

# **NCERT SOLUTIONS For Class 11 Business Studies**

## **<http://freehomedelivery.net/Solutions> Chapter 1 Nature and Purpose of Business**

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#### **I. Multiple Choice Questions**

**Question 1. Which of the following does not characterise business activity?**

- (i) Production of goods and services**
- (ii) Presence of risk**
- (iii) Sale or exchange of goods and services**
- (iv) Salary or wages**

**Question 2. Which of the broad categories of industries covers oil refinery and sugar mills?**

- (i) Primary (ii) Secondary**
- (iii) Tertiary (iv) None of them**

**Question 3. Which of the following cannot be classified as an auxiliary to trade?**

- (i) Mining (ii) Insurance**
- (iii) Warehousing (iv) Transport**

**Question 4. The occupation in which people work for others and get remunerated in return is known as**

- (i) Business (ii) Employment**
- (iii) Profession (iv) None of them**

**Question 5. The industries which provide support services to other industries are known as**

- (i) Primary industries (ii) Secondary industries**
- (iii) Commercial industries (iv) Tertiary industries**

**Question 6. Which of the following cannot be classified as an objective of business?**

- (i) Investment (ii) Productivity**
- (iii) Innovation (iv) Profit earning**

**Question 7. Business risk is not likely to arise due to**

- (i) Changes in government policy (ii) Good management**
- (iii) Employee dishonesty (iv) Power failure**

**Answer:** 1. (iv) 2. (i) 3. (i) 4. (ii) 5. (iv) 6. (i) 7. (ii)

#### **II. Short Answer Type Questions**

**Question 1. State the different types of economic activities.**

**Answer:** Different types of economic activities are of three types:

1. Business refers to those economic activities which are concerned with the production or purchase and sale of goods or supply of services with the main object of earning profits.
2. Profession refers to those activities which require special knowledge and skill to be applied by individuals in their occupations.
3. Employment refers to the occupation in which people work for others and get remunerated in return.

### Question 2. Why is business considered an economic activity?

**Answer:** Any activity is called an economic activity when it is done with a view to earning money. The motive of a business is to earn profit primarily. However, there are some other objectives as well like increasing market share, improvement in productivity, employee satisfaction, consumer satisfaction, social objectives but the main and basic objective of a business is to make profits. Therefore, it is called economic activity.

### Question 3. Explain the concept of business.

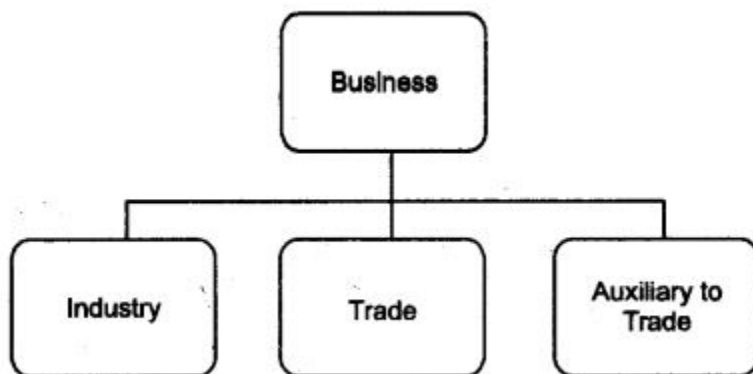
**Answer: Business:** An economic activity involving the production and sale of goods and services undertaken with a motive of earning profit by satisfying human needs in society is called business.

#### Characteristics of Business:

1. **Economic activity:** All business activities are economic activities and are done for the sole purpose of earning money.
2. **Production and procurement of goods and services:** A business activity involves production or procurement of goods and services. A manufacturer is involved in production, while a shopkeeper is involved in procurement.
3. **Sale and exchange of goods and services for the satisfaction of human needs:** Sale and exchange of goods and services is done to satisfy human needs.
4. **Dealing in goods and services on a regular basis:** One time dealing in goods or services cannot be termed as a business. The business should happen on a regular basis.
5. **Profit earning:** Profit earning is the fundamental motive of doing a business. Other motives are there but they depend on profit motive.
6. **Uncertainty of returns:** Returns can never be certain in business activity. This happens because of external factors which are outside the control of the business organization.
7. **Element of risk:** An element of risk is always present in business activity.

### Question 4. How would you classify business activities?

**Answer:** Business activities can be classified in the following ways:



#### I. Industry: Different types of industries are as follows:

1. **Primary Industry:** The primary industry includes those activities through which the natural resources are used to provide raw materials to other industries. Primary industries are of two types.
2. **Secondary Industry:** Under this industry new products are manufactured by using the previously produced things e.g., producing cotton is a primary industry and manufacturing cloth out of cotton is a secondary industry. It is of two types.
3. **Tertiary or Service Industry:** It includes those services which help business to move smoothly e.g. transport, bank, insurance, storage and advertising.

**II. Commerce:** Commerce refers to all those activities which are concerned with the transfer of goods and services from the producers to the consumers. It embraces all those activities which are necessary for maintaining a free flow of goods and services. It includes trade and auxiliary to. trade. Trade refers to buying and selling of goods and services with the objective of earning profit. It is classified into two categories.

1. **Internal Trade:** It takes place within a country. Internal trade is classified into two categories—retail trade and wholesale trade.
2. **Retail Trade:** It refers to buying of goods and services in relatively small quantities and selling them to the ultimate consumers.
  - (a) **External Trade:** It happens between two or more countries. External trade can be classified into three categories.
  - (b) **Import Trade:** If goods are purchased from another country, it is called import trade.
  - (c) **Export Trade:** If goods are sold to other countries it is called export trade.
  - (d) **Entrepot Trade:** Goods are imported for export to other countries e.g. Indian firm may import some goods from America and export the same goods to Nepal.

**III. Auxiliaries to Trade:** All those activities which help in removing various hindrances which arise in connection with the production and distribution of goods are called auxiliaries to trade. An overview of these activities is given below:

1. **Transportation and Communication:** The production of goods takes place at one place whereas these are demanded in different parts of the country. The obstacle of place is removed by the transport. Along with transport, communication is also an important service. It helps in exchange of information between producers, consumers and traders. The common communication services are postal service, telephone, fax, internet etc.
2. **Banking and Finance:** Business needs funds for acquiring assets, purchasing raw materials and meeting other expenses. Necessary funds can be obtained from a bank.
3. **Insurance:** It provides a cover against the loss of goods, in the process of transit, storage, theft, fire and other natural calamities.
4. **Warehousing:** There is generally a time lag between the production and consumption of goods. This problem can be solved by storing the goods in warehouses.
5. **Advertising:** Advertising brings goods and services to the knowledge of prospective buyers. It is through advertising that the customers come to know about the new products and their utility.

#### **Question 5. What are various types of industries?**

**Answer:** Different types of industries are as follows:

**1. Primary Industry:** The primary industry includes those activities through which the natural resources are used to provide raw materials to other industries. Primary industries are of two types.

- **Extractive:** It refers to those industries under which something is extracted out of the earth, water or air e.g., coal, iron, gas etc.
- **Genetic:** It refers to those industries under which the breed of animals and vegetables are improved and made more useful e.g., poultry farms, tree planting etc.

**2. Secondary Industry:** Under this industry, new products are manufactured by using the previously produced things e.g., producing cotton is a primary industry and manufacturing cloth out of cotton is a secondary industry. It is of two types.

- **Manufacturing:** These industries convert raw materials or semi finished products into finished products e.g., paper from bamboo, sugar from sugar cane. It is further being divided into four parts.
- **Analytical:** Different things are manufactured out of one thing e.g., petrol, diesel, gasoline out of crude oil.
- **Processing:** Those industries wherein useful things are manufactured by making the raw material to pass through different production process e.g., steel from iron ores.
- **Synthetic:** Many raw materials are mixed to produce more useful product e.g., paints, cosmetics etc.
- **Assembling:** The parts manufactured by different industries are assembled to produce new and useful product e.g., computers, watches etc.
- **Construction Industry:** Such types of industries constructions of roads, bridges, buildings etc. are covered.

**3. Tertiary or Service Industry:** It includes those services which help business to move smoothly e.g. transport, bank, insurance, storage and advertising.

**Question 6. Explain any two business activities which are auxiliaries to trade.**

**Answer:** Two business activities which are auxiliary to trade are explained below:

1. **Transportation and Communication:** The production of goods takes place at one place whereas these are demanded in different parts of the country. The obstacle of place is removed by the transport. Along with transport, communication is also an important service. It helps in exchange of information between producers, consumers and traders. The common communication services are postal service, telephone, fax, internet etc.
2. **Banking and Finance:** Business needs funds for acquiring assets, purchasing raw materials and meeting other expenses. Necessary funds can be obtained from a bank. Finance is the life blood of any business. We cannot think of any business which does not need finance and providing finance to other businesses become another business. Finance is also required for consumption purposes.

**Question 7. What is the role of profit in business?**

**Answer:** Profits play a vital role in any business. Earning of profits is essential for any business because of the following reasons given below:

- **Means of Livelihood:** Profits act as a means of livelihood for the entrepreneurs. Without profits, entrepreneurs cannot continue with the business.
- **Rewards for taking risks:** It provides returns for taking risks.
- **Funds for Growth:** It would provide funds for growth of the business.
- **Symbolic of efficiency and efficacy:** Profits symbolise that management is efficient and business is operating in a healthy manner.
- **Enhancement in goodwill:** A business making higher profits has a better goodwill and reputation in the market.

**Question 8. What is business risk? What is its nature?**

**Answer:** The term business risk refers to possibility of inadequate profits or even losses due to uncertainties e.g., changes in tastes and preferences of consumers, strike, increased competition, change in Government policy etc. These are of two types—speculative and pure.

**Nature of Business Risks**

1. **Business risks arise due to uncertainties:** Natural calamities, change in demand and prices, change in technology etc. are some of the examples of uncertainty which create risks.
2. **Risk is an essential part of every business:** No business can avoid risk. Risk can be minimised but cannot be eliminated.
3. **Degree of risk depends mainly upon the nature and size of business:** For small scale business it is less and for large scale business it is more.
4. **Profit is the reward for risk taking:** An entrepreneur assumes risks and in consideration he gets reward which is called profit. Greater the risk higher is the chance of profit.

### III. Long Answer Type Questions

**Question 1. Explain the characteristics of business.**

**Answer:** Characteristics of business are as follows:

1. **An economic activity:** All business activities are economic activities and are done for the sole purpose of earning money.
2. **Production and procurement of goods and services:** A business activity involves production or procurement of goods and services. A manufacturer is involved in production, while a shopkeeper is involved in procurement.
3. **Sale and exchange of goods and services for the satisfaction of human needs:** Sale and exchange of goods and services is done to satisfy human needs.
4. **Dealing in goods and services on a regular basis:** One time dealing in goods or services cannot be termed as a business. The business should happen on a regular basis.
5. **Profit earning:** Profit earning is the fundamental motive of doing a business. Other objectives cannot be attained without it.
6. **Uncertainty of returns:** Returns can never be certain in business activity. This happens because of external factors which are outside the control of the business organization.
7. **Element of risk:** An element of risk is always present in business activity.

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**Question 2. Compare business with profession and employment.**

**Answer:** Business has been compared with profession and employment in tabular form given below:

<b>Basis of Distinction</b>	<b>Business</b>	<b>Profession</b>	<b>Employment</b>
<b>Mode of Establishment</b>	Starts after completing some legal formalities if needed.	Membership of a professional body and certificate of practice required.	Start after getting appointment letter.
<b>Qualification</b>	No minimum qualification is necessary.	Professional qualification and training required.	Qualification and training required prescribed by the employer.
<b>Capital Investment</b>	Capital needed according to nature and size of business.	Limited capital for establishment.	No capital required.
<b>Risk</b>	It involves high risk.	The degree of risk is low.	No risk in it.
<b>Code of conduct</b>	No code of conduct.	Professional code of conduct is to be followed.	The terms and conditions of service contract are to be followed.
<b>Nature of work</b>	Provision of goods and services to the public.	Personalized services of expert nature.	Work allotted by the employee according to the contract.
<b>Reward/Return</b>	Profits.	Professional Fee.	Salary or wage.

**Question 3. Explain with examples the various types of industries.**

**Answer:** Different types of industries are as follows:

- Primary industry:** Primary industry includes all those activities, which are connected with extraction and production of natural resources and reproduction and development of living organisms, plants, etc. Primary industries are of two types.
  - Extractive:** It refers to those industries under which something is extracted out of the earth, water or air. e.g., coal, iron, gas etc.
  - Genetic:** It refers to those industries under which the breed of animals and vegetables are improved and made more useful e.g., poultry farms, tree planting etc.
- Secondary Industry:** Secondary industry includes all those activities, which are connected with using the materials, which have already been extracted at the primary stage. It is of two types.
  - Manufacturing:** These industries convert raw materials or semi finished products into finished products, e.g., paper from bamboo, sugar from sugar cane. It has further been divided into four parts.
  - Analytical:** Different things are manufactured out of one thing e.g., petrol, diesel, gasoline out of crude oil.

- **Processing:** Those industries wherein useful things are manufactured by making the raw material to pass through different production processes e.g., steel from iron ores.
  - **Synthetic:** Many raw materials are mixed to produce more useful product e.g., paints, cosmetics etc.
  - **Assembling:** The parts manufactured by different industries are assembled to produce new and useful product e.g., computers, watches etc.
  - **Construction Industry:** Such type of industries include construction of roads, bridges, buildings etc.
3. **Tertiary or Service Industry:** Tertiary industry includes all those activities, which are concerned with providing support services to primary and secondary industries as well as activities relating to trade. It includes banking, finance, insurance, communication, transportation etc.

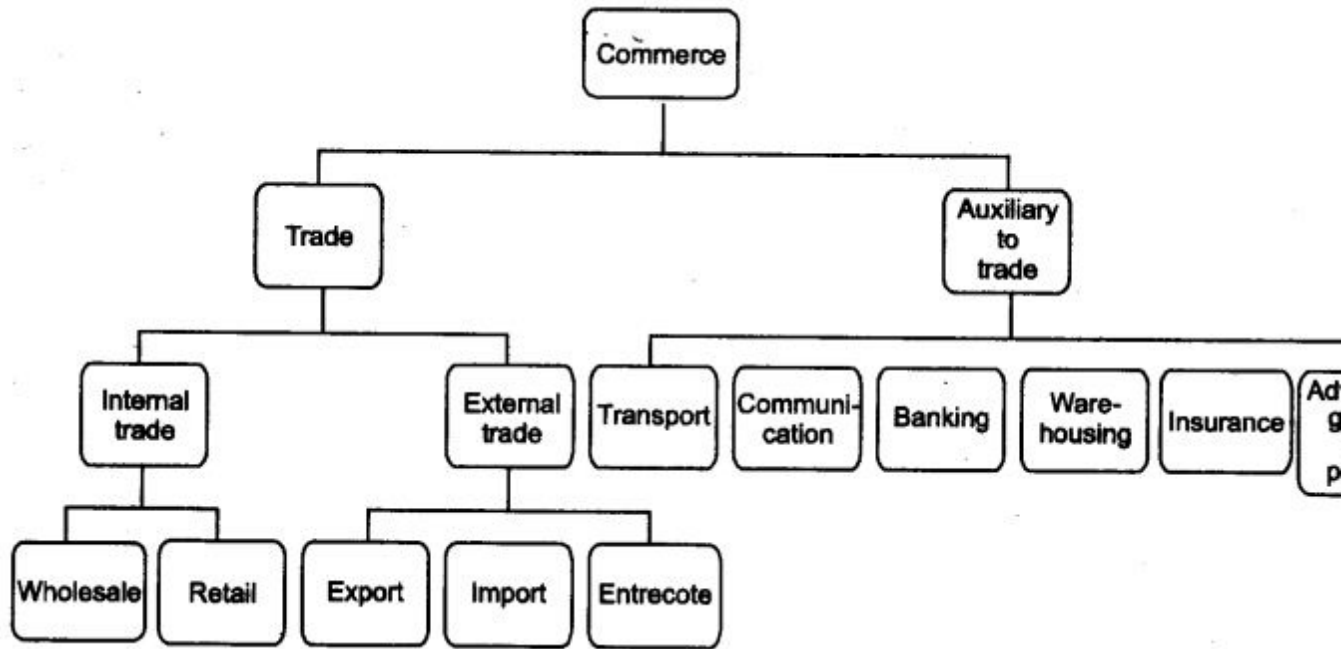
#### Question 4. Describe the activities relating to commerce.

**Answer:** Commerce refers to all , those activities which are concerned with the transfer of goods and services from the producers to the consumers. It embraces all those activities which are necessary for maintaining a free flow of goods and services. It includes trade and auxiliary to trade.

