. *Extensive paperwork.* The paperwork filed to start a corporation is just the beginning. Tax laws demand that a corporation prove that all its expenses and deductions are legitimate. Corporations must therefore process many forms. A sole proprietor or a partnership may keep rather broad accounting records; a corporation, in contrast, must keep detailed financial records, the minutes of meetings, and more.

2. *Double taxation.* Corporate income is taxed twice. First the corporation pays tax on income before it can distribute any to stockholders. Then the stockholders pay tax on the income (dividends) they receive from the corporation. States often tax corporations more harshly than they tax other enterprises. Sometimes they levy special taxes that apply to corporations but not other forms of business.

3. *Two tax returns.* If an individual incorporates, he or she must fill both a corporate tax return and an individual tax return. Depending on the size of the corporation, a corporate return can be quite complex and require the assistance of a certified public accountant (CPA).

4. *Difficulty of termination.* Once a corporation is started, it is relatively hard to end.

5. *Initial cost.* Incorporation may cost thousands of dollars and involve expensive lawyers and accountants.

6. *Possible conflict with shareholders and board of directors.* Some conflict may brew if the stockholders elect a board of directors that disagrees with the present management.

7. *Size.* Size may be one advantage of corporation but it can be a disadvantage as well. Large corporations sometimes become too inflexible and too tied down in red tape to respond quickly to market changes.

4.0 CONCLUSION

As you can see, you may participate in the business world in a variety of ways. You can start your own sole proprietorship, partnership or corporation. There are advantages and disadvantages to each. However, there are risks no matter which form you choose. Before you decide, you need to evaluate all the alternatives carefully.

5.0 SUMMARY

In summary, sole proprietorship is the type of business ownership that is owned and controlled by one person. Partnership on the other hand is the type of business ownership in which two people come together to start a business while corporation is the type in which the business is separated totally from the owners property and is legally backed up.

6.0 TUTOR-MARKED ASSIGNMENT

Compare and contrast the three types of business ownership discussed, which one is best for a beginner?

7.0 REFERENCES/FURTHER READING

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MODULE 3

UNIT 1 SOURCES OF FINANCE

CONTENTS

1.0 INTRODUCTION

Finance is very crucial and indispensable for the success of any business organisation. No special or business organisation can succeed without funds. Hence, it is necessary to be exposed to the various sources of finance, especially for small and medium scale enterprises which is the subject of this unit.

2.0 OBJECTIVES

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

- outline the importance of finance in business
- differentiate the kinds of capital available in business
- explain how small firms can raise capital.

3.0 MAIN CONTENT

3.1 Importance of Finance in Business

First, it is necessary to place finance or funds in its proper perspective with regards to the operations of a business enterprise, be it large or small.
The four traditional factors of production are:

- land
- labour
- capital
- entrepreneurship

Today we may add a fifth factor, which is technology, information or technical know-how. Our focus in this unit is on the third factor which is capital, otherwise known as finance, money or funds.

In management, we have the four capital M's viz:

- Man
- Money
- Materials
- Markets.

The importance of capital or finance cannot be overemphasised because no form of business large or small, concept or scope, can succeed without capital. Capital can simply be defined as wealth used in the production of further wealth. This we say in Economics that demand for capital is *Derived Demand* because capital is required for the procurement of equipment, machinery, foods and for the purchase of raw materials and for payment of wages etc. It follows therefore, that an organisation without finance is like a ship without a rudder or an automobile without an engine.

3.1.1 Kinds of capital

The capital used in the running of the business enterprise can be divided into two broad categories. These are fixed and circulating capital.

1. Fixed capital

The fixed capital of a firm is the money needed for permanent investment such as the purchase of land, erection of factory buildings, purchase and installation of equipment, etc. from the foregoing, we deduced fixed assets of a firm include the land on which the firm stands, the buildings, machines, trucks and furniture which usually depreciate over a long period of time.

The commercial banks are jointly-stock banks or limited liability organisations which owe a duty to their shareholders to make profits. Consequently, banks usually do not engage in very risky investments such as financing projects that are not likely to be viable, or giving long-term credits or loans and as such, firms have to explore other sources of finance in order to provide the capital needed for their fixed assets.

2. Circulating capital

This is otherwise known as working capital and it is the money needed for defraying the recurrent expenditure of firms. Working capital is used for such purposes as payment of wages and salaries, purchase of raw materials, fueling of vehicles, settlement of electricity bills, etc. since these are short-term credits, firms can obtain loans from banks to finance their working capital.

3.1.2 Sources of Capital

The capital available to a business organisation can be raised from two main sources:

1. Internal sources

These include the firm's own funds or self financing, money realised from past savings, ploughing back of undistributed profits into the business, mergers and the pooling together of resources as in the case of partnership and joint ventures.

2. External sources

The external sources of capital comprises loans or all sorts of borrowing from banks, private sources, investment trusts and finance corporations; government subsidy or grants, and capital realised form the issue of shares, stocks and debentures as in the case of public limited liability companies.

3.1.3 Capital for Large and Small Firms

All the various sources of capital summarised above are not accessible to all types of firms. Much depends on the type, age, size and magnitude of the business organisation in question. Therefore, various firms raise their capital from various sources.

1. Small firms

The main sources from which small firms, such as the sole proprietor and the partnership, obtain capital or funds for financing their business are as follows:

a. Small firms can raise initial capital from the savings which the proprietor or partners have accumulated over a period of time. Such savings may be targeted saving specifically earmarked for the launching of the business in question.

b. The owners of small business can also raise capital by borrowing money from private sources such as individuals, relatives and friends. A common feature in West Africa is to start business with funds contributed by the members of the family, a group of friends or an age group from the same village who had decided to go into partnerships or cooperatives.

c. Another source of capital open to small firms is self-financing through ploughing back or re-investing of profits into the business to an optimum size to enable it enjoy the economic of scale.

d. In West Africa, the government has on some occasions, given loans to small businesses which they are satisfied are likely to be viable through such organisations as the Nigeria Industrial Development bank (N.I.D.B.), the Fund for Agricultural and Industrial Development (F.A.I.D.), the rehabilitation commission, the poultry subsidy and oil palm rehabilitation schemes of the ministry of agriculture, the bank for commerce and industry and the agricultural bank.