Commerce = Trade + Auxiliary to Trade

1. **Trade:** Trade refers to buying and selling of goods and services with the objective of earning profit. It is classified into two categories.
  - **Internal Trade:** It takes place within a country. Internal trade is classified into two categories retail trade and wholesale trade.
  - **Retail Trade:** It refers to buying of goods and services in relatively small quantities and selling them to the ultimate consumers.
  - (a) **External Trade:** It is done between two or more countries. External trade can be classified into three categories.
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  - (d) **Entrecote Trade:** Where goods are imported for export to other countries e.g., Indian firm may import some goods from America and export the same goods to Nepal.
2. **Auxiliaries to Trade:** All those activities which help in removing various hindrances which arise in connection with the production and distribution of goods are called auxiliaries to trade. An overview of these activities is given below.
  - **Transportation and Communication:** The production of goods takes place at one place whereas these are demanded in different parts of the country. The obstacle of place is removed by the transport. Along with transport, communication is also an important service. It helps in exchange of information between producers, consumers and traders. The common communication services are postal service, telephone, fax, internet etc.
  - **Banking and Finance:** Business needs funds for acquiring assets, purchasing raw materials and meeting other expenses. Necessary funds can be obtained from a bank.
  - **Insurance:** It provides a cover against the loss of goods, in the process of transit, storage, theft, fire and other natural calamities.
  - **Warehousing:** There is generally a time lag between the production and consumption of goods. This problem can be solved by storing the goods in warehouses.
  - **Advertising:** Advertising brings goods and services to the knowledge of prospective buyers. It is through advertising that the customers come to know about the new

products and their utility.



**Question 5. Why does business need multiple objectives? Explain any five such objectives.**

**Answer:** Since a business has to balance a number of needs and goals, it requires multiple, objectives.

Business is dependent on many people's satisfaction whose objectives for being involved in it are different and many times conflicting. Owners want profits, employees want good working conditions and remuneration, investors want good return and consumers want good quality product. Therefore, a business needs to have multiple objectives. Some of these objectives are given below:

- **Market standing:** Business can survive for a longer period only if it is able to capture a big share in the market and has market standing.
- **Innovation:** It means developing new products and their multiple uses. Old customers can be maintained and new can be attracted by innovation only.
- **Improving productivity:** Every business enterprise must aim at greater productivity by making optimum use of available resources.
- **Earning profit:** One of the objectives of business is to earn profits on the capital invested. Every business must earn a reasonable profit to survive and grow.
- **Optimum use of physical and financial resources:** Every business requires physical (plant, machine, office etc) and financial resources (money or funds) to produce goods and services; the business enterprise must aim to use them efficiently.
- **Workers performance and attitude:** Every business enterprise must aim at improving its workers performance and creating positive attitudes towards workers. It will boost the morale of the employees.
- **Social Responsibility:** A business is a part of society and so it must meet the expectations of the society. It can set goals in the areas of the environmental protection, supply of desired quality of products, employment generation etc.

**Question 6. Explain the concept of business risk and its causes.**

**Answer:** The term 'business risk' refers to possibility of inadequate profits or even losses due to uncertainties e.g., changes in tastes and preferences of consumers, strike, increased competition,



change in Government policy etc. These are of two types: speculative and pure.

### **Causes of Business Risks:**

1. **Natural causes:** The causes which are beyond human control e.g., flood, earthquake, heavy rains, famine etc.
2. **Human causes:** It includes carelessness or negligence of employees e.g., theft, strikes, riots, misappropriation of cash and products etc.
3. **Economic causes:** It is related to a chance of loss due to change in market condition e.g., fluctuations in demand and prices, competition, change in technology etc.
4. **Physical causes:** Mechanical defects or failures which may also lead to losses e.g., bursting of boiler or machine, may cause death or destruction.
5. **Other causes:** These include unforeseen events like political disturbances, fluctuation in exchange rates etc.

**Question 7. What factors are important to be considered while starting a business? Explain.**

**Answer:** Following factors are considered while starting a new business:

1. **Selecting the line of business:** The first thing to be decided by the entrepreneur is the line and type of business to be undertaken.
2. **Scale or size of business:** After deciding the line of business the businessman must decide whether he/she wants to set up large scale or small scale business.
3. **Choice of form of business organization:** The next decision must be taken is to finalise the form of business i.e., to set up sale, proprietorship, partnership or joint stock company.
4. **Location of business enterprise:** The entrepreneur has to decide the place where the business will be located. Before taking this decision he/she must find out availability of raw materials, power, labour, banking, transportation etc.
5. **Financial requirement:** The businessman must analyse the amount of capital he/ she might require to buy for fixed assets and for working assets). Proper financial planning must be done to determine the amount of funds needed.
6. **Physical facilities:** It includes machinery, equipment building etc. This decision depends upon the size, scale and type of business activities he/she wants to carry on.
7. **Plant layout:** Showing the physical arrangement of machines and equipment needed to manufacture a product.
8. **Competent and committed workforce:** The entrepreneur must find out the requirement of skilled and unskilled workers and managerial staff to perform various activities.
9. **Tax planning:** The entrepreneur must try to analyse the types of taxes, because there are a number of tax laws in the country which affect the functioning of business.
10. **Setting up the enterprise:** After analysing the above mentioned points carefully the entrepreneur can start the business which would mean mobilising various resources and completing legal formalities.

## **MORE QUESTIONS SOLVED**

### **I. Multiple Choice Questions**

**Question 1. Which of the following is an economic activity?**

- (a) Cooking food for self consumption (b) Cooking food for sale  
(c) Cooking food for donation (d) All of the above

**Question 2. Which of the following is not a business activity?**

- (a) Production of goods (b) Trading of goods

(c) Storage of goods (d) Working in a hospital for wages

Question 3. Which of the following is not a feature of employment?

(a) Fixed wages (b) Agreement between employer and employee

(c) Terms and conditions (d) Element of risk

Question 4. Choose the odd one out:

(a) Insurance (b) Warehousing

(c) Mining (d) Banking

Question 5. Which of the following is not an insurable risk?

(a) Risk of theft

(b) Risk of fire

(c) Risk of change in pattern of demand

(d) All of these

Question 6. Which of the following is a cause of business risk?

(a) Natural causes (b) Political causes

(c) Economic causes (d) All of the above

Question 7. Profits are necessary for:

(a) Expansion (b) Survival

(c) Innovation (d) All of the above

Question 8. Objectives of business do not include:

(a) Higher returns to investors (b) Employee satisfaction

(c) Maximum price-from consumers (d) Market standing.

Question 9. Which of the following is an example of genetic industry?

(a) Mining (b) Lumbering

(c) Animal husbandry (d) Hunting

Question 10. Which of the following is an example of secondary industry?

(a) Genetic industry (b) Extractive industry

(c) Synthetic industry (d) All of the above

Answers: 1. (b) 2. (d) 3. (d) 4. (c) 5. (c)

6. (d) 7. (d) 8. (c) 9. (c) 10. (c)

## II. Short Answer Type Questions

Question 1. Differentiate between economic and non-economic activities.

**Answer:** All human beings have different types of needs. So, in order to full fill those needs, they have to perform some activities. Human activities are classified into economic and non-economic activities.

<b>Basis</b>	<b>Economic</b>	<b>Non-economic</b>
<b>Meaning</b>	Those activities whose aim is to earn money.	Those activities whose aim is not to earn money, and to create wealth, but to satisfy social, psychological and emotional needs.
<b>Example</b>	A teacher teaching in a school. People working in factories.	A teacher teaches his/her son/daughter at home. A housewife cooks food for her family.

**Question.2. What are the functions of commerce?**

**Answer:** The functions of commerce are as follows:

1. Removing the hindrance of person and that means lack of information to producer about consumer and to consumer about the producer. It is removed by advertising.
2. Transportation removes hindrance of place.
3. Storage and warehousing activities remove the hindrance of time.
4. Banking removes the hindrance of finance.
5. Insurance removes the hindrance of risk.
6. Advertising removes the hindrance of information.

**Question 3. Distinguish between industry, trade and commerce.**

**Answer:**

<b>Basis</b>	<b>Industry</b>	<b>Commerce</b>	<b>Trade</b>
<b>Meaning</b>	<b>Production of goods and services.</b>	<b>Distribution of goods and services.</b>	<b>Buying and selling of goods and services.</b>
<b>Capital requirement</b>	<b>Large amount of capital invested.</b>	<b>Comparatively lesser invested capital.</b>	<b>Less capital depending on the nature of business.</b>
<b>Scope</b>	<b>It includes primary, secondary and services industries.</b>	<b>It includes trade and auxiliaries to trade.</b>	<b>It includes home and foreign trade.</b>
<b>Risk</b>	<b>It involves maximum risk.</b>	<b>Less risk as compared to industry.</b>	<b>Least risk involved.</b>
<b>Utility</b>	<b>Creates form utility.</b>	<b>Creates place and time utility.</b>	<b>Creates possession utility.</b>

**Question 4. Can profits be the sole objective of a business? Justify your answer by giving suitable reasons.**

**Answer:** A layman may say that profits are the only objective with which a business is carried on but a good business man cannot keep profits as his only motive. A business organization is an economic unit which makes use of various factors of production. Capital is one of the factors of production. It pays interest in the form of profits. Ur wick has put it beautifully, "Earning of profits cannot be objective of business any more than eating is the objective of living." There must be other objectives of a business which are non-monetary but as important as monetary, like employee satisfaction, innovation, productivity, consumer satisfaction, etc.

Following reasons can be given to justify our opinion that profits cannot be the sole objective of a business.

1. If we make profits to be only objective then interests of consumers, employees and society will be ignored.
2. Maximum profits in the short run, may result worse for long term interest of the company.

3. In present day scenario, when consumer awareness is increasing, labour laws are becoming stringent, social responsibilities of business is being highlighted, environment is being talked about, a business needs to set its objectives for satisfaction of consumers, employees, environmentalists, government etc.

**Question 5. Explain political and legal causes of business risks.**

**Answer:** The causes of business risk include:

1. Changes in government policies regarding foreign trade
2. Entry of multinational companies
3. Changes in laws affecting the business like licensing, taxation etc.
4. Changes in consumer laws and labour laws.

For example, an increase in tax rates may reduce profit margin of the business or an increase in minimum wages may increase labour cost for the business.

**Question 6. Differentiate between insurable risks and non-insurable risks.**

**Answer:** Differences between insurable risks and non-insurable risks is summarised below:

<b>Basis</b>	<b>Insurable risks</b>	<b>Non-insurable risks</b>
<b>Meaning</b>	Those risks which can be covered up by some type of insurance policy are called insurable risk.	Those risks which cannot be covered up by some type of insurance policy are called non-insurable risk.
<b>Business Risks</b>	Business risks are not insurable risks.	Business risks are non insurable risks.
<b>Example</b>	Risk of damage due to fire, accident, theft etc.	Risk of damage due to change in technology or change in government policy etc.

**Question 7. What are the hindrances in the commerce? Which agencies are used to remove these hindrances?**

**Answer:** Following are the hindrances in commerce:

- **Lack of Personal Contact:** This hindrance is removed by traders and middlemen.
- **Distance or Place:** This hindrance is removed by transportation.
- **Finance:** This hindrance is removed by banking.
- **Time or Storage:** This hindrance is removed by warehousing.
- **Risk:** This hindrance is removed by insurance companies.
- **Information:** This hindrance is removed by advertisement or communication.

### III. Long Answer Type Questions

**Question 1. Define Profession. Discuss its salient features.**

**Answer:** When a person is engaged in an occupation which provides services on the basis of specialized knowledge and experience in their respective occupations, it is called profession. For

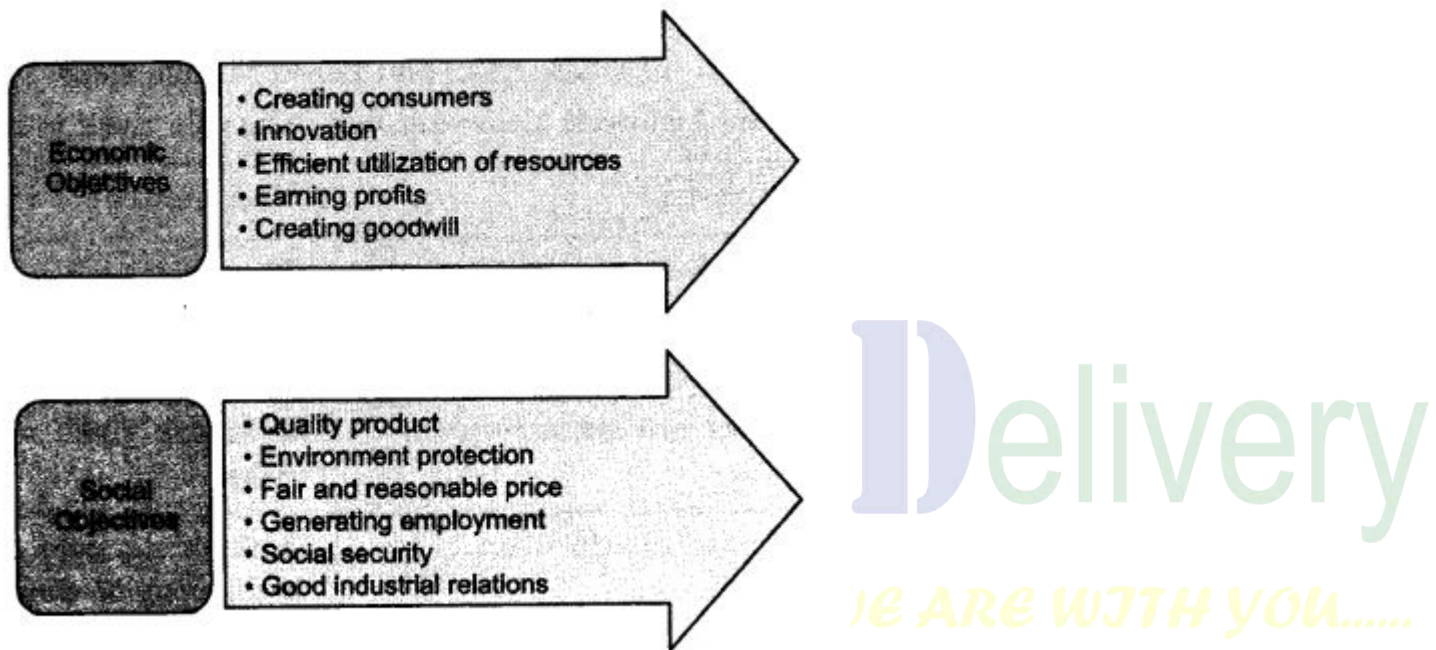


example, Legal (Lawyer), Medical (Doctor), Accountancy (C.A).  
An occupation can be called a profession if it has the following features:

1. Membership of a professional body and certificate of practice is required.
2. Personalised services of expert nature.
3. Professional qualification and training are required.
4. Professional fee is charged in lieu of services.
5. The limited capital for establishment is required.
6. The degree of risk is low.
7. Professional code of conduct is to be followed that has been given by the concerned authority.

**Question 2. Explain the economic and social objectives of the business.**

**Answer:**



**1. Economic Objectives:**

- **Creating consumers:** It means producing and distributing such useful goods and services which satisfy the consumers.
- **Innovation:** Innovation includes production of new products, replacing older products with latest and with new ones, improvement and modernisation in production methods so as to improve quality and/or reduce cost.
- **Effective utilisation of Resources:** A business tries to minimise and optimise its resource usage so as to minimise the cost and maximise the profits. By reducing cost and increasing profits, it ensures survival, growth, expansion and diversification.
- **Earning profits:** According to Dicksee, "Business is a form of activity pursued primarily with the objective of earning profit for the benefit of those on whose behalf activity is conducted.
- **Creating Goodwill:** When a business is able to make good profits and other economic activities, its goodwill amongst investors and competitors goes up.

**2. Social Objectives**

- **Quality product:** A business aims at providing quality product so that it has good demand in the market and consumers feel satisfied to consume it. Inferior goods do not satisfy consumers.

- **Environment protection:** Another social objective of a business is protecting the environment from pollution of any kind and to ensure that nonrenewable resources are not depleted.
- **Fair and reasonable price:** Prices must be fair and reasonable. Business aims at maximizing social satisfaction in right sense instead of maximizing profit.
- **Generating employment:** Business activities aim at providing employment opportunities for entrepreneurs and self-employed persons. Who provide some goods and services to businessmen?
- **Social security:** Businessmen follow certain social welfare programmes like group insurance, provident fund, pension fund, medical facilities of employees, etc. it enhances social security.
- **Good industrial relations:** Employees are an important part of an organization. Their problems and grievances must also be considered, while running a business. Business must aim at building sound industrial relations.

### **Question 3. Define commerce. Discuss its importance in the business world.**

**Answer:** Commerce is related to the exchange and distribution of goods and services. It involves trade and activities which facilitate trade like transportation, banking, warehousing, and finance, etc. Commerce can be defined as the sum total of all such activities which are related to transfer of goods and services from manufacturer to consumer, i.e., from the place of production to the place of consumption.

Commerce is of great importance in the business world:

#### **Removal of Obstacles or Hindrance of Trade:**

- Removing the hindrance of person: It means lack of information to producer about consumer and to consumer about the producer. It is removed by advertising.
- Transportation removes the hindrance of place.
- Storage and warehousing activities remove the hindrance of time.
- Banking removes the hindrance of finance.
- Insurance removes the hindrance of risk.
- Advertising removes the hindrance of information.

#### **These functions are divided into:**

##### **1. Service Functions**

Those activities which help in removing hindrance of place, i.e. distance, knowledge, information and risk are included in service functions. These activities make use of the following means:

(i) Transportation (ii) Communication (iii) Insurance (iv) Advertisement (v) Entertainment services.

##### **2. Financial Functions**

It includes those activities which help in removing hindrance to finance. It includes:

- (i) Commercial banks
- (ii) Financial institutions like LIC, UTI, etc.
- (iii) Stock exchanges .
- (iv) Private financiers
- (v) Lease, hire purchase and installment supply agencies.

##### **3. Marketing Functions**

Those activities which help in the removal of the hindrances of exchange and person are included in this category.

It includes:

(i) Channels of distribution (ii) Storing and warehousing facilities (iii) Packaging, grading and trade marks.

**Question 4. “No business is risk free.” Do you agree? Justify your answer, mentioning the nature and causes of business risk.**

**Answer:** Yes, we agree. We cannot think of any business which is risk free. You start a general store—the simplest business. There is a risk of things you buy getting wasted due to changes in demand pattern. You start a garments shop, fashion may change making your stock a waste and so on. There is not even a single business where there is no risk. It will be clearer when we look at the nature and causes of risk.

**1. Nature of Business Risks**

- Business risks arise due to uncertainties: Natural calamities, change in demand and prices, change in technology, etc. are some of the examples of uncertainty which create risks.
- Risk is an essential part of every business: No business can avoid the risk. Risk can be minimized, but cannot be eliminated.
- Degree of risk depends mainly upon the nature and size of business: For small scale business it is less and for large scale business it is more.
- Profit is the reward for risk taking: An entrepreneur bears risks and in consideration, he gets rewarded in the form of profit. Greater the risk higher is the chance of profit.

**2. Causes of Business Risk**

- Natural causes: These are beyond human control, e.g., flood, earthquake, heavy rains, famine, etc.
- Human causes: It includes carelessness or negligence of employees, e.g. theft, strikes, riots, misappropriation of cash and goods, etc.
- Economic causes: These are related to a chance of loss due to changes in market condition, e.g., fluctuations in demand and prices, competition, change in technology etc.
- Physical causes: Mechanical defects or failures may also lead to losses, e.g. bursting of the boiler or machine may cause death or destruction.
- Legal and Political Causes: These causes of business risk include:
  - (a) Changes in government policies regarding foreign trade
  - (b) Entry of multinational companies
  - (c) Changes in laws affecting the business like to license, taxation, etc
  - (d) Changes in consumer laws and labour laws.

Think of any business. Risk in one way or the other must be applied to it. Hence, we may conclude that no business is risk free.

**IV. Higher Order Thinking Skills (HOTS)**

**Question 1. “Earning of profits is the main objective of a business and other objectives are there to aid it only.” Do you agree? Justify your answer.**

**Answer:** It is incorrect to assume there can be only one objective of a business. Peter F. Drucker remarked, “To Manage a business is to balance a variety of needs and goals. And this requires multiple objectives.” Thus, the management of a business must set objectives, in every ‘key area’ that influences its survival and growth. Peter F. Drucker has suggested eight key areas where objectives must be set. These are discussed below:

1. **Market standing:** It refers to the market position of a business in relation to its competitors, e.g. position of 'Liberty' against that of 'Bata'. A dynamic enterprise must aim at increasing its market standing by offering better products at competitive prices and winning permanent customers.
2. **Innovation:** It means the introduction of new products, new uses of existing products, or new methods of production. Innovations are essential for a business enterprise to grow in the competitive world. For example, LG introduced door cooling technology in refrigerators.
3. **Productivity:** It is the ratio between output and inputs in the production process. Productivity is often used as an indicator of the efficiency of an organization. More productivity will lead to reduced cost of production.
4. **Employee satisfaction:** An organization must also aim at moulding the attitudes of employees so that they may contribute better towards organizational goals. It is also important to provide such working conditions to employees that they feel satisfied in working with and for the organization.
5. **Resources—Physical and financial:** A business enterprise requires many physical and financial resources. A business must aim at procuring these resources.
6. **Managerial performance:** A team is entrusted with the tasks of planning, organizing, staffing, directing and controlling which is called management. Management needs to set targets in the areas of planning, organizing, staffing, directing and controlling and also overall targets for the development of the organization.
7. **Social responsibility:** A business is a part of society. There are some responsibilities of business towards society like generating employment, using eco-friendly methods of production, etc. I must fulfill these responsibilities.
8. **Profitability:** Consider all the above objectives. They are either not possible to be attained without profits like consumer wants good quality. So for market standing we need to provide good quality product which can be provided only when we have enough profits. Similarly, employees want good monetary and non-monetary benefits which are dependent on profits. Some other objectives contribute towards higher profits like innovation and managerial performance. Therefore, we can conclude that the main aim of a business is to earn profits and other aims are either an outcome of the profits or profits are not possible without these.

**Question 2. "Risk is the element which makes the business different from other economic activities." Do you agree? Justify your answer.**

**Answer:** All economic activities are divided into three categories.

1. Employment
  2. Profession
  3. Business.
1. Employment is a contract between employer and employee whereby the employee agrees to work on pre-fixed terms and conditions for an employer for a fixed wage or salary. There is no risk associated with employment as wages or salary is pre-fixed.
  2. Profession includes those activities, which are requiring special knowledge and skill to be applied by individuals in their occupation to earn fees. A professional also takes a minimal risk of whether he will get clients or not.
  3. Business refers to those economic activities, which are connected with production, purchase and sale of goods or supply of services with the main object of earning profit. Since there is no pre-determined contract, return which is profit, is not fixed. There may be profits in millions or there may be a heavy loss.  
Therefore, business as an economic activity is different from other economic activities mainly



due to profit. However, there are other differences as well. For example, a business man does not need specific qualifications as required in a profession. A businessman has relative more freedom than a person who is employed or is a professional.

## **V. Value Based Questions**

**Question 1. “Economic and non-economic activities don’t substitute, but complementary to each other.” Do you agree? Explain.**

**Answer:** Yes, we agree. Economic activities are undertaken with an economic motive, i.e., to earn money, but non-economic activities are undertaken without any economic purpose. For example, when our parents go to office or workplace, it is an economic activity, but when a mother cooks food for their children, we do some donations, we get pocket money, we take a bath, and these are non economic activities. But these activities cannot take place unless and until we have money to support them.

No one can work without getting a sound sleep, while sleeping is a non-economic activity. Similarly, bathing is a non-economic activity, but it is compulsory to be healthy. Without being healthy getting involved in economic activity is not possible. Therefore, economic and non-economic activities don’t substitute, but complementary to each other.

**Question 2. If you need , to start doing an economic activity to earn livelihood for your family, which one would you like and why?**

**Answer:** Economic activities can be grouped under business, profession and employment. All the three have their own merits and demerits. Therefore, one will decide according to the conditions, he/she is facing.

1. If one has enough funds to invest and he/she is a person who has an ability to take initiative and decision making then he/she will prefer business.
2. If one has a professional degree and minimum funds to start their own practice, he/she will prefer to be a professional.
3. If one has no such degree and no funds to start any venture of their own but some qualification to suit the requirement of a job, he/she will prefer employment.

**Question 3. If one starts a business, which objective will be of utmost importance to you and why?**

**Answer:** If one starts their own business, our social objectives will be of utmost importance to me because:

1. It will create employment opportunities in the economy. He/she will make use of such methods which are desirable from society point of view.
2. It will help us to provide good quality product at reasonable prices to customers.
3. It will keep environment pollution free.
4. When we will concentrate on these objectives, it will satisfy one consumers and employees.

Consumer satisfaction will lead to improvement in these goodwill and market standing. Employee satisfaction will lead to increase in productivity. These two factors will increase profits in the long run automatically.

# **NCERT SOLUTIONS For Class 11 Business Studies**

## **<http://freehomedelivery.net/Solutions Chapter 2 Forms of Business Organisation>**

### **Class 11 Business Studies Solutions Chapter 2 Forms of Business Organisation**

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#### **I. Multiple Choice Questions**

**Tick the appropriate answer.**

**Question 1. The structure in which there is separation of ownership and management is called**

- (i) Sole proprietorship (ii) Partnership**
- (iii) Company (iv) All business organizations**

**Question 2. The Karta in Joint Hindu family business has:**

- (i) Limited liability (ii) Unlimited liability**
- (iii) No liability for debts (iv) Joint liability**

**Question 3. In a cooperative society the principle followed is:**

- (i) One share one vote (ii) One man one vote**
- (iii) No vote (iv) Multiple votes**

**Question 4. The board of directors of a joint stock company is elected by:**

- (i) General public (ii) Government bodies**
- (iii) Shareholders (iv) Employees**

**Question 5. The maximum number of partners allowed in the banking business are:**

- (i) Twenty (ii) Ten**
- (iii) No limit (iv) Two**

**Question 6. Profits do not have to be shared. This statement refers to:**

- (i) Partnership (ii) Joint Hindu family business**
- (iii) Sole proprietorship (iv) Company**

**Question 7. The capital of a company is divided into number of parts each one of which are called:**

- (i) Dividend (ii) Profit**
- (iii) Interest (iv) Share**

**Question 8. The Head of the Joint Hindu family Business is called (i) Proprietor (ii) Director**

- (iii) Karta (iv) Manager**

**Question 9. Provision of residential accommodation to the members at reasonable rates is the objective of**

- (i) Producer's cooperative (ii) Consumer's objective**
- (iii) Housing cooperative (iv) Credit cooperative**

**Question 10. A partner whose association with the firm is unknown to the general public is called**

- (i) Active partner (ii) Sleeping partner**
- (iii) Nominal partner (iv) Secret partner**

**Answer:**

1. (iii) 2. (ii) 3. (ii) 4. (iii) 5. (ii)  
6. (iii) 7. (iv) 8. (iii) 9. (iii) 10. (iv)

## II. Short Answer Type Questions

**Question 1. For which of the following types of business do you think a sole proprietorship firm of organization would be more suitable, and why?**

- (i) Grocery store (ii) Medical store  
(iii) Legal consultancy (iv) Craft centre  
(v) Internet cafe (vi) Chartered accountancy firm

**Answer:** Sole proprietorship will be more suitable for grocery store, medical store, and internet cafe because:

- It has easy formation and closure.
- It needs limited resources.
- He will be sole risk bearer which is not so high and profit recipient.
- He will have 100% control.

**Question 2. For which of the following types of business do you think a partnership firm of organization would be more suitable, and why?**

- (i) Grocery store (ii) Medical store  
(iii) Legal consultancy (iv) Craft centre  
(v) Internet cafe (vi) Chartered accountancy firm

**Answer:** For legal consultancy and chartered accountancy firm, partnership firm will be more suitable because it has:

- Ease of formation and closure
- Balanced decision making
- More funds
- Sharing of risks
- Maintain secrecy

**Question 3. Explain the following terms in brief:**

- (i) Perpetual succession (ii) Common seal  
(iii) Karta (iv) Artificial person

**Answer: (i) Perpetual Succession:** Perpetual succession refers to continuous succession of a corporation. Perpetual succession is one of the remarkable features of a corporation. The very objective of a corporation is to have a perpetual succession, for there can not be a succession forever without incorporation. The company has perpetual succession. The death or insolvency of a shareholder does not affect its existence. A company comes into end only when it is liquidated according to provision of the Companies Act.

**(ii) Common Seal:** The expression 'Common Seal' is not defined in the Companies Act, 1956. General practice is to adopt the Common Seal, at the first Board Meeting of the company. It must be kept under the safe custody of authorized director/officer. The Articles of Association, may set out how and when the common seal has to be affixed.

**(iii) Karta:** Karta is the head of Joint Hindu family business. He has unlimited liability and final decision making power.

**(iv) Artificial Person:** A person in the eyes of law is called an artificial person. An entity which has a separate legal entity in the eyes of law is called artificial person. A joint stock company and a cooperative society are artificial persons.

**Question 4. Compare the status of a minor in a Joint Hindu Family Business with that in a partnership firm.**

**Answer:** A minor becomes a member of Joint Hindu Family Business by virtue of his birth. On the other hand, in partnership, minor can be a partner only in profits.

**Question 5. If registration is optional, why do partnership firms willingly go through this legal formality and get themselves registered? Explain.**

**Answer:** However registration is optional, partnership firms willingly go through this legal formality and get themselves registered because it has some merits:

1. **Settlement of Claims:** Registered firms can file suit against the third parties. So the rights of registered firms are safeguarded by law. But an un-registered firm or its partner cannot enforce its claim against the third parties or its co-partner.
2. **Protection of Rights:** The rights and privileges of new partner are also protected in registered firm. But if incoming partner fails to register himself, he will incur great risk, because he will not be in a position to file suit for his dues against his firm or his co-partners.
3. **Protection of Property:** The property of the retired or deceased partner continues to be liable for the acts firm does after his death or retirement until public notice is served for the change to registrar, So there is strong inducement for partners of registered firms to have the changes noted in the register. But if there is unregistered firm, the private property of the outgoing partner will be considered liable to charge the debts in spite of retirement.
4. **Protection to Creditors:** Registered firm has to maintain correct, complete and up-to-date record of its partners who will be liable for the obligations of the firm. The statement recorded in the register regarding constitution of firm would afford a strong safeguard against untrue refusal of partnership and the evasion of liability to persons who want to deal with the firm.

**Question 6. State the important privileges available to a private company.**

**Answer:** A company can be registered as a private company or a public company. When a company is incorporated as a private company, it enjoys certain privileges and exemptions when compared to a public company.

Some of the privileges enjoyed by a Private Company are:

- The minimum number of members required to form a Private Company is only 2, whereas it is 7 in case of a Public Company.
- A Private company can start its business immediately after its incorporation. It need not obtain the Certificate of Commencement of Business.  
'Certificate of Commencement of Business, is issued by the Registrar of Companies to Public Companies. Once a Company has been registered or formed, it shall apply for the Certificate of Commencement of Business in the prescribed form to the ROC (Registrar of Companies). Only after this certificate has been obtained it can commence its business. This certificate has to be obtained within 6 months from the date of incorporation of a Company.'
- No qualification shares and consent of the Director to act as a Director is required to be filed with the ROC at any time during the tenure of the company, as in case of a Public company.
- A Private Company is not required to issue or file a prospectus or statement in lieu of prospectus with the Registrar of Companies.  
'Prospectus, is an important document for a public company. It is nothing but an invitation to the public to subscribe for the shares of the Company. In case a public company does not intend to invite the public to subscribe to the shares, it has to file a statement in lieu of prospectus.'



- It is not required to have an index of members, as in case of a public company. The reason being the Companies Act limits the maximum number of members required for a Private Company to 50.
- It is not required to hold a statutory meeting or file a statutory report.  
‘Statutory meeting is a general meeting of the shareholders of the Company which has to be held within a period of not less than one month and not more than 6 months from the date, on which it is entitled to commence its business.’
- It is not required to offer new shares to existing shareholders in proportion to their shareholdings.  
In case of a Public Company further issue of capital shall be made to the persons who at the date of the issue are holders of the equity shares of the Company in proportion to their holding.
- A Private Company need to have a minimum of two directors only whereas a Public Company needs to have a minimum of three directors.
- All the Directors may be appointed by a single resolution in case of a Private Company.
- The Directors of a Private Company need not to retire by rotation i.e., they can be Permanent Directors.

### **Question 7. How does a cooperative society exemplify democracy and secularism?**

#### **Explain.**

**Answer:** Cooperative is a form of organization wherein persons voluntarily associate together as human beings on the basis of equality for the promotion of an economic interest for themselves. In a cooperative society, the power to take decisions lies in the hands of an elected managing committee. The right to vote gives the members a chance to choose the members who will constitute the managing committee and this lends the cooperative society a democratic character. Also, the principle of ‘one man, one vote’ governs the cooperative society, irrespective of the amount of capital contribution by a member, each member is entitled to equal voting rights. The membership of a cooperative society is voluntary. A person is free to join a cooperative society, and can also leave anytime as per his desire. Membership is open to all, irrespective of their religion, caste and gender. Thus, by keeping all these points in mind, a cooperative society exemplifies democracy and secularism.