2. Large firms

Unlike the firms, capital is usually not a serious problem for the large business organisation, such as joint stock companies and co-operative societies because they have by far richer and multifarious sources of raising capital for their business operations.

a. *Selling of shares:* this is particularly true of the joint stock companies. The chief source of capital for public limited liability company is from the sale of shares to the public. Once a company has received its certificate of incorporation, it can then proceed to publish its prospectus inviting the public to apply for shares and thus subscribe to the capital of allotment or stock certificate which designate them as shareholders of the company by virtue of their having contributed funds to the running of the business. Shares need not always be paid for in full, but when the company is in difficulty or needs more capital for expansion, it calls on shareholders to pay for any balance outstanding on their shares.

b. *Debenture:* apart from selling shares, a public company obtains loans from the public in the form of debentures or loan certificate to those from whom it has borrowed money. Such creditors or debenture holders receive a stipulated amount as interest on the capital they have invested in the business.

c. *Internal self-finance:* occasionally, rather than issue fresh shares or take more loans, a company may decide to set aside a proportion of its profits for purposes of expansion and research. Instead of distributing all profits among shareholders, some of it is ploughed back into the business and this constitutes another source of capital for many firms.

d. *Bank Loans:* commercial banks can more readily give loans to large firms than small ones because these are more firmly established in business and besides, they have got the necessary collateral security which banks demand in case of default.

e. *Investment trusts:* some companies specialise in giving loans for business or credit facilities to firms and other establishments. These are investment trusts, hire purchase and insurance company. Such companies usually have on their staff, a panel of economists who are charged with the responsibility for undertaking feasibility studies of projects for which loans are being sought before recommending the approval of such loans on basis of the financial viability of the applicants firms.

f. *Finance corporations:* these are set up by the government to finance projects which are vital for a country’s economic development e.g. Agricultural Credit Corporation and Industrial Development Corporation. The latter provides capital for the establishment of basic industries, food processing factories and pioneer industries. Government can also provide capital for resuscitation of businesses that have fallen on evil days. The Rehabilitation Commission and the Cooperation for American Relief Everywhere (C.A.R.E) were actively engaged in such ventures in the immediate post-war Nigeria.

The public statutory corporation is in a distinct class of their own in terms of capital procurement for business because these are fully financed by the government and besides, although they are expected to pay their way, they were not established solely with the profit motive as a predominant objective. Thus, the government will usually come to their rescue anytime they are genuinely in financial difficulties.

3.1.4 Survival of Small Firms

From the foregoing analysis, we see that large firms have more sources of capital and so can afford to grow. The small firms, on the other hand, are not so lavishly financed and so most of them remain small. Nevertheless, these small units of business organisation are able to hold their own and remain in business in the face of several odds, such as, paucity of finance and fierce competition with the giant oligopolies, i.e. the large firms.

There are reasons why the small firms survive side by side with the large business and commercial establishments.

a. First of all, it must be realised that the growth of firms is a dynamic phenomenon which is a continuing process with several interacting factors. New firms are born continually and most of them start on a small scale. There is a considerable amount of prestige attached to being in business on ones own and entry into some businesses is fairly easy. Besides, there seems to be an unending supply of potential entrepreneurs who are ready to venture into the exploitation of some new ideas or favourable market opportunities. Some of the small firms of today will grow into the large firms of tomorrow. Many will die in the wake of competitions, but other new small firms quickly emerge to take their places.

b. Some aspects of our economy are associated with small scale production e.g. weavers, tailors, and tinkers operate quite economically in their small firms with very little overhead costs and so remain in business in spite of the large factors engaged in similar production. Such small firms are more flexible than the large firms and also less vulnerable during periods of depression.

c. Another advantage which contributes to their survival is that they are able to add variety to their products as well as pay attention to details according to the speculations of their individual customers. These small firms open at odd hours, give personal attention to their clients, are not subject to bureaucratic control like the large firms, and so can afford to remain in business.

d. Furthermore, the existence of the small firms does not jeopardise the interest of the large firms nor threaten the quasi-monopoly of certain trades. They only fill the vacuum created by the giant oligopolies and so both of them can exist side by side.

e. In addition, there are obvious obstacles to growth, chief among which are lack of capital for expansion and security of high-level managerial personnel. Where long distance transportation is expensive, as in West Africa and many of the underdeveloped countries, operating on a small scale production at a few points, particularly if the necessary raw materials are located at different places and the finished product is bulky and expensive to transport.

f. There is limit to growth of any firm beyond which diseconomies of scale set in. as a business concern grows in size, there is increased risk of borrowed capital, and higher magnitude of losses in the event of failure. In terms of personnel, there is tendency for management to deteriorate in efficiency as a business organisation expands because there are far too many departments and branches to be coordinated, more people are involved in decision making, and formidable difficulties of communication emerge. As the organisation becomes more bureaucratic, there is considerable loss of interest and decline of morale. These risks and defects associated with increase size and scale of production trends to keep firm smaller in size.

g. Security and logistics reasons, the fear of war and possibilities of economic blockade could influence a country to adopt the policy of establishing several small industries in various parts of the country rather than supplying the whole country from one giant firm. If such industry is captured or destroyed by the enemy during war, the nation would have no alternative source of internal supply.

h. A common feature of West African entrepreneurs is their unwillingness to combine with others resulting from the fact that they are mutually suspicious of one another. There is the unusual love of freedom coupled with a desire for quick return on investments and many of the businessmen are reluctant to take risk on a large scale. There is a limit to what a single person can do and so, as a result of lack of capital, managerial expertise and other constraints, many business units in West Africa remain small. On the other hand, SME’s collapse mainly because of mismanagement of funds and mal-administration.

3.1.5 Small and Medium Scale Equity Fund Scheme

The topic of this unit is consonance with the workshop theme of the 14th Enugu International Trade Fair which is on Empowering Small and Medium Scale Enterprise for Sustainable Economic Development. Coupled with the fact that the managers and staff of small and medium scale enterprise have been invited as participants at the workshop; it is necessary to examine the new government policy aimed at encouraging the growth of small and medium scale equity fund scheme.

Under the federal government policy on small and medium scale equity fund scheme which is administered by registered banks with the supervision of the Central bank of Nigeria (CBN), banks are required to set aside 10% of their pre-tax profits for small and medium scale enterprises funding. Equity participation is between the beneficiary enterprises and the funding banks. Owners of such businesses are allowed to use the land on which the business is situated as collateral; while the banks provide funds for direct purchase of equipment form manufacturers as their own equity participation in business. A special account is opened for each SME benefiting from which disbursements are made in gradual liquidation of the investment capital.

It is a matter for regret that many small and medium scale enterprises promoters, proprietors and managers are ignorant of the existence of this very important laudable scheme, due mainly to lack of public enlightenment about the scheme and to the lethargy on the part of the banks to enthusiastically participate in the scheme.