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### **Question 8. What is meant by ‘partner by estoppel’? Explain.**

**Answer:** When a person, by words spoken or written or by conduct, represents himself or herself, or consents to another representing him or her to anyone, as a partner in an existing partnership or with one or more persons not actual partners, he or she is liable to any such person to whom such representation has been made, who has, on the faith of such representation, given credit to the actual or apparent partnership and, if he or she has made such representation or consented to its being made in a public manner, he or she is liable to such person, whether the representation has or has not been made or communicated to such person so giving credit by or with the knowledge of the apparent partner making the representation or consenting to its being made, as follows:

1. If a partnership liability results, he or she is liable as though he or she were an actual member of the partnership.
2. If no partnership liability results, he or she is liable jointly with the other persons, if any, so consenting to the contract or representation as to incur liability, otherwise separately.
3. When a person has been thus represented to be a partner in an existing partnership, or with one or more persons not actual partners, that person is an agent of the persons consenting to such representation to bind them to the same extent and in the same manner as though that person were a partner in fact, with respect to persons who rely upon the representation where all the members of the existing partnership consent to the representation, a partnership act or

obligation results; but in all other cases it is the joint act or obligation of the person acting and the persons consenting to the representation.

### III. Long Answer Type Questions

#### Question 1. What do you understand by a sole proprietorship firm? Explain its merits and limitations.

**Answer:** If entrepreneur starts sole proprietor form of business, then he has the following advantages.

Advantages of Sole Proprietor Form of Business:

**1. Easy formation:** The formation of sole proprietorship business is very easy and simple. No legal formalities are involved for setting up the business except a license or permission in certain cases. The entrepreneur with initiative and certain amount of capital can set up such form of business.

**2. Direct motivation:** The entrepreneur owns all and risks all. The entire profit goes to his pocket. This motivates the proprietor to put his heart and soul in the business to earn more profit. Thus, the direct relationship between effort and reward motivates the entrepreneur to manage the business more efficiently and effectively.

**3. Better control:** The entrepreneur takes all decisions affecting the business. He chalks out the plan and executes the same. His eyes are on everything and everyone. There is no scope for laxity. This results in better control of the business and ultimately leads to efficiency.

**4. Promptness in decision-making:** When the decision is to be taken by one person, it is sure to be quick. Thus, the entrepreneur as sole proprietor can arrive at quick decisions concerning the business by which he can take the advantage of any better opportunities.

**5. Secrecy:** Each and every aspect of the business is looked after by the proprietor and the business secrets are known to him only. He has no legal obligation to publish his accounts. Thus, the maintenance of adequate secrecy leaves no scope to his competitors to be aware of the business secrets.

**6. Flexibility in operations:** The sole proprietorship business is undertaken on a small scale. If any change is required in business operations, it is easy and quick to bring the changes.

**7. Scope for personal touch:** There is scope for personal relationship with the entrepreneur and customers in sole proprietorship business. Since the scale of operations is small and the employees work under his direct supervision, the proprietor maintains a harmonious relationship with the employees. Similarly, the proprietor can know the tastes, likes and dislikes of the customers because of his personal rapport with the customers.

**8. Free from Government control:** Sole proprietorship is the least regulated form of business. Regulated laws are almost negligible in its formation, day-to-day operation and dissolution.

Disadvantages of Sole Proprietor Form of Business:

The sole proprietorship business is not free from criticism. It suffers from certain limitations and drawbacks, because of its very nature and scope of operations. These points may be duly taken care of while entrepreneur adopting this mode of business.

**1. Limited resources:** The financial resources of any small business as an individual is limited. He mainly finances from his own savings or borrows from financial institutions, friends and relatives as per his capacity. Thus, limited resource is the major drawback of this form of business.

**2. Limited managerial capability:** Modern business requires updated managerial skills in each and every sphere of activity. We cannot hope a single individual to possess all the managerial, talents necessary to carry on a business efficiently. The limited financial resources of the sole proprietorship is a hindrance to hire the services of managers with expertise in different areas, thereby the growth of the business.

**3. Unlimited liability:** Since the liability of the sole proprietor is unlimited, the private properties of the proprietor is also at risk. When the business fails, the private properties of the owner are utilized to pay off the business debts. Thus, the proprietor must have to look this aspect carefully.

**4. Uncertainty of continuity:** The continuity of the business is uncertain because the business may come to an end due to the incapacity or death of the proprietor. Even if at all the business passes on to the successor of the proprietor, it is unlikely that they may pose the business acumen like that of the proprietor. The discontinuance of the business is a social loss.

**5. Not suitable for large-scale business:** The limited financial resources, limited managerial capability of the proprietor, risk to the private property etc. makes the proprietorship business unsuitable for large-scale business. This system of business cannot afford for large-scale operation.

**6. Difficult to maintain personal contact:** Even though there is scope for personal touch in sole proprietorship business, it is unlikely to happen when the business is undertaken in different areas. It is not so easy on the part of the proprietor to have personal contact with customers and suppliers at the same time.

**Question 2. Why is partnership considered by some to be a relatively unpopular form of business ownership? Explain the merits and limitations of partnership.**

**Answer:** Partnership is considered by some to be relatively unpopular form of business ownership because:

1. **Uncertainty of duration:** A partnership suffers from a possible limited span of life. Legally, a partnership firm must be dissolved on the retirement, death, bankruptcy, or lunacy of any partner or demanded by any partner. The probability of any one of these events occurring when the number of partners is much greater than in the case of a sole proprietor.
2. **Risks of additional liability:** It is true that like the sole proprietor, each partner has unlimited liability. But his liability may arise not only from his own acts but also from the acts and mistakes of co-partners over whom he has no control.
3. **Lack of harmony:** The old saying that “too many cooks spoil the broth” can be apt for a business partnership. Harmony may be difficult to achieve, especially when there are many partners. Lack of centralized authority and conflicts in policy can disrupt the organization.
4. **Difficulty in withdrawing investment:** Investment in a partnership can be simple, but its withdrawal may be difficult or costly when this aspect is considered from the point of view of individual partners. This is so because no partner can withdraw his interest from the firm without the consent of all partners.
5. **Lack of public confidence:** A partnership may suffer from lack of public confidence
6. **Lack of public confidence:** A partnership may suffer from lack of public confidence because, like that of a company there is no legal mechanism to enforce the registration of a partnership firm and the disclosure of its affairs.
7. **Limited resources:** A partnership is good as it can be started with limited capital. However, it becomes a handicap in the growth and expansion phases of the business. There is a limit beyond which it is almost impossible for partners to collect capital. This limit is generally up to the personal properties of the partners.
8. **Unlimited liability:** Unlimited liability discourages partners to undertake risky ventures, and therefore, their risk-taking initiative is very risky.

**Merits of Partnership**

- It is easy to set up.
- It has more capital, which can be brought into the business.
- Partners bring new skills and ideas to a business.
- Decision-making can be much easier with more brains to think about a problem.
- Partners share responsibilities and duties of the business.
- Division of labour is possible as partners may have different skills.

## Limitations of Partnership

- There is an unlimited liability: All the partners are responsible for the debts of the firm and if the business goes bankrupt, all the partners will have to clear the debts even if they have to sell off their personal belongings.
- Disagreement among the partners can lead to problems for the business.
- There is a limit to the capital invested. Because of the fact that maximum 20 members are allowed, the business may find it difficult to expand after a certain limit.
- There is no continuity of existence. Partnership is dissolved if one of the partners die or resigns or becomes bankrupt.

### **Question 3. Discuss the characteristics, merits and limitations of the cooperative form of organization. Also describe briefly different types of cooperative societies.**

**Answer:** It is important to choose an appropriate form of organization as it will determine:

1. Extent of control;
2. Extent of liability;
3. Availability of resources;
4. Legal formalities.

All these in turn will determine profits of the business.

**Different types of cooperative societies are explained below:**

1. **Producer's cooperative societies:** The producer's cooperatives are established by the small producers. The members of the society produce goods in their houses or at common place. The raw materials, tools, money, etc. are provided to them by the society. The output is collected by the society and sold in the market at the wholesale rate. The profit is distributed among the members in proportion to the goods supplied by each member.
2. **Consumer's cooperative societies:** Consumer's cooperative societies are established to remove middlemen from the field of trade. These societies purchase foods at the wholesale prices and sell these goods to the members at cheaper rates than the market prices. However, the goods are sold to the non-members at the market rates. The profit, if any, is distributed among the members in the shape of bonus according to their purchase ratio.
3. **Marketing cooperative societies:** The marketing cooperative societies are formed by the small producers for the promotion of trade. The two main objectives of these societies are, to sell the good at reasonable prices by eliminating middlemen and to make there ready for the product of the member. These types of societies are formed by the small agriculturalist and artisans. These societies collect the products of its members and make its grading and keep them in warehouses and sell them in the market at whole sale rate when the market is ready for these products. The profit is distributed among the members according to the ratio of goods supplied by them.
4. **Credit cooperative societies:** These cooperative societies are formed for the financial help of the members. These societies provide loans to the members at low rate of interest. In rural areas these provide loans to the farmers for the purchase of seeds, fertilizers and cattle. In urban areas these societies provide loan to its members for the purchase of raw materials and tools.
5. **Farming cooperative societies:** These societies are formed by the small agriculturalist to get the benefits of large scale farming. These societies provide help to the farmer for the improve method of cultivations by providing large scale farming tools such as tractors, threshers and harvesters, etc.
6. **Housing cooperative societies:** These societies are formed for the procurement of land for the construction of houses on a homogeneous basis. These societies are formed by those



members who are intended to construct their own home. These societies provide loan to the members for the construction of houses. These also purchase construction materials in bulk and provide this material to its member at cheaper rates.

**Question.4. Distinguish between a Joint Hindu family business and partnership.**

**Answer:** Differences between Joint Hindu family systems and sole proprietorship are given below:

1. **Regulating law:** A partnership is governed by the provisions of the Indian Partnership Act, 1932. A Joint Hindu family business is governed by the principles of Hindu law.
2. **Mode of creation:** A partnership arises out of a contract, whereas a Joint Hindu family business arises by the operation of law and is not the result of a contract.
3. **Admission of new members:** In a partnership no new partner is admitted without the consent of all the partners, while in the case of a Joint Hindu family firm, a new member is admitted just by birth.
4. **The position of families:** In a partnership women can be full-fledged partners, while in a Joint Hindu family business membership is restricted to male members only. After the passage of the Hindu Succession Act, 1956, families get only co-sharer's interest at the death of a coparcener and they do not become coparceners themselves.
5. **Number of members:** In partnership the maximum limit of partners is 10 for banking business and 20 for any other business, but there is no such maximum limit of members in the case of Joint Hindu Family business.
6. **Liability of members:** In partnership, the liability of the partners is joint and several as well as unlimited. In other words, each partner is personally and jointly liable to an unlimited extent and if partnership liabilities cannot be fully discharged out of the partnership property each partner's separate personal property is liable for the debts of the firm.

In a Joint Hindu family business, only the 'Karta' is personally liable to an unlimited extent, i.e., his self-acquired or other separate property besides his share in the joint family property is liable, for debts contracted on behalf of the family business.

**Question 5. Despite limitations of size and resources, many people continue to prefer sole proprietorship over other forms of organization. Why?**

**Answer:** Despite limitations of size and resources, many people continue to prefer sole proprietorship over other forms of organization because of following merits:

1. **Easy to start and close:** It can be easily started and closed without any legal formalities.
2. **Quick decision making:** As sole trader is not required to consult or inform anybody about his decisions.
3. **Secrecy:** He is not expected to share his business decisions and secrets with anybody.
4. **Direct incentive:** Direct relationship between efforts and reward provide incentive to the sole trader to work hard.
5. **Personal touch:** The sole trader can maintain personal contacts with his customers and employees.
6. **Social utility:** It provides employment to persons with limited money who are not interested to work under others. It prevents concentration of wealth in a few hands.

**MORE QUESTIONS SOLVED**

**I. Multiple Choice Questions**

**Question 1. Name the form of business organization found only in India.**

- (a) Sole Proprietorship (6) Partnership  
(c) Joint Hindu Family (d) Cooperatives

**Question 2. Choose the type of business in which sole proprietorship is very suitable.**

- (a) CA Firm (b) Beauty Parlour  
(c) A shopping mall (d) All of these

**Question 3. Name the person who manages a Joint Hindu Family Business.**

- (a) Manager (b) Minor  
(c) Members (d) Karta

**Question 4. Name the law which governs Joint Hindu Family Business.**

- (a) Partnership Act (b) Hindu Law  
(c) Companies Act, 1956 (d) Contract Act

**Question 5. Which document is called charter of a company?**

- (a) Memorandum of Association (b) Articles of Association  
(c) Prospectus (d) All of the above

**Question 6. What is the minimum number of persons required to form a co-operative society?**

- (a) 2 (b) 7  
(c) 10 (d) 20

**Question 7. Which of the following has unlimited liability in business?**

- (a) Sole Proprietor (b) Karta  
(c) Partners (d) All of the above

**Question 8. Name the type of company which must have a minimum paid up capital of 5 lacks,**

- (a) Public Company (b) Private Company  
(c) Government Company (d) All of the above

**Question 9. Which of the following has a separate legal entity?**

- (a) Joint Stock Company (b) Co-operative Society  
(c) Both of the above (d) None of the above

**Question 10. Minor can be full-fledged member of:**

- (a) Co-operative Society (b) Joint Stock Company  
(c) Joint Hindu Family (d) Partnership

**Answer:**

1. (c) 2. (b) 3. (d) 4. (b) 5. (a)  
6. (b) 7. (d) 8. (a) 9. (c) 10. (c)

## **II. Short Answer Type Questions**

**Question 1. Explain the concept of mutual agency in partnership with suitable example.**

**Answer:** The right of all the partners in a partnership to act as the agents for the partnership's normal business activities, with the authority to bind the partnership in to business agreements which have been entered into is called mutual agency. This statement sums up the partnership relationship. The relationship should offer flexibility, opportunity and balanced against that, risk. In partnership you entrust to fellow partners your future reputation and prosperity. Each of us has within our power the ability to enter into undertakings which could bankrupt our fellow partners.

**Question 2. What is the role of Karta in Joint Hindu Family business?**

**Answer:** In a Hindu Joint Family, the Karta or Manager occupies a pivotal and unique place. In that there is no comparable office or institution in any other system in the world. His office is independent and hence, his position is termed as sui generis.

Karta's position is sui generis. As had been explained earlier, his position/ office is independent and there is no comparable office in any system in the world.

- He has unlimited powers and even though he acts on behalf of other members, he is not a partner or agent.
- He manages all the affairs of the family and has widespread powers.
- Ordinarily he is accountable to none. The only exception to this rule is if charges of misappropriation, fraud or conversion are levelled against him.
- He is not bound to save, economise or invest. That is to say that he need not invest in land if the land prices are about to shoot up, and hence, miss out on opportunities etc. He has the power to use the resources as he wishes, unless the above mentioned charges are levelled against him.
- He is not bound to pay income of joint family in any fixed proportion to other members. This means that the Karta need not divide the income generated from the joint family property equally among the family members. He can discriminate one member from another and is not bound to treat everyone impartially. Only responsibility is that he has to pay everyone something so that they can avail themselves of the basic necessities such as food, clothing, shelter, education etc. Karta's Liabilities:

Apart from all the unlimited powers that are bestowed upon the Karta, he also has liabilities thrust on him.

- Karta has to maintain all the members of the joint family properly. If there is any shortfall in his maintenance, then any of the members can sue for maintenance.
- He is responsible for marriage of all the unmarried members in the family. Special emphasis is laid with respect to daughters in this case.
- In case of any partition suit, the Karta has to prepare accounts.
- He has to pay taxes on behalf of the family.
- Karta represents the family in all matters including legal, religious and social matters.

### **Question 3. Explain procedure of registering a partnership firm.**

**Answer:** Procedure for Registration: In order to get a partnership firm registered an application in the prescribed form must be filed with the Registrar of Firms. The application should contain the following information:

1. The name of the firm,
2. The principal place of business of the firm,
3. Names of other places where the firm's business is carried on,
4. Names in full and permanent addresses of the partners,
5. The date on which each partner joined the firm,
6. Duration of partnership, if any.

The application should be signed and verified by each partner. A small amount of registration fee is also deposited along with the application. The application is to be submitted to the Registrar for registration of the firm for its verification.

If everything is in order and all legal formalities have been observed, the Registrar shall make an entry in the register of firms. He will also issue a certificate of registration.

Any change in the information submitted at the time of registration, should be communicated to the Registrar. Registration does not provide a legal entity to the partnership firm.

### **Question 4. Is registration of partnership firm compulsory? What are the consequences of non-registration?**

**Answer:** Registration of a partnership firm is not compulsory under law. The Partnership Act, 1932

provides that if the partners so desire they may register the firm with the Registrar of Firms of the state in which the main office of the firm is situated.

**Consequences of Non-Registration: An unregistered partnership firm suffers from the following situations:**

1. It cannot enforce its claims against a third party in a court of law.
2. It cannot claim adjustment for any sum exceeding Rs 100. Suppose an unregistered firm owes ? 1200 to A and A owes Rs 1000 to the firm the firm cannot enforce adjustment of ? 1000 in a court of law.
3. It cannot file a legal suit against any of its partners.
4. Partners of an unregistered firm cannot file any suit to enforce a right against the firm.
5. A partner of an unregistered firm cannot file a suit against other partners. Non-registration of a firm, however, does not affect the following rights:
  - The right of a partner to sue for the dissolution of the firm or for the accounts of a dissolved firm or to enforce any right or power to realise the property of a dissolved firm.
  - The power of an Official Assignee or Receiver to realize the property of an insolvent partner.
  - The rights of the firm, or its partners, having no place of business.
  - Any suit or set off in which the claim does not exceed rupees one hundred.
  - The right of a third party to sue the unregistered firm or its partners.

**Question 5. What are the steps required for raising funds from public?**

**Answer:** Following steps are required for raising funds from public:

1. **SEBI Approval:** SEBI regulates the capital market of India. A public company is required to take approval from SEBI.
2. **Filing of Prospectus:** Prospectus means any documents which invites offers from the public to purchase share and debenture of the company.
3. **Appointment of Bankers, Brokers, Underwriters:** Bankers of the company receive the application money. Brokers encourage the public to apply for the shares. Underwriters are the persons who undertake to buy the shares if these are not subscribed by the public. They receive a commission for underwriter.
4. **Minimum Subscription:** According to the SEBI guidelines, minimum subscription is 90% of the issue amount. If minimum subscription is not received then the allotment cannot be made and the application money must be returned to the applicants within 30 days.
5. **Application to Stock Exchange:** It is necessary for a public company to list their shares in the stock exchange. Therefore, the promoters apply in a stock exchange to list company shares.
6. **Allotment of Shares:** Allotment of shares means acceptance of share applied. Allotment letters are issued to the shareholders. The name and address of the shareholders is to be submitted to the Registrar.

**Question 6. Define Articles of Association. What are its contents?**

**Answer:** The Articles of Association are the rules for the management of the internal affairs of a company. The articles define the duties, rights and power of the officer and director of the company. Contents of the Articles of Association (It is not an exhaustive but illustrative list)

- The amount of share capital and different types of shares.
- Rights of each class of shareholder.
- Procedure for making allotment of shares.

- Procedure for issuing share certificates.
- Procedure for forfeiture and reissue of share.
- Procedure for conducting, voting and proxy.
- Procedure for appointment of director.
- Procedure for declaration of dividend.
- Procedure for alteration of share capital.
- Procedure regarding winding up of the company.

**Question 7. Differentiate between:**

- Memorandum of Association and Articles of Association.
- Private and Public Company

**Answer: Differences between Memorandum of Association and Articles of Association**

<b>Memorandum of Association</b>	<b>Articles of Association</b>
<b>1. Importance:</b> It has primary importance in the formation of company.	It has a secondary importance in the formation of company.
<b>2. Constitution:</b> It is a constitution of the company.	It contains rules which govern the administration of the company.
<b>3. Object:</b> It lays down the objects of the company.	It contains the procedure of achieving objects. The provision can be changed by the special resolution easily.
<b>4. Alternate:</b> It is not alterable but it can be amended by special resolution and sanction of the court or central government.	Articles of Association can be amended by a special resolution.
<b>5. Relation:</b> Its nature is like contract between the company and outsiders like bankers and creditors.	It maintains relation between the company and the persons inside the company.
<b>6. Regulation:</b> It contains rules which governs the administration of the company.	The Registration of Articles is optional for the company limited by shares. It may adopt all or any of regulations.
<b>7. Nature of Document:</b> It does not allow the company to act against the company ordinance.	It is a subsidiary document to Memorandum of Association.
<b>8. Limits:</b> This document determines the limits of the company business.	Business limits are not mentioned in it.



## Differences between Public Company and Private Company

Private Company	Public Company
<b>1. Minimum and Maximum Members:</b> It has minimum 2 and maximum 50 members.	It has minimum 7 and maximum unlimited members.
<b>2. Invitation to Public:</b> It cannot invite general public to buy its shares and debentures.	It invites general public to buy its shares and debentures.
<b>3. Transfer of Shares:</b> There are certain restrictions on transfer of its shares.	Its share are freely transferable.
<b>4. Commencement of Business:</b> It can commence business after incorporation.	It can commence business after obtaining certificate of commencement of business.
<b>5. Name:</b> It has to write "Private Ltd" after its name.	It has to write only "Limited" after its name.
<b>6. Minimum Capital:</b> Minimum capital required is one lakh.	In it minimum capital required is five lakhs.

### Question 8. Define promoter. What are the functions of a promoter?

**Answer:** Promoter is a person who conceives the idea of starting a business, examines the feasibility of idea, assemble various resources, prepare necessary documents and perform other activities needed to commence the business.

#### Functions of a promoter

1. Identification of business opportunity;
2. Feasibility studies: the following feasibility studies may be undertaken:  
(a) technical feasibility (b) financial feasibility (c) economic feasibility
3. Name approval;
4. Fixing up signatories to the Memorandum of Association;
5. Appointment of professionals;
6. Preparation of necessary documents.

### Question 9. Explain the contents of Memorandum of Association.

**Answer:** Contents of Memorandum of Association: The memorandum must contain the following clauses:

1. **The Name Clause:** It contains the name of company with which the company will be known.
2. **Registered Office Clause:** It contains the name of the state, in which the registered office of the company is proposed to be situated.
3. **Objects Clause:** It defines the purpose for which the company is formed. It is further divided into two sub-clauses: (1) the main objects (2) other objects.
4. **Liability Clause:** It states that the liability of members is limited to the amount unpaid on shares owned by them.

5. **Capital Clause:** It specifies the maximum capital, which the company will be authorized to raise through issue of shares.
6. **Association Clause:** In this clause, signatories to the memorandum, state their intention to be associated with the company and give their consent to purchase qualification shares.

### III. Long Answer Type Questions

#### Question 1. What do you mean by incorporation of a company? What are the steps involved in incorporation of a company?

**Answer:** Incorporation of the company: It means registration of the company under Companies Act, 1956. The second stage involves the following steps:

1. **Filling of documents:** An application to the registrar for incorporation must be accompanied with following documents:
  - Memorandum of Association;
  - Articles of Association or statement in lieu of the prospectus (in case table A is adopted by public limited company);
  - Written consent of proposed directors;
  - Agreement (if any) with proposed managing director, manager, etc.;
  - Copy of registrar's letter approving the company's name;
  - Statutory declaration;
  - Notice of the exact address of the registered office.
2. **Payment of fees:** Along with the above documents, necessary fees is to be paid.
3. **Certificate of incorporation:** The registrar issues a certificate of incorporation after being satisfied. Certificate is a conclusive evidence of regularity of incorporation of a company irrespective of any deficiency in its registration.

#### Question 2. Explain different types of partners.

**Answer:** Different types of partners are given below:

1. **General/Active Partner:** Such a partner takes active part in the management of the firm.
2. **Sleeping of Dormant Partner:** Although he does not take active part in the management of the firm, he invests money, shares profit and loss, has unlimited liability.
3. **Secret Partner:** He participates in business secretly without disclosing his association with the firm to general public. His liability is also unlimited.
4. **Nominal Partner:** Such a partner only gives his name and goodwill to the firm. He neither invests money nor takes profit. But his liability is unlimited.
5. **Partner by Estoppels:** He is the one who by his words or conduct gives impression to the outside world that he is a partner of the firm whereas actually he is not. His liability is unlimited towards the third party who has entered into dealing with firm on the basis of his pretension.
6. **Partner by Holding out:** He is the one who is falsely declared partner of the firm whereas actually he is not. And even after becoming aware of it, he does not deny it. His liability is unlimited towards the party who has dealt it with firm on the basis of this declaration.

#### Question 3. Explain meaning, features, merits and demerits of Sole Proprietorship.

**Answer:** Sole Proprietorship means a business owned, financed and controlled by a single person who is recipient of all profits and bearer of all risks. It is suitable in areas of personalized services like beauty parlour, hair cutting saloons and small scale activities like retail shops.

**Features:**

- **Single Ownership:** It is wholly owned by one individual.
- **Control:** Sole proprietor has full power of decision making.
- **No Separate legal entity:** Business and businessman are not separate entities in the eyes of law.
- **Unlimited liability:** The liability of owner is unlimited. In case the assets of business are not sufficient to meet its debts, the personal property of owner can be used for paying debts.
- **No legal formalities:** No legal formalities are required to start, manage and dissolve such business organization.
- **Sole risk bearer and profit recipient:** He bears the complete risk and there is nobody to share profit / loss with him.

#### Merits:

- **Easy to start and close:** It can be easily started and closed without any legal formalities.
- **Quick decision making:** As sole owner is not required to consult or inform anybody about his decisions.
- **Secrecy:** He is not expected to share his business decisions and secrets with anybody.
- **Direct incentive:** Direct relationship between efforts and reward provide incentive to the sole trader to work hard.
- **Personal touch:** The sole trader can maintain personal contacts with his customers and employees.
- **Social utility:** It provides employment to persons with limited money who are not interested to work under others. It prevents concentration of wealth in a few hands.

#### Limitations:

- **Limited financial resources:** Funds are limited to the owner's personal savings and his borrowing capacity.
- **Limited managerial ability:** Sole trader can't be good in all aspects of business and he can't afford to employ experts also.
- **Unlimited liability:** Unlimited liability of sole trader compels him to avoid risky and bold business decisions.
- **Uncertain life:** Death, insolvency, lunacy or illness of a proprietor affects the business and can lead to its closure.
- **Limited scope for expansion:** Due to limited capital and managerial skills, it cannot expand to a large scale.

#### Question 4. Explain meaning, features, merits and demerits of partnership firm.

**Answer:** Partnership is a voluntary association of two or more persons who agree to carry on some business jointly and share its profits and losses. The partnership was evolved to overcome the shortcomings of sole proprietorship and Joint Hindu Family business.

#### Features:

- **Two or more persons:** There must be at least two persons to form a partnership. The maximum number of persons is 10 in banking business and 20 in non-banking business.
- **Agreement:** It is an outcome of an agreement among partners which may be oral or in writing.
- **Lawful business:** It can be formed only for the purpose of carrying on some lawful business.
- **Decision making and control:** Every partner has a right to participate in management and decision making of the organization.

- **Unlimited liability:** Partners have unlimited liability.
- **Mutual agency:** Every partner is an implied agent of the other partners and of the firm. Every partner is liable for acts performed by other partners on behalf of the firm.
- **Lack of continuity:** Firms existence is affected by the death, lunacy and insolvency of any of its partner. It suffers from lack of continuity.

#### Merits:

- **Ease of formation and closure:** It can be easily formed. Only an agreement among the partners is required.
- **Larger financial resources:** There are more funds as capital is contributed by number of partners.
- **Balanced decisions:** As decisions are taken jointly by partners after consulting each other.
- **Sharing of risks:** In it, risk gets distributed among partners which reduces anxiety, burden and stress on individual partner.
- **Secrecy:** Secrecy can be easily maintained about business affairs as they are not required to publish their accounts or to file any report to the government.

#### Limitations:

- **Limited resources:** There is a restriction on the number of partners and hence capital contributed by them is also limited.
- **Unlimited liability:** The liability of partners is unlimited and they are liable individually as well as jointly. It may prove to be a big drawback for those partners who have greater personal wealth. They will have to repay the entire debt in case the other partners are unable to do so.
- **Lack of continuity:** Partnership comes to an end with the death, retirement, insolvency or lunacy of any of its partners.
- **Lack of public confidence:** Partnership firms are not required to publish their reports and accounts. Thus they lack public confidence.

#### Question 5. Explain meaning, features, merits and demerits of joint stock company.

**Answer:** Joint stock company is a voluntary association of persons having a separate legal existence, perpetual succession and common seal. Its capital is divided into transferable shares.

#### Features:

- **Separate legal existence:** It is created by law and it is a distinct legal entity independent of its members. It can own property, enter into contracts, can file suits in its own name.
- **Perpetual existence:** Death, insolvency and insanity or change of members has no effect on the life of a company. It can come to an end only through the prescribed legal procedure.
- **Limited Liability:** The liability of every member is limited to the nominal value of the shares bought by him or to the amount, guaranteed by him.
- **Transferability of shares:** Shares of public company are easily transferable. But there are certain restrictions on transfer of share of private company.
- **Common seal:** It is the official signature of the company and it is affixed on all important documents of company.
- **Separation of ownership and control:** Management of company is in the hands of elected representatives of shareholders known individually as director and collectively as board of directors.

#### Merits:



- **Limited liability:** Limited liability of shareholders reduces the degree of risk borne by him.
- **Transfer of Interest:** Easy transferability of shares increases the attractiveness of shares for investment.
- **Perpetual existence:** Existence of a company is not affected by the death, insanity, insolvency of member or change of membership. Company can be liquidated only as per the provisions of companies Act.
- **Scope for expansion:** A company can collect huge amount of capital from unlimited number of members who are ready to invest because of limited liability, easy transferability and chances of high return.
- **Professional management:** A company can afford to employ highly qualified experts in different areas of business management.

### Limitations:

- **Legal formalities:** The procedure of formation of company is very long, time consuming, expensive and requires lot of legal formalities to be fulfilled.
- **Lack of secrecy:** It is very difficult to maintain secrecy in case of public company, as company is required to publish and file its annual accounts and reports.
- **Lack of motivation:** Divorce between ownership and control and absence of a direct link between efforts and reward lead to lack of personal interest and incentive.
- **Delay in decision making:** Red tapism and bureaucracy do not permit quick decisions and prompt actions. There is little scope for personal initiative.
- **Oligarchic management:** Company is said to be democratically managed but actually managed by a few people i.e., Board of Directors. Sometimes they take decisions keeping in mind their personal interests and benefit, ignoring the interests of Shareholders and company.

### Question 6. Explain the meaning, features, merits and demerits of cooperative society.

**Answer:** A cooperative society is a voluntary association of persons of moderate means, who unite together to protect and promote their common economic interests.

#### Features:

- **Voluntary association:** Everyone having a common interest is free to join a cooperative society and can also leave the society after giving proper notice.
- **Legal status:** Its registration is compulsory and it gives it a separate identity.
- **Limited liability:** The liability of the member is limited to the extent of their capital contribution in the society.
- **Democratic control:** Management and control lies with the managing committee elected by the members by giving vote. Every member has one vote irrespective of the number of shares held by him.
- **Service motive:** The main aim is to serve its members and not to maximize the profit.
- **State control:** They have to abide by the rules and regulations framed by government for them.
- **Distribution of surplus:** The profit is distributed on the basis of volume of business transacted by a member and not on the basis of capital contribution of members.

#### Merits:

- **Ease of formation:** It can be started with minimum of 10 members. Registration is also easy as it requires very few legal formalities.



- **Limited liability:** The liability of members is limited to the extent of their capital contribution.
- **Stable existence:** Due to registration it is a separate legal entity and is not affected by death, lunacy or insolvency of any of its members.
- **Economy in operations:** There is economy in operation due to elimination of middle man and voluntary services provided by its members.
- **Government support:** Government provides support by giving loans at lower interest rates, subsidies and by charging less taxes.
- **Social utility:** It promotes personal liberty, social justice and mutual cooperation. They help to prevent concentration of economic power in a few hands.

### Limitations:

- **Shortage of capital:** It suffers from shortage of capital as it is usually formed by people with limited means.
- **Inefficient management:** Cooperative society is managed by elected members who may not be competent and experienced. Moreover it can't afford to employ expert and experienced people at high salaries.
- **Lack of motivation:** Members are not inclined to put their best efforts as there is no direct link between efforts and reward.
- **Lack of secrecy:** Its affairs are openly discussed in its meeting which makes it difficult to maintain secrecy.
- **Excessive government control:** It suffers from excessive rules and regulations of the government. It has to get its accounts audited by the auditor and has to submit a copy of its accounts to registrar.
- **Conflict among members:** The members are from different sections of society with different view points. Sometimes when some members become rigid, the result is conflict.