Something drastic must be done to create awareness and ensure proper utilisation of fund, including establishment of a special bank as a receptacle for the 10% equity fund scheme and a special department in CBN charged with monitoring of the fund.

4.0 CONCLUSION

ECCIMA and Manmark would have achieved our objective in organising this workshop, if an awareness is created in the minds of participants on the theme of the 14th Enugu International Trade Fair, and if small and medium scale enterprises (SMEs) are conscious of how best to obtain funds for their businesses and manage same more efficiently.

On the part of government, the organised private sector and funding agencies, it is strongly recommended that more seminars of this nature be organised for SMEs. Besides, a specialised bank should be established for administration of the small and medium scale Equity Fund Scheme, just like its forerunners, and Education Tax Fund Banks which had functioned with comparative success, to the advantage of specialised sectors of the economy, respectively.

It should be reiterated that profits, the reward for entrepreneurship, do not fall like manna from heaven. You need capital and efficient management to generate profits. Participants have been exposed to various sources of capital in this brief paper; which should be explored to their advantage. Finally, it is pertinent to add that with modest capital, prudent management and ingenious entrepreneurship; small and medium scale enterprises will grow by leaps and bounds into large scale businesses and with it, their multifarious services to our society in particular and to humanity in general.

5.0 SUMMARY

There are various sources of finance available for small and medium enterprises.

6.0 TUTOR-MARKED ASSIGNMENT

List the various sources of finance you know.

7.0 REFERENCES/FURTHER READING

Central Bank of Nigeria: *Economic and Financial Review* (Various Issues).

Constitution of the Federal Republic of Nigeria, 1999.

Ocheoha A. O. (1980). *Synthesis of Modern Economics.* Benin City: Ethiope Publishing Corporation.

Synopsis of Policy Analysis and Decision Making Models. Enugu: Amicus – Virgo Academy, 2000.

UNIT 2 INVENTORY MANAGEMENT AND SUPPLY OF RESOURCES

CONTENTS

1.0 INTRODUCTION

The investment in inventories for most firms represents a sizeable sum. Since this investment is so large, management practices which result in savings of a few per cent of total inventory values represent large savings of naira and kobo.

Inventory control is important in production in several ways. First, inventories must be large enough to provide balance in the production line. If some machines operate at different rates from others, one way to overcome these imbalances in production rates is to provide temporary inventories or banks as they are called, between machines.

Second, inventories of raw materials, semi-finished products take up the slack when sales or productions volumes fluctuate. This leads to the third reason that inventory control is important. Inventories tend to provide a smooth flow of production, and this facilitates scheduling.

Finally, inventory control leads to the production and purchasing in economic lot sizes. These economic lot sizes represent the optimum quantity to produce to minimise costs.

2.0 OBJECTIVES

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

- list the importance and objectives of inventory control
- describe how to carry out effective inventory control.

3.0 MAIN CONTENT

3.1 Objectives of Inventory Control

There are several objectives of inventory control. Sometimes compromises must be made in attempting to achieve these goals, since meeting all of them at one time is not possible. The objectives of inventory control are to:

1. minimise investment in inventory.
2. minimise warehousing costs.
3. minimise losses from damage, obsolescence and perish ability.
4. maintain enough inventory so that production does not run out of raw materials, parts, and supplies.
5. maintain efficient transportation of inventories, including the functions of shipping and receiving.
6. maintain an efficient inventory information system
7. supply information on the value of inventory to accounting
8. co-operate with procurement so that efficient and economical purchasing can be accomplished.
9. make forecast of inventory requirements.

3.2 Benefits of Inventory Control

An effective inventory-control system secures numerous benefits as the followings.

1. It assures proper execution of policies covering procurement and use of materials and makes possible rapid shifts in business to meet changes in market conditions.
2. It obtains economies through a reduction in needless variety of items carried in stock.
3. It eliminates delays in production caused by non availability of required materials and tools
4. It avoids over accumulation of inventories and tools, and thereby maintains the minimum investment consistent with production needs and procurement policies

5. It reduces inventory losses caused by inadequacy inspection of incoming materials, damage, deterioration, obsolescence, waste, or theft.
6. It provides "balance-of-store" records to serve as a reliable basis for effective production planning, economical procurement, cost accounting, and preparation of financial reports.

3.3 Procedures for Establishing an Efficient Inventory Control System

1. Determine the place of inventory control in the organisation
2. Develop a method for classifying and identifying inventory
3. Set up and secure control through balance of stores records (perpetual inventory cards) for planning inventory needs and allocating materials, requisitioning purchases, taking physical inventory, and preparing financial statements
4. Establish the steps in the materials control cycle for the regulation of the flow of items from requisitioning procurement to completion of the product
5. Set up procedures for tool procurement and for its control
6. Secure physical control in inventory through an effective system of keeping stores.

The major responsibility for control of inventory should normally be placed in the manufacturing division under the chief of production planning and control. This means that all phases of the inventory-control cycle (requisitioning, procurement, receiving, storage, allocation, processing and replenishing) will have centralised direction, even through the execution of the cycle concerning the purchasing, engineering, inspection, and sales departments.

3.4 Control of Materials

3.4.1 Classification and Identification of Inventory

In order to save time and simplify identification and allocation and control, the various types of inventory should be classified by means of symbols. Indeed, an identification system should be set up for all aspects of the business departments and sections, machines, operations positions, etc.

Types of Inventories

Inventory includes tools, standard supply items, raw materials, goods in process, and finished products. Raw materials are commodities (steel, lumber, asbestos, fabrics) and purchased parts (machined forging and casting such as gears and pistons) that go into the final product. Goods in process are materials that have been partly fabricated but are not yet completed. Finished goods are completed items ready for shipment.

Symbols for Identification

The numeric and mnemonic are common systems of symbolisation for classifying and identifying inventories (including tools). The numeric system identifies and classifies items and subgroups by numbers and decimals. When the system is properly set up, the various digits and decimal positions are significant in designating models, location, sizes, or physical properties. The mnemonic system classifies and identifies items and subgroups by employing letters and numbers which assist the memory. The first letter may designate the general (e.g. "Z" for model, "SA" for Subassembly and "P" for component parts). Stores may also be identified by use of tags, paint colour or distinctive marking.