### Question 7. Explain different types of partners.

**Answer:** The different kinds of partners that are found in partnership firms are as follows:

1. **Active or managing partner:** A person who takes active interest in the conduct and management of the business of the firm is known as active or managing partner. He carries on business on behalf of the other partners. If he wants to retire, he has to give a public notice of his retirement; otherwise he will continue to be liable for the acts of the firm.
2. **Sleeping or dormant partner:** A sleeping partner is a partner who 'sleeps', that is, he does not take active part in the management of the business. Such a partner only contributes to the share capital of the firm, is bound by the activities of other partners, and shares the profits and losses of the business. A sleeping partner, unlike an active partner, is not required to give a public notice of his retirement. As such, he will not be liable to third parties for the acts done after his retirement.
3. **Nominal or ostensible partner:** A nominal partner is one who does not have any real interest in the business but lends his name to the firm, without any capital contributions, and doesn't share the profits of the business. He also does not usually have a voice in the management of the business of the firm, but he is liable to outsiders as an actual partner.
4. **Partner by estoppel or holding out:** If a person, by his words or conduct, holds out to another that he is a partner, he will be stopped from denying that he is not a partner. The person who thus becomes liable to third parties to pay the debts of the firm is known as a holding out partner.

There are two essential conditions for the principle of holding out : (a) The person to be held

out must have made the representation, by words written or spoken or by conduct, that he was a partner ; and (b) The other party must prove that he had knowledge of the representation and acted on it, for instance, gave the credit.

5. **Partner in profits only:** When a partner agrees with the others that he would only share the profits of the firm and would not be liable for its losses, he will own as partner in profits only.
6. **Minor as a partner:** A partnership is created by an agreement. And if a partner is incapable of entering into a contract, he cannot become a partner. Thus, at the time of creation of a firm a minor (i.e., a person who has not attained the age of 18 years) cannot be one of the parties to the contract. But under section 30 of the Indian Partnership Act, 1932, a minor 'can be admitted to the benefits of partnership, with the consent of all partners. A minor partner is entitled to his share of profits and to have access to the accounts of the firm for purposes of inspection and copy.

He, however, cannot file a suit against the partners of the firm for his share of profit and property as long as he remains with the firm. His liability in the firm will be limited to the extent of his share in the firm, and his private property cannot be attached by creditors.

On his attaining majority, he has to decide within six months whether he will remain regular partner or withdraw himself from partnership. The choice in either case is to be intimated through a public notice, failing which he will be treated to have decided to continue as a partner, and he becomes personally liable like other partners for all the debts and obligations of the firm from the date of his admission to its benefits (and not from the date of his attaining the age of majority). He also becomes entitled to file a suit against other partners for his share of profit and property.

7. **Other partners:** In partnership firms, several other types of partners are also found, namely, secret partner who does not want to disclose his relationship with the firm to the general public. Outgoing partner, who retires voluntarily without causing dissolution of the firm, limited partner who is liable only up to the value of his capital contributions in the firm, and the like.

#### IV. Higher Order Thinking Skills (HOTS)

**Question 1. X is interested in the floatation of a company. Briefly discuss the steps he should take.**

**Answer:** Stages in the formation of a company: The formation of a company involves the following four stages:

1. Promotion,
2. Incorporation,
3. Subscription of capital,
4. Commencement of business.

These four stages are relevant for formation of a public limited company. For a private limited company, only the first two stages are needed.

1. **Promotion:** Promotion stage includes all the steps right from the identification of a business opportunity till the company is formed. All the tasks during the stage of promotion are performed by a promoter.
2. **Incorporation of the company:** It means registration of the company under Companies Act, 1956. This second stage involves the following steps:
  1. Filing of documents: An application to the registrar for incorporation must be accompanied with the following documents:
    - (i) Memorandum of Association.
    - (ii) Articles of Association or statement in lieu of the prospectus (in case table A is adopted by Public Limited Company).

- (iii) Written consent of proposed directors.
- (iv) Agreement (if any) with proposed managing director, manager, etc.
- (v) Copy of registrar's letter approving the company's name.
- (vi) Statutory declaration.
- (vii) Notice of the exact address of the registered office
- 2. **Payment of fees:** Along with the above documents, necessary fees is to be paid.
- 3. **Certificate of Incorporation:** The registrar issues a certificate of incorporation after being satisfied. Certificate is a conclusive evidence of regularity of incorporation of a company irrespective of any deficiency in its registration.
- 3. **Capital subscription:** In the stage, following steps are required to be followed by public company to raise funds from the public:
  - o SEBI approval;
  - o Filling of prospectus or statement in lieu of prospectus;
  - o Appointment of bankers, brokers and underwriters;
  - o Minimum subscription;
  - o Application to stock exchange.
- 4. **Commencement of business:** In this stage, public company makes an application (along with some documents) to registrar for issue of "Certificate of Commencement of Business". The registrar issues the certificate after being satisfied. The company can start its business activities from the date of issue of the certificate.

## Question 2. Distinguish between Joint Hindu Family Business and Partnership.

Answer:

1. **Regulating law:** A partnership is governed by the provisions of the Indian Partnership Act, 1932. A Joint Hindu Family business is governed by the principles of Hindu law.
2. **Mode of creation:** A partnership arises out of a contract, whereas a Joint Hindu family business arises by the operation of law and is not the result of a contract.
3. **Admission of new members:** In a partnership no new partner is admitted without the consent of all the partners, while in the case of a Joint Hindu family firm a new member is admitted just by birth.
4. **The position of females:** In a partnership women can be full-fledged partners, while in a Joint Hindu family business membership is restricted to male members only. After the passage of the Hindu Succession Act, 1956, females get only co-sharer's interest at the death of a coparcener and they do not become coparceners themselves.
5. **Number of members:** In partnership the maximum limit of partners is 10 for banking business and 20 for any other business but there is no such maximum limit of members in the case of Joint Hindu Family business.
6. **Authority of members:** In partnership each partner has an implied authority to bind his co-partners by act done in the ordinary course of the business, there being mutual agency between various partners.  
In a joint family business all the powers are vested in the 'Karta' and he is the only representative of the family who can contract debts or bind his coparceners by acts done in the ordinary course of business, there being no mutual agency between various coparceners.
7. **Liability of members:** In partnership, the liability of the partners is joint and several as well as unlimited. In other words, each partner is personally and jointly liable to an unlimited extent and if partnership liabilities cannot be fully discharged out of the partnership property each partner's separate personal property is liable for the debts of the firm. In a Joint Hindu family business only the 'Karta' is personally liable to an unlimited extent, i.e., his self-acquired or other separate property besides his share in the joint family property is liable, for debts

contracted on behalf of the family business. Other coparceners' liability is limited to the extent of their interest in the joint family property and they do not incur any personal liability.

8. **Right of members to share in profits:** In a partnership each partner is entitled to claim his separate share of profits but a member of a Joint Hindu family business has no such right. His only remedy lies in a suit for partition.

**Question 3. Explain the factors which affect the choice of form of business organization.**

**Answer:** The following factors are important for taking decision about form of organization.

1. **Cost and Ease in Setting up the Organization:** Sole proprietorship is least expensive and can be formed without any legal formalities to be fulfilled. Company is most expensive with a lot of legal formalities.
2. **Capital Consideration:** Business requiring less amount of finance prefer sole proprietorship and partnership form, where as business activities requiring huge financial resources prefer company form.
3. **Nature of Business:** If the work requires personal attention such as tailoring unit, hair cutting saloon, it is generally set up as a sole proprietorship. Units engaged in large scale manufacturing are more likely to be organized in company form.
4. **Degree of Control Desired:** A person who desires full and exclusive control over business prefers proprietorship rather than partnership or Co. because control has to be shared in these cases.
5. **Liability or Degree of Risk:** Projects which are not very risky can be organized in the form of sole proprietorship and partnership. Whereas the risky ventures should be done in company form of organization because the liability of shareholders is limited.

**Question 4. Which form of business is suitable for following types of business and why?**

- (a) Beauty Saloon;  
(b) Garments shop;  
(c) Garment Factory.

**Answer: (a) Beauty Saloon: Sole Proprietor is the right form of business because:**

- It needs limited capital.
- It is easy to form.
- Entire profits will belong to the owner.
- It requires personal attention.

**(b) Garments Shop: Sole Proprietor is the right form of business because:**

- It needs limited capital.
- It is easy to form.
- Entire profits will belong to the owner.

**(c) Garment Factory: Partnership is more suitable because:**

- It can be easily started and closed without any legal formalities.
- He is not expected to share his business decisions and secrets with anybody.
- Direct relationship between efforts and reward provide incentive to the sole trader to work hard.
- The sole trader can maintain personal contacts with his customers and employees.



- It provides employment to persons with limited money who are not interested to work under others. It prevents concentration of wealth in a few hands.

**Question.5. Differentiate between a Joint Stock Company and a Cooperative Society.**

**Answer.** The main differences between Cooperative Organisation and Company Organisation are given below:

1. **Governing statute:** A company is governed by the Companies Act, 1956 while a co-operative organisation is subject to the provisions of the Cooperative Societies Act, 1912 or State Cooperative Societies Acts.
2. **Basic objects:** The primary objective of a cooperative society is to provide service, whereas a company seeks to earn profits. This does not mean that a cooperative society does not earn profits or a company does not render service to society. It simply means that all the activities of a cooperative society are guided by service motive and profits are incidental to this objective. On the other hand, the activities of a company are inspired by profit taking and services rendered to society are incidental to profit motive.
3. **Number of members:** The minimum number of persons is 7 in a public company and 2 in a private company. A cooperative requires at least 10 members. The maximum number of members is 50 in a private company and 100 in cooperative credit society. There is no maximum limit in case of public companies and non-credit cooperative societies.
4. **Member's liability:** The liability of members of a company is generally limited to the face value of shares held or the amount of guarantee given by them though the Companies Act permits unlimited liability to companies. The members of a cooperative society can opt for unlimited liability. But in practice their liability is generally limited.
5. **Management and control:** The management of a cooperative society is democratic as each member has one vote and there is no system of proxy. In a company, the number of votes depends upon the number of shares and proxies held by a member. There is little separation between ownership and management in a cooperative society due to limited and local membership.
6. **Distribution of surplus:** The profits of a company are distributed as dividends in proportion to the capital contributed by the members. In a cooperative society a minimum part of surplus must be set aside as a reserve and for the general welfare of the public. The rest is distributed in accordance with the patronage provided by different members after paying dividend up to 10 per cent on capital.
7. **Share capital:** In a company, one member can buy any number of shares but an individual cannot buy more than 10 per cent of the total number of shares or shares worth Rs 1,000 of a cooperative society.  
A public company must offer new shares to the existing members while a cooperative society issues new shares generally to increase its membership.  
The subscription list of a cooperative society is kept open for new members whereas, the subscription list of a company is closed after subscriptions. A company is thus capitalistic in nature while a cooperative society is socialistic.
8. **Transferability of interest:** The shares of a public limited company are freely transferable while the shares of cooperative society cannot be transferred but can be returned to the society in case a member wants to withdraw his membership. A member of a cooperative society can withdraw his capital by giving a notice to the society. A shareholder, on the other hand, cannot demand back his capital from the company until it's winding up.



### Question 6. How is a partnership firm different from a sole proprietorship?

**Answer:** The difference between a partnership and sole proprietorship form of business may be as follows. This helps the entrepreneur in selecting form of business of his choice.

- **Membership:** Partnership is owned by two or more persons subject to the limit ten in banking business and twenty in case of other business. Sole proprietorship is owned by one and only one person.
- **Formation:** It is formed through an agreement which may be oral or in writing, is formed quite easily as it is the outcome of a single person's decision without any legal administrative approval.
- **Registration:** The registration is not compulsory. It needs no registration except some compliance.
- **Regulating law:** It is governed by the rules contained under the Indian Partnership Act, 1932. There is no specific statutory law to govern the functioning of sole proprietors business.
- **Capital:** There is more scope for raising a larger amount of capital as there are more than one person. It has a limited financial capability. Hence, the scope for rising capital is naturally least.
- **Quickness in decision-making:** Decision-making in partnership is corporately delayed as the partners arrive at decision after consultation with one another. The decision of the sole proprietor is prompt as he need not consult anyone.
- **Maintenance of secrecy:** Maintenance of absolute secrecy is not possible if partnership as business secrets are accessible to more than one partners. The sole proprietor need not share his business secrets with anybody.
- **Management:** Every partner has the right to take active part in the management of the business. Each partner also enjoys the authority to bind the firm and other partners for his acts in the ordinary course of business. The sole proprietorship is self-managed one and a few employees may support him. However, the decision of the proprietor is final and binding.
- (i) **Risk:** The risk connected with the business is comparatively less as it is shared by all the partners. The risk of the sole proprietor is greater than that of partnership form of business.
- (j) **Duration:** It continues as long as the partners desire. Even though legally it comes to an end on the death, insolvency or retirement of any of the partners, the business is continue with the remaining partners. It comes to an end with the death, insolvency incapacity of the proprietor. Thus, there is uncertainty of duration of sole proprietorship

### V. Value Based Questions

#### Question 1. From social welfare point of view, which type of organization is most desirable from employment generation point of view?

**Answer:** Sole Proprietorship is most desirable from employment generation point of view because it is done at a small scale and small scale labour intensive methods are used. It will create more employment opportunities.

#### Question 2. Which value is of utmost importance when partnership form of business is used?

**Answer:** Maintaining trust and confidentiality of information is of utmost importance in a partnership business.

It is also important to use mutual agency in utmost good faith keeping in mind the interests of all partners.

# **NCERT SOLUTIONS For Class 11 Business Studies**

## **<http://freehomedelivery.net/Solutions Chapter 3 Private, Public and Global Enterprises>**

### **Class 11 Business Studies Solutions Chapter 3 Private, Public and Global Enterprises**

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#### **I. Multiple Choice Questions**

**Question 1. A government company is any company in which the paid up capital held by the government is not less than**

- (a) 49 per cent (b) 51 per cent  
(c) 50 per cent (d) 25 per cent

**Question 2. Centralised control in MNC's implies control exercised by**

- (a) Branches (b) Subsidiaries  
(c) Headquarters (d) Parliament

**Question 3. PSE's are organizations owned by**

- (a) Joint Hindu Family (b) Government  
(c) Foreign companies (d) Private entrepreneurs

**Question 4. Reconstruction of sick public sector units is taken up by**

- (a) MOFA (b) MoU  
(c) BIER (d) NRF

**Question 5. Disinvestments of PSE's implies**

- (a) Sale of equity shares to private sector/public  
(b) Closing down operations  
(c) Investing in new areas  
(d) Buying shares of PSE's

**Answers:**

1. (b) 2. (c) 3. (b) 4. (c) 5. (a)

#### **II. Short Answer Type Questions**

**Question 1. Explain the concept of Public Sector and Private Sector.**

**Answer:** Private sector consists of business owned by individuals or a group of individuals. Examples of private sector include sole proprietorship, partnership, Joint Hindu Family system, cooperative and company. On the other hand, the public sector consists of various organizations owned and managed by the government, owned either wholly or partly by the central or the state government. These may be part of a ministry or come into existence by a special act of the parliament. Public sector works for social welfare while private sector works for profit motive. Public sector organizations may take form of departmental undertaking, statutory corporation and a government company. Private sector may take form of sole proprietorship, partnership, Joint Hindu Family, company or a cooperative.

**Question 2. State the various types of organizations in the private sector.**

**Answer:** Various types of organizations in the private sector include:

1. **Sole Proprietorship:** Sole proprietorship refers to a form of business organization which is owned, managed and controlled by an individual who is the recipient of all profits and bearer of all risks.
2. **Hindu Undivided Family Business:** It refers to a form of organization wherein the business is owned and carried by the members of the Hindu Undivided Family (HUF).
3. **Partnership:** Partnership is the relation between persons who have agreed to share the profit of the business carried on by all or any one of them acting for all.
4. **Cooperative Society:** Cooperative society is a voluntary association of persons, who join together with the motive of welfare of the members.
5. **Joint Stock Company:** A company is an association of persons formed for carrying out business activities and has a legal status independent of its members.
6. **Multinational Corporations:** An MNC is a company whose business operations extend beyond the country in which it has been incorporated.

**Question 3. What are the different kinds of organizations that come under the public sector?**

**Answer:** Following are the different kinds of organizations that come under the private sector.

1. **Departmental Undertaking:** This is the oldest and traditional form of public enterprises. It is managed by government officials as one of the government departments. It is under the control of concerned minister of the department, who is answerable to government through parliament.
2. **Statutory Corporation:** Statutory Corporation is a corporate body with a separate legal existence, set up under a special act of parliament or of the state legislature.
3. **Government Company:** According to the Indian Companies Act 1956, a government company means any company in which not less than 51 per cent of the paid up capital is held by the government or by any state government or partly by central government and partly by one or more state governments.