3.5 Balance of Stores Record (Perpetual Inventory)

The balance of stores records plays the central role in the inventory control systems, particularly in a job-order plan. In essence, it controls the movement of each item as it goes in and out and shows the current balance on hand. Since the record is closely associated with production planning, it is generally best kept by a balance of stores clerk in the production planning office.

a. Perpetual Inventory Form

The store record must be specially designed to serve the needs of the business. A loose-leaf ledger or card is kept for each item in terms of unit quantities (pounds, pieces, or gallons) and usually in terms of monetary value. The date frequently carried on the record include the name and identification of the items, location in storage, rate of consumption, ordering point, ordering quantity, and the following balance columns:

1. *Ordered* - quantity placed on order by purchase requisition
2. *Received* - quantity supplied to the storeroom
3. *Issued* - quantity released to the plant in response to requisitions for materials
4. *Balance on hand* - current quantity and value of stores
5. *Allocated or applied to* - quantity apportioned to a production order but not as yet issued for use in plant
6. *Available* - quantity still available for allocation

b. Ordering Point and Ordering Quantity

To prevent shortage and high costs due to under or over buying and to determine when and how much to order, a minimum quantity (ordering point) and a maximum quantity (ordering quantity) should be established for each item and should be indicated in the stores record. The *ordering point* indicating the minimum quantity which must be kept in stock and thus the time at which the item must be recorded, is determined by the rate of use in production and the time necessary for purchasing or fabricating the item. The *ordering quantity* is determined by striking an economic balance among the following factors that influence procurement costs.

1. Inventory-carrying charges (e.g. storage, insurance, and interest
2. clerical costs of ordering for purchase or for fabrication in the plants
3. Transportation costs
4. Quantity discount on purchases.

The increase in carrying charges accruing from larger ordering quantities must be balanced against the resulting savings in terms of clerical and transportation costs and quantity discounts. The ordering quantity should be periodically revised to meet the financial situation of the company and to meet seasonal fluctuation in production and market trends-rising or falling prices.

4.0 CONCLUSION

In the course of our discussion in this unit, we concluded that inventory management and control have a lot of embedded benefits if properly managed by any organisation. It is therefore important for any organisation in the hospitality sector of the economy to establish a good inventory management and control.

5.0 SUMMARY

This unit focuses on the following areas; the importance and objectives of inventory control and how to carry out effective inventory control.

6.0 TUTOR-MARKED ASSIGNMENT

1. Discuss the benefits of inventory management to any organisation .
2. How can you control material within the scope inventory management?

7.0 REFERENCE/FURTHER READING

Central Bank of Nigeria: *Economic and Financial Review* (Various Issues).

Constitution of the Federal Republic of Nigeria, 1999.

Ocheoha A. O. (1980). *Synthesis of Modern Economics.* Benin City: Ethiope Publishing Corporation.

Synopsis of Policy Analysis and Decision Making Models.Enugu: Amicus – Virgo Academy, 2000.

UNIT 3 THE START UP PROBLEM

CONTENTS

1.0 INTRODUCTION

Given that a man has what he thinks is a unique product or service to offer the market place and a strong desire to be his own boss, how does he proceed to establish himself as the head of a business enterprise? What are the major factors to consider if the business venture is not to end in failure and bankruptcy- as nine out of ten do? What sources of information and outside help are available? Is there a better chance of success from acquiring an on-going business or buying into a franchise chain, rather than starting a new business from the ground up? In this unit, the pitfalls to avoid in starting your own business, Maury Delman discusses these questions, as well as the major reasons for business failures, and lists sources of help in making the initial decisions. Delman's suggestions underscore the necessity of thoroughly understanding the operational and financial considerations involved in starting one's own business.

The entrepreneur will usually experience severe difficulties during his first two years in business. Delivery date must be met, products must be reliable, and bills and employees must be paid. But mainly, the entrepreneur must convince potential customers that his gadget is better and less costly and that his business has a long life expectancy. An obvious requirement is that the entrepreneur must have confidence in his entrepreneurial abilities and be committed to the successful exploitation of his product concept.

To repeat, both his abilities and his strategies must be documented in a business plan that is used as a tool in establishing financial support for the new venture, and as a reference framework with which to compare the future status of the business.

OBJECTIVES

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

- identify some of the pitfalls in starting a new business
- suggest solutions to the identified pitfalls

3.0 MAIN CONTENT

3.1 Pitfalls to Avoid in Starting Your Own Business

U.S. Department of Commerce studies show that about half of new small businesses never make the third year. Retailing suffers the most, with only 29% surviving three-and-a-half years. Wholesales show best with a 48% survival after the same period.

Nevertheless, Dun & Bradstreet figures suggest that more than 400,000 firms are started annually with about an equal number being discontinued.

Survival depends upon a variety of factors. Dun & Bradstreet people have been able to pinpoint nine major reasons for failure of new businesses.

Topping the list is simply lack of managerial experience. Even those who have managed other businesses successfully have come quickly to bankruptcy when operating businesses they knew little about. For example, take the case of a young Pennsylvanian who went into the building business after nine years as an insurance agent. With his cash tied up in real estate and “receivables,” suppliers were willing to sell to him on a cash basis only. He couldn’t buy enough to keep going. After four years, he filled a voluntary petition in bankruptcy with liabilities twice the size of his assets.

A “receivable” is simply money somebody owes you that you can’t get your hand on yet. Experience in selling insurance is hardly a good training for another business that requires buy-sell judgement and heavy day-to-day expenses before the profits roll in. But even with specific experience in some lines there is no assurance of success. The importance of experience is not the time spent but what is learned. Successful businessmen underscore the need for balanced experience. This includes knowledge of your product, financial handling, buying and selling.

Insufficient starting capital ranks just under lack of experience as a cause of all business failures. The notion that a few thousand dollars and very hard work will bring success has held very little validity since the 1930s. An experienced women's-wear retailer says, "anyone going into business now without plenty of capital in back of him should have his head examined." Even if a new business venture should survive its first year with limited capital, this disadvantage takes many years to overcome.

Borrowing the needed capital often seems an easier solution than it is. Those who don't calculate exactly how much the interest on the borrowed money will eat into their expected profits often come to grief-discovering too late that they've only been working for the bank. A man who earns 9% "clear profit" on capital that he borrowed for 9% can have a great time running his own business until he starves to death.

Yet the attractions of being "independent" have been known to induce new "businessmen" to close their eyes to the hard fact that they won't earn a cent for themselves until they have met all operating costs and the interest.

Today, anyone starting a new business must first figure his normal operating expenses plus his salary. For safety, the expense figure should be adjusted upward from 25% to 50%. There are always unforeseen costs. Then, he'll have to determine the volume of business he must do to cover these expenses. The cost of supplies, merchandise, etc., to produce this volume must be figured. Finally, what fixtures are needed and what receivables will have to be carried if credit is granted to customers? In essence, what capital is needed to produce income enough for a reasonable net profit after expenses? A surprising number of people go into business without doing this hard arithmetic.