**Question 4. List the names of some enterprises under the public sector and classify them.**

**Answer:** Some of the enterprises under the public sector are as follows:

Railways	Departmental Undertaking
Reserve Bank of India	Statutory Corporation
Life Insurance Corporation of India	Statutory Corporation
The Hindustan Steel Limited	Government Company
Coal India Limited	Government Company
Post and Telegraph Department.	Departmental Undertaking
Food Corporation of India	Statutory Corporation
State Financial Corporation	Statutory Corporation
Damodar Valley Corporation	Statutory Corporation
Hindustan Machine Tools	Government Company
State Trading Corporation of India	Statutory Corporation
Hindustan Aircrafts Limited	Government Company

**Question 5. Why is the government company form of organization preferred to other types in the public sector?**

**Answer:** Government company form of organization is preferred to other forms of organizations due to its advantages over other forms. These advantages are as follows:

- It is registered or incorporated under Companies Act.
- It has a separate legal entity.
- Management is regulated by the provision of Companies Act.
- Employees are recruited and appointed as per the rules and regulations contained in Memorandum and Articles of Association.
- The government company obtains its funds from government shareholdings and other its private shareholdings. It can also raise funds from capital market.
- It can be easily formed as per the provision of Companies Act. Only an executive decision of government is required.
- It enjoys autonomy in management decisions and flexibility in day to day working.
- It can appoint professional managers on high salaries.

**Question 6. How does the government maintain a regional balance in the country?**

**Answer:** The government is responsible for developing all regions of a country. Earlier, most of the development was limited to few areas like port towns. For providing employment to the people and for accelerating the economic development of backward areas many industries were set up by public sector in those areas.

1. Four major steel plants “were set up in the backward areas to accelerate economic development.
2. The government also makes efforts to prevent mushrooming growth of private sector units in already advanced regions.
3. Government provided many incentives to private sector like tax concessions, loan at cheap rate of interest etc. to motivate them to set up industries in backward regions.

**III. Long Answer Type Questions**

**Question 1. Describe the Industrial Policy 1991, towards the public sector.**

**Answer:** Development of a country originates from industrial development. Industrially developed countries are also economically prosperous. The 2nd Five Year Plan also called the Mahalanobis Model led to the promotion of heavy and key industries in India. The period 1950 onwards witnessed development of infrastructure, research and development, establishment of large scale along with many small scale industries, co-existence of public and private sector enterprises, growth of both consumer and capital goods industries. The industrial sector made a significant contribution to agriculture and trade.

The industrial policy plays a key role in influencing the foreign trade policy, fiscal policy, the monetary policy, the economic policy of the country. Government of India declared its 1st Industrial Policy Resolution (IPR) in 1948. It divided the industries into four categories.

1. Industries that were to be state monopolies. These were limited to atomic energy, arms and ammunition and railways (3 in all).
2. Basic industries in which the state would have the exclusive right to new investment- 6 industries were included in this – iron and steel, ship building, mineral oils, coal, aircraft production and telecommunication equipments.
3. Industries of national importance that the state might regulate and license in consultation with state government. 18 industries were placed in this category.



4. All other industries that would be opened to the private sector without constraints. IPR 1948 remained in force till 1956. Two developments had taken place. One; the first plan which was initiated in 1951 was completed. Second, Parliament accepted socialistic pattern of society. This led to IPR 1956.

**Special features of IPR 1956 were as follows:**

1. Specific and all important roles assigned to the public sector – all industries were classified into 3 groups. These groups were called schedule A,B,C.
    - Schedule A – Exclusive responsibility of state. There were 17 industries in this.
    - Schedule B – Progressively state owned – 12 industries.
    - Schedule C – Generally left to private sector. The state reserved the right to enter this if need be.
  2. Protection to cottage and small scale industries.
  3. Cautious approach towards foreign capital.
- IPR 1956 remained the basis of industrial policy till 1991.

**Question 2. What was the role of the public sector before 1991?**

**Answer:** Before 1991, public sector was supposed to perform the following role in India:

1. **Rapid Economic Development:** It was required to make efforts so that the rate of economic development accelerates.
2. **Provision of Infrastructure:** Another expectation from public sector was to provide infrastructure in the form of better roads, more hospitals, more schools, better irrigation facilities etc.
3. **Sound Industrial Base:** We also needed public sector to develop a sound industrial base because Private Sector either did not have huge capital required for these or were not interested in this sector as they had a long gestation period.
4. **Development of Backward Regions:** Public sector also aimed at developing backward regions as it is necessary for the balanced development of a country. Private sector being profit minded does not take interest in investing in backward regions.
5. **Generation of Surplus:** Another expectation from public sector was to generate a surplus that could be used for investment in other sectors whereby the growth rate could be accelerated.
6. **Creation of Employment Opportunities:** Public sector also played its role in creating employment opportunities in organized sector so that poverty can be reduced and standard of living can be enhanced.
7. **Control of Monopoly and Restrictive Trade Policies:** Public sector also aimed at controlling monopoly and restrictive trade policies. Otherwise few private industrialists would have gained extreme economic power. It could be harmful for the nation as a whole.
8. **Serving of Strategic National Interests:** Public sector also plays its role in serving strategic national interests. They provide law and order, administrative services, police, defence, and many infrastructural facilities even when they are not given any profit as such in monetary terms.

**Question 3. Can the public sector companies compete with the private sector in terms of profits and efficiency? Give reasons for your answer.**

**Answer:** It is difficult for a public sector undertaking to compete with a private sector undertaking in terms of profits due to following reasons:

1. **Motive of public sector is not profit:** Public sector works not for profit but for social welfare. It gives first priority to social welfare then it is almost impossible for it to compete with private sector enterprise on the basis of profit which mainly works for profit only.
2. **Public sector takes care of strategic industries:** Public sector invests in strategic areas even when these industries have low return generating capacity and long gestation period. These industries do not give monetary returns but if we consider their return in development of our economy otherwise their return is really high.
3. **Public sector provides many facilities free of cost to the weaker section of society:** We can't expect a government hospital or a government school to generate profits. Many public sector undertakings provide many facilities for free or at a very low cost due to the benefits that it gives to other sectors of the society.

It is difficult for a public sector undertaking to compete with a private sector undertaking in terms of efficiency due to following reasons:

1. **Dependence on authorities for taking minor decisions:** Public Sector undertakings follow a protocol for everything. It leads to delay in decision making and inefficiency in operations.
2. **Job security:** Workers of Public Sector enjoy job security. It reduces their performance as they know that in spite of bad performance there is no fear of losing job.
3. **Red tapism and bureaucracy:** In public sector undertakings there is red tapism and bureaucracy. It leads to inefficiency in operations.

#### Question 4. Why are global enterprises considered superior to other business organizations?

**Answer:** Global enterprises are considered superior to other business organizations because it has following advantages which other business organizations may not have.

1. **Huge capital resources:** MNCs possess huge capital resources and they are able to raise lot of funds from various sources.
2. **International operations:** A MNC has production, marketing and other facilities in several countries.
3. **Centralized control:** MNCs have headquarters in their home countries from where they exercise their control over all branches and subsidiaries. It provides only broad policy, framework to them and there is no interference in their day to day operations.
4. **Foreign collaboration:** Usually they enter into agreements relating to sale of technology, production of goods, use of brand name etc. with local firms in the host country
5. **Advanced technology:** These organisations possess advanced and superior technology which enable them to provide world class products and services.
6. **Product innovations:** MNCs have highly sophisticated research and development departments. These are engaged in developing new products and superior design of existing products.
7. **Marketing strategies:** MNCs use aggressive marketing strategies. Their brands are well known and spend huge amounts on advertising and sale promotion.

#### Question 5. What are the benefits of entering into joint ventures?

**Answer:** Benefits of joint ventures are as follows:

1. **Greater resources and capacity:** In a joint venture the resources and capacity of two or more firms are combined which enables it to grow quickly and efficiently.

2. **Access to advanced technology:** It provides access to advanced techniques of production which increases efficiency and then helps in reduction in cost and improvement in quality of product.
3. **Access to new markets and distribution network:** A foreign company gains access to the vast Indian market by entering into a joint venture with Indian company. It can also take advantage of the well established distribution system of local firms.
4. **Innovation:** Foreign partners in joint ventures have the ideas and technology to develop innovative products and services. They have an advantage in highly competitive and demanding markets.
5. **Low cost of Production:** Raw materials and labour are comparatively cheap in developing countries so if one partner is from developing country they can be benefited by the low cost of production.
6. **Well known brand names:** When one party has well established brands and goodwill, the other party gets its benefits. Products of such brand names can be easily launched in the market.

## MORE QUESTIONS SOLVED

### I. Multiple Choice Questions

**Question 1. Which of the following is a departmental undertaking?**

- (a) Life Insurance Corporation Limited (b) Railways  
(c) Bharat Heavy Electrical Limited (d) All of the above

**Question 2. In which form of public sector enterprise, private individuals can also become shareholders?**

- (a) Departmental Undertaking (b) Government Company  
(c) Statutory Corporation (d) None of the above

**Question 3. Which of the following is most suitable when purpose is to generate revenue for the government?**

- (a) Departmental Undertaking (b) Government Company  
(c) Statutory Corporation (d) None of the above

**Question 4. Which of the following is most suitable when national security is of utmost importance?**

- (a) Departmental Undertaking (b) Government Company  
(c) Statutory Corporation (d) None of the above

**Question 5. Steel Authority of India Limited (SAIL) is an example of:**

- (a) Departmental Undertaking (b) Government Company  
(c) Statutory Corporation (d) None of the above

**Question 6. Which of the following is an example of Statutory Corporation?**

- (a) Life Insurance Corporation Limited (b) Railways  
(c) Bharat Heavy electrical Limited (d) All of the above

**Question 7. BIFR stands for:**

- (a) Bureau of Industrial and Financial Reconstruction  
(b) Board of Industrial and Financial Reconstruction  
(c) Board of Indian Financial Reconstruction  
(d) Board of Industrial and Financial Reformation

**Question 8. Which of the following has 51% of the capital from government?**

- (a) Departmental Undertaking (b) Government Company  
(c) Statutory Corporation (d) None of the above

**Question 9. Which of the following is under the control of a ministry?**

- (a) Departmental Undertaking (b) Government Company

(c) Statutory Corporation (d) None of the above

Question 10. Which of the following is controlled and managed as per the provisions of the statute under which it has been formed?

(a) Departmental Undertaking (b) Government Company

(c) Statutory Corporation (d) None of the above

Question 11. When two or more businesses join hands for mutual benefit and common purpose, it is called:

(a) Public Private Partnership (b) Joint Venture

(c) Global Enterprises (d) Statutory Corporation

Question 12. Which year brought a drastic change in the role of public sector in India?

(a) 1951 (b) 1956

(c) 1991 (d) 2001

Question 13. Memorandum of Understanding (MOU) is a term used in context of:

(a) Public Private Partnership (b) Joint Venture

(c) Changing role of public Sector (d) All of the above

Question 14. Employees of which of the following are considered as government employees?

(a) Departmental Undertaking (b) Government Company

(c) Statutory Corporation (d) None of the above

Question 15. Since 1991, number of has increased in India.

(a) Departmental Undertaking (b) Government Company

(c) Statutory Corporation (d) Global Enterprises

Answer:

1. (b) 2. (b) 3. (b) 4. (a) 5. (c)

6. (a) 7. (b) 8. (b) 9. (a) 10. (c)

11. (b) 12. (c) 13. (d) 14. (a) 15. (d)

## II. Short Answer Type Questions

Question 1. What is the difference between Public and Private sector?

Answer: Differences between public and private sectors are summarised in the table given below:

Basis	Public Sector	Private Sector
Ownership	These are owned by the government-central or state.	These are owned by individuals or group of individuals.
Aim	It aims at social welfare.	It aims at profit maximisation.



<b>Efficiency</b>	It is likely to be less efficient due to lack of autonomy and too much interference.	It is likely to be more efficient due to quick decision making.
<b>Management Control</b>	It is subject to control from the government.	It is controlled only by business laws but not directly by the government.
<b>Accountability</b>	These are accountable to the government.	These are accountable to the owners.
<b>Example</b>	Railways, BHEL, LIC Ltd, SAIL, GAIL	Reliance Industries Limited, Partnership firms, HUF, Cooperatives etc.

## Question 2. Discuss the merits and demerits of Departmental Undertaking.

**Answer:** These are established as departments of the ministry and are financed, managed and controlled by either central government or state government. Examples: Indian railways, post and telegraph.

### Features

- **No separate entity:** It does not have separate legal entity.
- **Finance:** It is financed by annual budget allocation of the government and all its earnings go to government treasury.
- **Accounting and Audit:** The government rules relating to audit and accounting are applicable to it.
- **Staffing:** Its employees are government employees and are recruited and appointed as per government rules.
- **Accountability:** These are accountable to the concerned ministry.

### Merits

- It is more effective in achieving the objective laid down by government as it is under the direct control of govt.
- It is a source of government income as its revenue goes to government treasury.
- It is accountable to parliament for all its actions which ensures proper utilisation of funds.
- It is suitable for activities where secrecy and strict control is required like defence production.

### Demerits

- It suffers from interference from minister and top officials in their working. .
- It lacks flexibility which is essential for smooth operation of business.
- It suffers from red tapism in day to day work.
- These organizations are usually insensitive to consumer needs and do not provide goods and adequate service to them.
- Such organisations are managed by civil servants and government officials who may not have the necessary expertise and experience in management.

### Question 3. Explain three trends indicating changing role of public sector.

**Answer:** The changing role of public sector is clear from the following trends:

1. **Restricting the role of public sector only to critical areas:** The reservation of industries exclusively for the public sector has been reduced from 17 to 8 and further to 3 only.
2. **Performance improvement through Memorandum of Understanding (MOU):** Under this government lays down performance targets for the management and gives greater autonomy to hold the management accountable for the results.
3. **Disinvestment:** Equity shares of public sector enterprises were sold to private sector and the public. It was expected that this would lead to improved managerial performance and better financial discipline.
4. **Restructure and Revival:** All public sector sick units were referred to Board of Industrial and Financial Reconstruction (BIFR). Units which were potentially viable were restructured and which could not be revived were closed down by the board.

### III. Long Answer Type Questions

#### Question 1. Define Joint Venture and explain its major benefits.

**Answer: Meaning:** When two or more independent firms together establish a new enterprise by pooling their capital, technology and expertise, it is known as a Joint Venture. Example: Hero Cycle of India and Honda Motors Co. of Japan jointly established Hero Honda. Similarly Suzuki Motors of Japan and Govt. of India come together to form Maruti Udyog.

#### Benefits

1. **Greater resources and capacity:** In a joint venture the resources and capacity of two or more firms are combined which enables them to grow quickly and efficiently.
2. **Access to advanced technology:** It provides access to advanced techniques of production which increases efficiency and then helps in reduction in cost and improvement in quality of product.
3. **Access to new markets and distribution network:** A foreign company gain access to the vast Indian market by entering into a joint venture with Indian company. It can also take advantage of the well established distribution system of local firms.
4. **Innovation:** Foreign partners in joint ventures have the ideas and technology to develop innovative products and services. They have an advantage in highly competitive and demanding markets.
5. **Low cost of production:** Raw materials and labour are comparatively cheap in developing countries so if one partner is from developing country they can be benefited by the low cost of production.
6. **Well known brand names:** When one party has well established brands and goodwill, the other party gets its benefits. Products of such brand names can be easily launched in the market.

#### Question 2. Explain the main features of Multinational Company.

**Answer:** Multinational Company may be defined as a company that has business operations in several countries by having its factories, branches or offices in those countries. But it has its head quarter in one country in which it is incorporated. Example: GEC, IBM, PHILIPS, COCA-COLA etc.

#### Features

1. **Huge capital resources:** MNCs possess huge capital resources and they are able to raise lot of funds from various sources.

2. **International operations:** A MNC has production, marketing and other facilities in several countries.
3. **Centralised control:** MNCs have headquarters in their home countries from where they exercise control over all branches and subsidiaries. It provides only broad policy framework to them and there is no interference in their day to day operations.
4. **Foreign collaboration:** Usually they enter into agreements relating to sale of technology, production of goods, use of brand name etc. with local firms in the host country.
5. **Advanced technology:** These organisations possess advanced and superior technology which enable them to provide world class products and services.
6. **Product innovations:** MNCs have highly sophisticated research and development departments. These are engaged in developing new products and superior design of existing products.
7. **Marketing strategies:** MNCs use aggressive marketing strategies. Their brands are well known and spend huge amounts on advertising and sale promotion.

**Question 3. Differentiate between Statutory Corporation, Departmental Undertaking and Government Company.**

**Answer:** Differences between Statutory Corporation, Departmental Undertaking and Government Company are summarized in the table given below:

<b>Basis</b>	<b>Statutory Corporation</b>	<b>Departmental Undertaking</b>	<b>Government Company</b>
<b>Formation</b>	By a special act of Parliament or State Legislature	By a Ministry	Under Companies Act with or without Private Sector participation
<b>Ownership</b>	Wholly owned by the Government	Wholly owned by the Government	At least 51% share capital is held by the Government.
<b>Autonomy</b>	Sufficient	No Autonomy	Highest
<b>Legal Status</b>	Separate legal entity	No separate legal entity	Separate legal entity
<b>Public Accountability</b>	Moderate	Highest	Low
<b>Personnel</b>	Not government employees but hired under a contract of service	Government employees	Not government employees but hired under a contract of service
<b>Funds</b>	Financed from its own resources which may include issue of shares and debentures.	Financed from government budget	Financed from its own resources which may include issue of shares and debentures.
<b>Suitability</b>	Industrial and commercial undertakings	Defense, services of public utility like education, health etc.	Industrial and commercial undertakings
<b>Example</b>	LIC, GIC, SBI, RBI etc.	Railways, Post and Telegraph	SAIL, GAIL, BHEL etc.