The third business pitfall is the wrong location. Inexperienced people are prone to look for inexpensive locations. Good locations are bound to cost money but the volume realised from a good location can more than offset the higher rent.

Once a business is under way, it can readily fall victim to the fourth pitfall-inventory mismanagement. The common warning, "don't get too much inventory," should be modified to, "don't buy too much of the wrong merchandise."

The management of inventory is an art, if what you are doing is selling something that you keep in stock. Its ABC's are simply put, even if its XYZ's are not. The dollars you have invested in inventory must earn you money at a desirable rate. Fast turnover will earn money on goods that are priced at a small profit margin. Goods that turn over slowly only pay well if the markup is large. The great inventory tragedy is found in goods that sit on your shelves without buyers. They represent dollars you have invested that are not earning anything-in short, precious capital that's tied up. This is all just as obvious as it can be, but, oh, the businesses that go on the rocks because of ill-judged inventory.

In big successful retail stores there is not love, humanity, sentiment or personal whim in the matter of inventory. The hard questions are: "what sells, at how fast a turnover, for what mark up?" and buyers of stock succeed or fail in their ability to solve that equation most profitably. By contrast, I know of a successful man who quit his profession to invest his all in a store selling a "cultural" product that he thought the people "ought to" have. It bankrupted him because people buy what they want, not what you think they "ought to."

Pitfall five is too much capital going into fixed assets. Any money invested in fixtures or real estate will most likely come from your working capital or will be borrowed. Money tied up in frozen assets that aren't necessary to your business is working capital that may not be available when you need it for either a crisis or an opportunity.

The sixth pitfall is poor credit granting practices. The temptation to let customers "put it on books" can be very strong, particularly if your competition is coming from low-margin, big-volume cash competitors. If you offer easy credit in order to get the business, some customers may be so slow to pay that they'll give you "the business." When you force credit on people you are in danger of attracting the poorer payers. One of the shocks lying in wait for new businessmen is that well-heeled customers are very often the slowest to pay their debts.

In granting credit, two fundamental questions must be answered. Do I have enough capital? Do I know how to collect?

A general rule is that you must have additional capital on hand equal to one-and-a-half month's credit sales in order to give customers 30 days to pay. Credit granting and collecting takes skill. Many people just don't have it. One retailer with 25 years experience commented, "When I first started I also tried to sell on credit but found that I wasn't a good collector, so after several months I made all sales for cash and have since conducted a cash and carry business."

Pitfall number seven is taking too much out for yourself. It's an easy habit to fall into. Many new business starters pledge to themselves, "We are not going to take anything out of the business." And of course they can't stick to it. What's the purpose of going into business if you aren't going to take something out? The approach to what you take out for yourself should be flexible and realistic. When profits decline owners must curtail their drawing.

The eighth pitfall can come from too much success. Business is so good you decide to expand but unplanned expansion can be ruinous. Generally, businesses grow in two ways: slow and steady from within-marked by increased sales and profits, or by rapid expansion through addition or acquisition.

Rapid expansion must be carefully planned since it requires skills to manage new people, you must hire more as you have additional capital. One storekeeper found out the hard way that two stores weren't twice as profitable for him as one. With one store going well he opened another across town. But the managerial help in his second store failed to grasp his successful methods. The owner had to supervise both stores with his wife helping out. When she got sick the load was too much. Eventually, physical and capital strain made him to sell the second store. Today, he operates one store profitably and without undue headaches.

Pitfall number nine-the wrong attitude-ruins many. Some businesses fail to prosper or come to grief because of wrong attitudes of their owners. Being in business is plain hard work, demanding full diligence. Some owners figure that since the business is theirs, they'll work hours only to suit themselves. Others get involved in outside interests to an excessive extent. They may even tell themselves that social and civic interests help promote the business when all they do is take the owner away from affairs that need tending. Greed kills off others. When products are misrepresented or shoddy, it is always found out. A well-known chain of fine restaurants had to be sold off because their owner evaded income taxes. The penalties levied by the internal revenue service in addition to jail sentence forced the sale of that restaurant chain.

But, even with all the hazards, the dream of having your own business can be realised. There are ways to overcome the obstacles and succeed. A prime source of help lies with the federal government through its agency, the small business administration, set up in 1953 to aid small business. The S.B.A. with field offices in principal cities, as well as in Guam and Puerto Rico, is available to assist new business hopefuls as well as established small businesses.

4.0 CONCLUSION

In conclusion, consultancy firms are open for counselling; you need enough information and experience on the business you are going into. An excellent source of information for anyone interested in starting a business is a trade association. Trade associations exist in every major industry and minor ones.

5.0 SUMMARY

The unit has been on the pitfalls to avoid in starting your own business like, lack of managerial skill, lack of experience, insufficient starting capital, wrong location, inventory mismanagement, too much capital going to fixed assets, poor credit granting, taking too much for yourself, the issue of expansion and lastly the wrong attitude. Some solutions were suggested to overcome the pitfalls.

6.0 TUTOR-MARKED ASSIGNMENT

Discuss five pitfalls you might fall into when starting your own business.

7.0 REFERENCES/FURTHER READING

Checklist for going into Business (Management Research Summaries No 120).

Factors in Small Business Success or Failure (Management Research Summaries No. 145).

Starting and Managing a Small Business of Your Own (starting and managing series No 1).

Clifford M. and Joseph R. (1975). *Entrepreneurship and Venture Management.*

UNIT 4 TOTAL QUALITY MANAGEMENT

CONTENTS

1.0 INTRODUCTION

Total Quality Management (TQM) is a philosophy and practice of management which aims to satisfy the customers by means of employee involvement, consistent leadership and continuous improvement. In so doing, it brings together a number of hard and soft technologies of quality management. This paper will examine the fundamental principles of TQM, TQM as a strategic management tool, the concept of TQM, antecedents of modern quality management, quality gurus, accelerating use of TQM, quality and business performance, service quality and product quality, top management commitment, the tools and improvement circle, the metric and the processes, the implementation of performance measurement systems and benchmarking.

2.0 OBJECTIVES

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

- define the concept of (TQM)
- apply the concept of (TQM) to your business

3.0 MAIN CONTENT

3.1 Overview of (TQM)

Total quality management (TQM) is the integration of all functions and processes within an organisation in order to achieve continuous improvement of the quality of goods and services. The goal is customers' satisfaction.

Of all the management issues faced in the last decade, none has had the impact of or caused as much concern as quality in American products and services. A report by the Conference Board indicates that senior executives in the United States agreed that the banner of total quality is essential to ensure competitiveness in global markets. Quality expert J. M. Juran calls it a major phenomenon in this age. This concern for quality is not misplaced.

The interest in quality is due, in part, to foreign competition and the trade deficit. Analysts estimate that the vast majority of U.S. businesses will continue to face strong competition from the Pacific Rim and the European Economic Community for the remainder of the 1990s and beyond. This comes in the face of a serious erosion of corporate America's ability to compete in global markets over the past 20 years.

As we come to the end of the 20th century, the competitive and trade deficit problems are compounded by the weakening situation in Asian and other global markets. To compete in these markets may require additional efforts in both cost reduction and quality.

3.2 The Concept of TQM

TQM is based on a number of ideas. It means thinking about quality in terms of all functions of the enterprise and is a start-to-finish process that integrates interrelated functions at all levels. It is a systems approach that considers every interaction between the various elements of the organisation. Thus, the overall effectiveness of the system is higher than the sum of the individual outputs from the subsystems. The subsystems include all the organisational functions in the life cycle of a product, such as:

1. design
2. planning
3. production
4. distribution
5. field service.

The management subsystems also require integration, including:

1. strategy with a customer focus
2. the tools of quality
3. employee involvement (the linking process that integrates the whole).

A corollary is that any product, process, or service can be improved, and a successful organisation is one that consciously seeks and exploits opportunities for improvement at all levels. The load bearing structure is customer satisfaction. The watchword is continuous improvement.

The Conference Board has summarised the key issues and terminology related to TQM:

- The *cost of quality* as the measure of non-quality (not meeting customer requirements) and a measure of how the quality process is progressing.

- A *cultural change* that appreciates the primary need to meet customer requirements, implements a management philosophy that acknowledges this emphasis, encourages employee involvement, and embraces the ethics of continuous improvement.

- *Enabling mechanisms of change*, including training and education, communication, recognition, management behaviour, teamwork, and customer satisfaction programs.

- *Implementing TQM* by defining the mission, identifying the output, identifying the customers, negotiating customer requirements, developing a "supplier specification" that details customer objectives, and determining the activities required to fulfil those objectives.

- *Management behaviour* that includes acting as role models, use of quality processes and tools, encouraging communication, sponsoring feedback activities, and fostering and providing a supporting environment.

3.2.1 Antecedents of Modern Quality Management

Quality control as we know it probably had its beginnings in the factory system that developed following the industrial revolution. Production methods at that time were rudimentary at best. Products were made from non-standardised materials using non-standardised methods. The result was products of varying quality. The only real standards used were measures of dimensions, weight, and in some instances purity. The most common form of quality control was inspection by the purchaser, under the common-law rule of caveat emptor.

Much later, around the turn of this century, Frederick Taylor developed his system of scientific management, which emphasised productivity at the expense of quality. Centralised inspection departments were organised to check for quality at the end of the production line. An extreme example of this approach was the Hawthorne Works at Western Electric Company, which at its peak in 1928 employed 40,000 people in the manufacturing plants, 5200 of whom were in the inspection process. Most involved visual inspection or testing of the product following manufacture. Methods of statistical quality control and quality control and quality assurance were added later. Detecting manufacturing problems was the overriding focus. Top management moved away from the idea of managing to achieve quality, and furthermore, the work force had no stake in it. The concern was limited largely to the shop floor.

Traditional quality control measures were (and still are) designed as defense mechanisms to prevent failure or eliminate defects. Accounts were taught (and are still taught) that expenditures for defect prevention were justified only if they were less than the cost of failure. Of course, cost of failure was rarely computed.

Following World War II, the quality of products produced in the United States declined as manufacturers tried to keep up with the demand for non-military goods that had not been produced during the war. It was during this period that a number of pioneers began to advance a methodology of quality control in manufacturing and to develop theories and practical techniques for improved quality. The most visible of these pioneers were W. Edwards Deming, Joseph M. Juran, Armand V. Feigenbaum, and Philip Crosby. It was a great loss to the quality movement when Deming died in December 1993 at the age of 93.

3.2.2 The quality Gurus

Deming, the best known of the “early” pioneers, is credited with popularising quality control in Japan in the early 1950s. Today, he is regarded as a national hero in that country and he is the father of the world-famous Deming Prize for quality. He is best known for developing a system of statistical quality control, although his contribution goes substantially beyond those techniques. His philosophy begins with top management but maintains that company must adopt the 14 points of his system at all levels. He also believes that quality must be built into the product at all stages in order to achieve a high level of excellence. While it cannot be said that Deming is responsible for quality improvement in Japan or the United States, he has played a substantial role in increasing the visibility of the process and advancing an awareness of the need to improve.

Deming defines quality as a predictable degree of uniformity and dependability, at low costs and suited to the market. Deming teaches that 96 percent of variations have common causes and 4 percent have special causes. He views statistics as a management tool and relies on statistical process control as a means of managing variations in a process. Deming develops what is known as the Deming chain reaction; as quality improves, costs will decrease and productivity will increase, resulting in more jobs, greater market share, and long-term survival. Although it is the worker who will ultimately produce quality products, Deming stresses workers pride and satisfaction rather than the establishment of quantifiable goals. His overall approach focuses on improvement of the process, in that the system, rather than the worker, is the cause of process variation.

Deming's universal 14 points for management are summarised as follows:

1. **Create consistency of purpose with a plan.** The objective is constancy of purpose for continuous improvement. An unwavering commitment to quality must be maintained by management. Quality, not short-term profit, should be at the heart of organisational purpose. Profit will follow when quality becomes the objective and purpose.

2. **Adopt the new philosophy of quality.** The modern era demands ever increasing quality as a means of survival and global competitiveness. Inferior material, poor workmanship, defective products, and poor service must be rejected. Reduction of defects is replaced by elimination of defects. The new culture of quality must reflect a commitment to quality and must be supported by all employees.

3. **Cease dependence on mass inspection.** Quality cannot be inspected during production, it must be built in from the start. Defects discovered during inspection cannot be avoided - it is too late; efficiency and effectiveness have been lost, as has continuous process improvement. Continuous process improvement reduces costs incurred by correcting errors that should not have been made in the first place.

4. **End the practice of choosing suppliers based on price.** Least cost is not necessarily the best cost. Buying from a supplier based

on low cost rather than a quality/cost basis defeats the need for a long-term relationship. Vendor quality can be evaluated with statistical tools.

5. **Identify problems and work continuously to improve the system.** Continuous improvement of the system requires seeking out methods for improvement. The search for quality improvement is never ending and results from studying the process itself, not the defects detected during inspection should be noted.

6. **Adopt modern methods of training on the job.** Training involves teaching employees the best methods of achieving quality in their jobs and the use of tools such as statistical quality control.

7. **Change the focus from production numbers (quantity) to quality.** The focus on volume of production instead of quality leads to defects and rework that may result in inferior products at higher costs.

8. **Drive out fear.** Employees need to feel secure in order for quality to be achieved. Fear of asking questions, reporting problems, or making suggestions will prevent the desired climate of openness.

9. **Break down barriers between departments.** When employees perceive themselves as specialists in one function or department without too much regard for other areas, it tends to promote a climate of parochialism and set up barriers between departments. Quality and productivity can be improved when there is open communication and coordination based on the common organisation goals.

10. **Stop requesting improved productivity without providing such methods to achieve it.** Continuous improvement as a general goal should replace motivational or inspirational slogans, sign, exhortations, and work force targets. The major cause of poor productivity and quality is the management systems, not the work force. Employees are frustrated when exhorted to achieve results that management systems prevent them from achieving.

11. **Eliminate work standards that prescribe numerical quotas.** Focus on quotas, like a focus on production, may encourage and reward people for numerical targets, frequently at the expense of quality.

12. **Remove barriers to pride of workmanship.** A major barrier to pride of workmanship is a merit or appraisal system based on targets, quotas, or some list of personal traits that have little to do with incentives related to quality. Appraisal systems that attempt to coerce performance should be replaced by systems that attempt to overcome obstacles imposed by inadequate material, equipment, or training.

13. **Institute vigorous education and retraining.** Deming emphasises training, not only in the methods of the specific job but in the tools and techniques of quality control, as well as instruction in teamwork and the philosophy of a quality culture.

14. **Create a structure in top management that will emphasise the preceding 13 points everyday.** An organisation that wants to establish a culture based on quality needs to emphasise the preceding 13 points on a daily basis. This usually requires a transformation in management style and structure. The entire organisation must work together to enable a quality culture to succeed.

3.3 Juran's ten steps

Juran, like Deming, was invited to Japan in 1954 by the union of Japanese Scientists and Engineers (J U S E). His lectures introduced the managerial dimensions of planning, organising, and controlling and focused on the responsibility of management to achieve quality and the need for setting goals. Juran defines quality as fitness for use in terms of design, conformance, availability, safety, and field use. Thus, his concept more closely incorporates the point of view of the customer. He is prepared to measure everything and relies on systems and problem-solving techniques. Unlike Deming, he focuses on top – down management and technical methods rather than worker pride and satisfaction.

Juran's ten steps to quality improvement are:

1. Build awareness of opportunities to improve.
2. Set goals for improvement.
3. Organise to reach goals.
4. Provide training.
5. Carry out projects to solve problems.
6. Report progress.
7. Give recognition.
8. Communicate results.

9. Keep score.
10. Maintain momentum by making annual improvement part of the regular systems and processes of the company.

Juran is the founder of the Juran Institute in Wilton, Connecticut. He promotes a concept known as Managing Business Process Quality, which is a technique for executing cross-functional quality improvement. Juran‘s contribution may, over the longer term, be greater than Deming’s because Juran has the broader concept, while Deming’s focus on statistical process control is more technically oriented.

Armand Feigenbaum, like Deming and Juran, achieved visibility through his work with the Japanese. Unlike the latter two, he used a total quality control approach that may very well be the forerunner of today’s TQM. He promoted a system for integrating efforts to develop, maintain, and improve quality by the various groups in an organisation. To do otherwise, according to Feigenbaum, would be to inspect for and control quality after the fact rather than build it in at an earlier stage of the process.

4.0 CONCLUSION

Total quality control cannot be overemphasised in any organisation. Starting a business may be fine but what about continuity? To keep your business going, you must ensure proper quality management.

5.0 SUMMARY

I will summarise these in the words of Philip Crosby.

Philip Crosby, author of the popular book *Quality is Free,* may have achieved the greatest commercial success by promoting his views and founding the Quality College in Winter Park, Florida. He argues that poor quality in the average firm costs about 20 percent of revenues, most of which could be avoided by adopting good quality practices. His “absolutes” of quality are:

- Quality is defined as conformance to requirements, not “goodness”.
- The system for achieving quality is prevention, not appraisal.
- The performance standard is zero defects, not “that’s close enough.”
- The measurement of quality is the price of non-conformance, not indexes.

6.0 TUTOR-MARKED ASSIGNMENT

Describe the steps to be taken to achieve total quality management

7.0 REFERENCES/FURTHER READING

John S. Oakland, (1998). *"Total Quality Management"*. Butterworth:Heinemann Publisher, UK.

Bank, J. (1992). *The Essence of Total Quality Management.* Prentice Hall: Hemel Hempstead (UK).

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UNIT 5 QUALITY AUDIT AND MEASUREMENT

CONTENTS

1.0 INTRODUCTION

Securing prevention by audit and review of the system

Error or defect prevention is the process of removing or controlling error/defect causes in the system. There are two major elements of this:

- checking the system.
- error/defect investigation and follow-up

These have the same objectives – to find, record and report possible causes of error and to recommend future corrective action.

Checking the system

There are six methods in general use:

a. *Quality audits and reviews*, which subject each area of an organisation's activity to a systematic critical examination. Every component of the total system is included, i.e., quality policy, attitudes, training process, decision features, operating procedures, documentation. Audits and reviews, as in the field of accountancy, aim to disclose the strengths and weaknesses and the main areas of vulnerability or risk.

b. *Quality survey,* a detailed, in-depth examination of a narrower field of activity, i.e. major key areas revealed by quality audits, individual plants, procedures or specific problems common to an organisation as a whole.

c. *Quality inspection*, which takes the form of a routine scheduled inspection of a unit or department. The inspection should check standards, employee involvement and working practices, and that work is carried out in accordance with the procedures, etc.

d. *Quality tour,* which is an unscheduled examination of a work area to ensure that, for example, the standards of operation are acceptable, obvious causes of errors are removed, and in general quality standards are maintained.

e. *Quality sampling*, which measures by random sampling, similar to activity sampling, the potential error. Trained observers perform short tours of specific locations by prescribed routes and record the number of potential errors or defects seen. The results may be used to portray trends in the general quality situation.

f. *Quality scrutiny,* which is the application of a formal, critical examination of the process and technological intentions for new or existing facilities, or to assess the potential for mal-operation or malfunction of equipment and the consequential effects of quality.

OBJECTIVES

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

- detect errors during investigations and follow up
- differentiate internal and external quality-system audits and reviews
- state TQM standard for self-assessment.

3.0 MAIN CONTENT

3.1 Error or Defect Investigations and Follow-up

The investigation of errors and defects can provide valuable error prevention information. The method is based on:

- collecting data and information relating to the error or defect.
- checking the validity of the evidence.

- selecting the evidence without making assumptions or jumping to conclusions.

The results of the analysis are then used to:

- decide the most likely cause(s) of the errors or defects.
- notify immediately the person(s) able to take corrective action.
- record the findings and outcomes.
- report them to everyone concerned, to prevent a recurrence.

The investigation should not become an inquisition to apportion blame, but focus on the positive prevention aspects.

3.2 Internal and External Quality-System Audits and Reviews

A good quality system will not function without adequate audits and reviews. The system reviews, which need to be carried out periodically and systematically, are conducted to ensure that the system achieves the required effect, while audits are carried out to make sure that actual methods are adhering to the documented procedures. The reviews should use the findings of the audits, for failure to operate according to the plan often signifies difficulties in doing so. A re-examination of the procedures actually being used may lead to system improvements unobtainable by other means.

A schedule for carrying out the audits should be drawn up, different activities perhaps requiring different frequencies. All procedures and systems should be audited at least once per year. There must be, however, a facility to adjust this on the basis of the audit results.

A quality-system review should be instituted, perhaps every 12 months, with the aims of:

- ensuring that the system is achieving the desire results.
- revealing defects or irregularities in the system.
- indicating any necessary improvements and/or corrective actions to eliminate waste or loss.
- checking on all levels of management.
- uncovering potential danger areas.
- verifying that improvements or corrective action procedures are effective.

Clearly, the procedures for carrying out the audits and reviews and the results from them should be documented, and be subject to review.

The assessment of a quality system against a particular standard or set of requirements by internal audit and review is known as a first-party assessment or approval scheme. If an external customer makes the assessment of a supplier against his own or a national or international standard, a second-party scheme is in operation. The external assessment by an independent organisation not connected with any contract between customer and supplier, but acceptable to them both, is known as an independent third-party assessment scheme. The latter usually results in some forms of certification or registration by the assessment body.

One advantage of the third-party schemes is that they obviate the need for customers to make their own detailed checks, saving both suppliers and customers time and money, and avoiding issues of commercial confidentiality. Just one knowledgeable organisation has to be satisfied, rather than multitude with varying levels of competence. This method often certifies suppliers for quality assurance based contracts without further checking.

Each certification body usually has its own recognised mark, which may be used by registered organisations of assessed capability in their literature, letter headings, and marketing activities. There are also publications containing lists of organisations whose quality systems and/or products and services have been assessed. To be of value, the certification body must itself be recognised and, usually, assessed and registered with a national or international accreditation scheme, such as the National Accreditation Council for Certification Bodies (NACCB) in the UK.

Many organisations have found that the effort of designing and implementing a written quality system good enough to stand up to external independent third-part assessment has been extremely rewarding in:

- encouraging staff and improving morale.
- better process control.
- reduced wastage.
- reduced customer service costs.

This is also true of those organisations that have obtained third-party registrations and simply companies that still insist on their own second-party assessment. The reason for this is that most of the standards on quality systems, whether national, international, or company-specific, are now very similar indeed. A system that meets the requirements of the ISO 9000 series will meet the requirements of all other standards, with only the sight modifications and small emphasis here and there required for specific customers. It is the author's experience, and that of his immediate colleagues, that an assessment carried out by one of the independent certified assessment bodies is at least as rigorous and delving as any carried out by a second-part representative.

Internal system audits and reviews must be positive, and conducted as part of the preventive strategy and not be carried out only before external audits, nor should they be left to the external auditor – whether second or third party. An external auditor discovering discrepancies between actual and documented systems will be inclined to ask why the internal review methods did not discover and correct them. As this type of behaviour in financial control and auditing is commonplace, why should things be different in the control quality?

Managements, anxious to display that they are serious about quality must become fully committed to operating an effective quality system for all personnel within the organisation, not just the staff in the quality department. The system must be planned to be effective and achieve its objectives in an uncomplicated way. Having established and documented the procedures, an organisation must ensure that they are working and that everyone is operating in accordance with them. The system once established is not static; it should be flexible, to enable the constant seeking of improvements or streamlining.

3.3 Quality Auditing Standard

There is a British and International Standard Guide to quality-systems auditing (BS 7229, ISO 10011: 1991). This points out that audits are required to verify whether the individual elements making up quality systems are effective in achieving the stated objectives. The growing use of standards internationally emphasises the importance of auditing as a management tool for this purpose. The guidance provided in the standard can be applied equally to any one of the three specific and yet different auditing activities:

a. First-party or internal audits, carried out by an organisation on its own systems, either by staff who are independent of the systems being audited, or by an outside agency.
b. Second-party audits, carried out by one organisation (a purchaser or its outside agent) on another with which it either has contracts to purchase goods or services or intend to do so.
c. Third-party audits, carried out by independent agencies, to provide assurance to existing and prospective customers for the product or service.

ISO 10011 (BS 7229) over audit objectives and responsibilities, including the roles of auditors and their independence, and those of the 'client'. It provides the following detailed guidance on audit.

- Initiation, including its scope and frequency..
- Preparation, including review of documentation, the programme, and working documents.
- Execution, including the opening meeting, examination and evaluation, collecting evidence, observations, and closing the meeting with the auditee.
- Report, including its preparation, content and distribution.
- Completion, including report submission and retention.

Attention is given at the end of the standard to corrective action and follow-up, where it is stressed that the improvement process should be continued by the client for a verification audit of the implementation of any corrective actions specified.

4.0 CONCLUSION

There have been many recent developments and there will continue to be many more, in the search for a TQM standard or framework against which organisations may be assessed or measure themselves, and carry out the so-called 'gap analysis'. To many companies, the ability to judge their TQM progress against an accepted set of criteria would be most valuable and informative.

5.0 SUMMARY

- Investigations proceed by collecting, checking and selecting data, and analysing it by deciding causes, notifying people, recording and reporting findings and outcomes.
- A good quality system will not function without adequate audits and reviews.
- System assessment by internal audit and review is known as first-party, by external customer as second-party, and by an independent organisation as third-party certification.

6.0 TUTOR-MARKED ASSIGNMENT

Discuss the internal quality-system audits

7.0 REFERENCES/FURTHER READING

John S. Oakland, (1998). *Total Quality Management.* Butterworth:Heinemann Publisher, UK.

Bank, J. (1992). T*he Essence of Total Quality Management*. Prentice Hall: Hemel Hempstead UK.