#### **Question 4. Explain the merits and demerits of public-private partnership.**

**Answer:** Public private partnership also called PPP or p3 is a contract between government and private business firms for the provision of public assets and/or public services.

##### **Merits**

- **Inflow of private investment:** PPP attracts private investment which is of utmost importance to undertake such essential projects.
- **Increased efficiency:** Involvement of private sector will bring efficiency in implementation of projects and cut down cost and time.
- **Innovation:** It helps in bringing innovative design and constructive practices.
- **Better economic viability:** Involvement of experienced and creditworthy sponsors and commercial lenders can increase economic viability of the projects.
- **Risk sharing:** The structuring of a PPP project allocates the risks to the agency which can handle it most suitably.

##### **Demerits**

- **Increased cost:** Cost of production increases for the government as private sector also demands its profit share for the money it invests.
- **Control gets divided:** Control gets divided between private and public sector. Government remains involved in all stages and private sector, is responsible for more commercial functions like project design, construction, finance and operations.

#### **Question 5. What is Statutory Corporation? Explain its features, merits and demerits.**

**Answer:** It is established under a special act passed in parliament or state legislative assembly. Its objectives, powers and functions are clearly defined in the Statute /Act. Examples include Unit Trust of India, Life Insurance Corporation of India, Steel Authority of India Limited etc.

##### **Features**

- It is established under a special act which defines its objects, powers and functions.
- It has a separate legal entity.
- Its management is vested in a Board of Directors appointed or nominated by the government.
- It has its own staff, recruited and appointed as per the provisions of act.
- This type of enterprise is usually independently financed. It obtains funds by borrowing from government or from public or through earnings.
- It is not subject to same accounting and audit rules which are applicable to Government Department.

##### **Merits**

- **Internal autonomy:** It enjoys a good deal of autonomy in its day to day operations and is free from political interference.
- **Quick decisions:** It can take prompt decisions and quick actions as it is free from the prohibitory rules of government.
- **Parliamentary control:** Their performance is subject to discussion in Parliament which ensures proper use of public money.
- **Efficient management:** Their Directors and top Executives are professionals and experts of different fields.



## Demerits

- **Flexibility is for name sake only:** In reality, there is not much operational flexibility. It suffers from lot of political interference.
- **Lack of profit motive:** Usually they enjoy monopoly in their field and do not have profit motive due to which their working turns out to be inefficient.
- **Corruption:** Where there is dealing with public, rampant corruption exists. Thus public corporation is suitable for undertaking requiring monopoly powers e.g., public utilities.

## Question 6. Give the meaning of Government Company. Explain three merits and three limitations of Government Company.

**Answer.** A Government Company is a company in which not less than 51% of the paid up share capital is held by the central government; or state government or jointly by both. Hindustan Insecticides Ltd., State Trading Corporation of India, Hindustan Cables Ltd.etc are some of the examples.

### Features

- It is registered or incorporated under Companies Act.
- It has a separate legal entity.
- Management is regulated by the provision of Companies Act.
- Employees are recruited and appointed as per the rules and regulations contained in Memorandum and Articles of Association.
- The Government Company obtains its funds from government shareholdings and other private shareholdings. It can also raise funds from capital market.

### Merits

- It can be easily formed as per the provision of Companies Act. Only an executive decision of government is required.
- It enjoys autonomy in management decisions and flexibility in day to day working.
- It can appoint professional managers on high salaries.

### Limitations

- It suffers from interference from government officials, ministers and politicians.
- It evades constitutional responsibility, which a company financed by the government should have, as it is not directly answerable to Parliament.
- The board usually consists of the politicians and civil servants who are interested more in pleasing their political bosses than in efficient operation of the company.

## IV. Higher Order Thinking Skills (HOTS)

### Question 1. “The basic rationale of public sector has changed significantly.” In the light of this statement explain any four initiatives taken by the government.

**Answer:** In the industrial policy 1991, the Government of India introduced four major reforms in public sector.

1. **Reduction in number of industries reserved for public sector:** This number is reduced from 17 to 8 and to 3 industries only in 2001. These three industries are atomic energy, arms and rail transport.

2. **Memorandum of Understanding (MOU):** Under this govt, lays down performance targets for the management and gives greater autonomy to hold the management accountable for the results.
3. **Disinvestment:** Equity shares of public sector enterprises were sold to private sector and the public. It was expected that this would lead to improved managerial performance and better financial discipline.
4. **Restructure and revival:** All public sectors, sick units were referred to Board of Industrial and Financial Reconstruction (BIFR). Units which were potentially viable were restructured and which could not be revived were closed down by the board.

**Question 2. “Global enterprises are giant both in size and operations.” Substantiate this statement.**

**Answer:** The statement is absolutely correct that global enterprises are giant both in size and operations.

1. It has huge capital resources.
2. It involves foreign collaboration.
3. It uses advanced technology.
4. It leads to product innovation.
5. It makes use of marketing strategies.
6. It leads to expansion of market territory.
7. It makes use of centralized control.

**Question 3. “MNC’s are in a position to exercise massive control on an economy.” Substantiate.**

**Answer:** MNC’s are in a position to exercise massive control on an economy because of the following reasons:

- MNC’s are characterised by possessing huge financial resources. These huge financial resources give them economic power in the economy. They can afford to survive even during losses as well.
- MNCs possess technological superiorities and are capable of conform to international standards and quality specifications.
- They make use of aggressive marketing strategies for their products.
- They have an established brand image in the market.

## **V. Value Based Questions**

**Question 1. Multinational Companies have done more harm than good. Explain.**

**Answer:** Yes, I agree that Multinational Companies have done more harm than good. It is clear from the following disadvantages which it is creating for the economy.

1. It disregards national priorities.
2. It leads to creation of monopoly.
3. It leads to depletion of natural resources.
4. It leads to technology obsolete .
5. It creates threat to national sovereignty.

**Question 2. “Public sector has changed its role since 1991 a great deal”. Do you agree? Justify your answer.**

**Answer:** The role and importance of public sector changed with passage of time.

1. **Development of infrastructure:** At the time of independence, India suffered from an acute shortage of heavy industries such as engineering, iron and steel, oil refineries, heavy machineries, etc. Because of huge investment requirement and long gestation period, private sector was not willing to enter these areas. The duty of development of basic infrastructure was assigned to public sector which it discharged quite efficiently.
2. **Regional balance:** Earlier, most of the development was limited to a few areas like port towns. For providing employment to the people and for accelerating the economic development of backward areas many industries were set up by public sector in those areas.
3. **Economics of scale:** In certain industries (like electric power plants, natural gas, petroleum, etc) huge capital and large base are required to function economically. Such areas were taken up by public sector.
4. **Control of monopoly and restrictive trade practices:** These enterprises were also established to provide competition to private sector and to check their monopolies and restrictive trade practices.
5. **Import substitution:** Public enterprises were also engaged in production of capital equipments which were earlier imported from other countries. At the same time public sector companies like STC and MMTC have played an important role in expanding exports of the country. Very important role was assigned to public sector but its performance was far from satisfactory which forced government to do rethinking on public enterprises.



# NCERT SOLUTIONS For Class 11 Business Studies

## <http://freehomedelivery.net/Solutions> Chapter 4

### Business Services

#### Class 11 Business Studies Solutions Chapter 4 Business Services

NCERT SOLUTIONS For Class 11 Business Studies <http://freehomedelivery.net/Solutions> Chapter 4  
Business Services

#### I. Multiple Choice Questions

Tick the appropriate answer:

Question 1. DTH services are provided by

- (a) Transport companies (b) Banks  
(c) Cellular companies (d) None of the above

Question 2. The benefits of public warehousing includes

- (a) Control (b) Flexibility  
(c) Dealer relationship (d) None of the above

Question 3. Which of the following is not a function of insurance?

- (a) Risk sharing (b) Assist in capital formation  
(c) Lending of funds (d) None of the above

Question 4. Which of the following is not applicable in Life Insurance contract?

- (a) Conditional contract (b) Unilateral contract  
(c) Indemnity contract (d) None of the above

Question 5. CWC stands for

- (a) Central Water Commission (b) Central Warehousing Commission  
(c) Central Warehousing Corporation (d) Central Water Corporation

Answers:

1. (c) 2. (b) 3. (c) 4. (c) 5. (c)

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#### II. Short Answer Type Questions

Question 1. Define services and goods.

**Answer:** A good is a physical product which can be delivered to a buyer and involves the ownership from seller to customer. For example; mobile phone, book, purse etc. Services are those separately identifiable, essentially intangible activities which provide satisfaction of wants, and are not necessarily linked to the sale of a product or another service. For example, communication services, teaching services, legal services etc.

Question 2. What is e-banking? What are the advantages of e-banking?

**Answer:** E-banking is a service provided by many banks, in which a customer is allowed to conduct banking transactions through internet. It includes ATMs, credit cards, debit cards, mobile banking and internet banking.

**Advantages of e-banking**

##### 1. To Banks

- It provides competitive advantage to a bank.
- Load on different branches gets considerably reduced due to centralised data base.
- Banking network is no more limited to the number of branches. It expands far and wide due to facility of internet banking.

##### 2. To Customers



- It provides 24 hours, 365 days a year service to the consumers.
- It can be used at any place and at any time even while travelling.
- It reduces risk and ensures greater security.
- It increases financial discipline by keeping record of each and every transaction.
- Availability of banking facility at any time and anywhere increases satisfaction of the consumers.

**Question 3. Write a note on various telecom services available for enhancing business.**

**Answer:** Various telecom services available for enhancing business are as follows:

- **Cellular Mobile Services:** These companies provide all types of telecom services like voice and non-voice messages, data services, PCO connectivity etc.
- **Radio Paging Services:** It is one way information broadcasting solution and has spread its reach to a large area. It includes services including tone only, numeric only and alpha/numeric only.
- **Fixed Line Services:** These services utilise any type of network equipment connected through fibre optic cable laid across the length and breadth of the country.
- **Cable Services:** These are linkages and switched services within a license area of operation to operate media services.
- **VSAT Services:** VSAT stands for Very Small Aperture Terminal. It is a satellite based communication service which is highly flexible and reliable communication solution in urban as well as rural areas. It is being used for tele-medicine, newspaper online, tele-education, online trading, e-banking etc.
- **DTH Services:** DTH stands for Direct to Home. It is also a satellite based service provide by cellular companies which allows one to receive media services through a satellite with the help of a small dish antenna and a set up box.

**Question 4. Explain briefly the principles of insurance with suitable examples.**

**Answer:** The principles of insurance are explained below:

1. **Principle of Utmost Good Faith:**

Under this insurance, contract both the parties should have faith over each other. As a client it is the duty of the insured to disclose all the facts to the insurance company. Any fraud or misrepresentation of facts can result into cancellation of the contract.

2. **Principle of Insurable interest:**

Under this principle of insurance, the insured must have interest in the subject matter of the insurance. Absence of insurance makes the contract null and void. If there is no insurable interest, an insurance company will not issue a policy.

An insurable interest must exist at the time of the purchase of the insurance. For example, a creditor has an insurable interest in the life of a debtor, A person is considered to have an unlimited interest in the life of their spouse etc.

3. **Principle of Indemnity:**

Indemnity means security or compensation against loss or damage. The principle of indemnity is such principle of insurance stating that an insured may not be compensated by the insurance company in an amount exceeding the insured's economic loss.

In this type of insurance the insured would be provided compensation with the amount equivalent to the actual loss and not the amount exceeding the loss.

This is a regulatory principle. This principle is observed more strictly in property insurance than in life insurance.

The purpose of this principle is to set back the insured to the same financial position that existed before the loss or damage occurred.

4. **Principle of Subrogation:**

The principle of subrogation enables the insured to claim the amount from the third party responsible for the loss. It allows the insurer to pursue legal methods to recover the amount of loss. For example, if you get injured in a road accident, due to reckless driving of a third party, the insurance company will compensate your loss and will also sue the third party to recover the money paid as claim.

5. **Principle of Contribution:**

If the same subject matter, except life is insured by more than one insurers, then the actual loss will be shared by all the insurers.

6. **Principle of Mitigation:**

It means that the insured should try to minimise the loss of the subject matter of the insurer even if it is insured.

7. **Principle of Proximate Cause:**

Proximate cause literally means the 'nearest cause' or 'direct cause'. This principle is applicable when the loss is the result of two or more causes. The proximate cause means; the most dominant and most effective cause of loss is considered. This principle is applicable when there are series of causes of damage or loss.

### Question 5. Explain warehousing and its functions.

**Answer:** Warehousing refers to holding or keeping of goods from the time of their production or purchase until they are sold or consumed. It removes time gap between production and consumption and thereby creates time utility. In addition to providing services of storage, warehouse also provides logistical service in a cost effective manner.

#### Functions of Warehouses

1. **Consolidation:** There are certain goods which are produced in small quantities but are sold to consumers in bulk quantity. Such goods need consolidation. Warehouses receive goods in small quantities from different producers and dispatch them to consumers in bulk.
2. **Break the Bulk:** This function is just opposite of consolidation. Under it, the warehouse receives the quantity in bulk from the producers and sells them in small quantities to consumer. These small quantities are then sold to customers according to their requirements.
3. **Stock Piling:** Usually there is a time gap between production and consumption of goods. Warehouse fills this gap. It stores those goods which are in surplus i.e., whose supply is more than their demand. When demand exceeds supply, it makes goods available from its own stock.
4. **Value Added Services:** Warehouses also provide some value added services like transit mixing, packaging and labeling.
5. **Price Stabilization:** Warehouses help to equalize demand and supply and thereby stabilize the prices.
6. **Financing:** Warehouse owners advance money to owners of goods on the security of these goods and they also provide these goods on credit to customers.

### III. Long Answer Type Questions

#### Question 1. What are services? Explain their distinct characteristics.

**Answer:** A service is an act or performance offered by one party to another. They are economic activities that create value and provide benefits for customers at specific times and places as a result of bringing desired change. According to Sir William B, "Service refers to social efforts which includes the Govt. to fight five giant evils – wants, disease, ignorance, squalor and illness in the society".

#### Characteristics of Services

Service is an act or performance offered by one party to another. They are economic activities that create value and provide benefits for customers at specific times and places as a result of bringing about a desired change in or on behalf of the recipient of the service. The term, service, is not limited to personal services like medical services, beauty parlors, legal services, etc. According to the marketing experts and management thinkers the concept of services is a wider one. The term services are defined in a number of ways but not a single one is universally accepted. The distinct characteristics of services are mentioned below:

1. **Intangibility:** Services are intangible. We cannot touch them, it is not a physical object. According to Carman and Uhl, a consumer feels that he has the right and opportunity to see, touch, hear, smell or taste the goods before they buy them. This is not applicable to services. The buyer does not have any opportunity to touch, smell, and taste the services. While selling or promoting a service one has to concentrate on the satisfaction and benefit a consumer can derive having spent on these services.  
For example: Railways sells a train ticket from A destination to B destination. Here it is the matter of consumer's perception of services than smelling it or tasting it.
2. **Inventory:** Services too, are perishable like labour. Service has a high degree of perishability. Here the element of time assumes a significant position. There will be complete loss of labour. If labour stops working, it is a complete waste. It cannot be stored. Utilized or unutilized services are an economic waste. An unoccupied building, an unemployed person, credit unutilized, etc. are economic waste. Services have a high level of perishability.
3. **Inseparability:** Services are generally created or supplied simultaneously. They are inseparable. For example, the entertainment industry, health experts and other professionals create and offer their services at the same given time. Services and their providers are associated closely and thus, not separable. Donald Cowell states 'Goods are produced, sold and then consumed whereas the services are sold and then produced and consumed'. Therefore inseparability is an important characteristic of services which proves challenging to service management industry.
4. **Inconsistency:** This character of services makes it difficult to set a standard for any service. The quality of services cannot be standardized. The price paid for a service may either be too high or too low as is seen in the case of the entertainment industry and sports. The same type of services cannot be sold to all the consumers even if they pay the same price. Consumers rate these services in different ways. This is due to the difference in perception of individuals at the level of providers and users. Heterogeneity "makes it difficult to establish standards for the output of service firm.
5. **Involvement:** In the sale of goods, after the completion of process, the goods are transferred in the name of the buyer and he becomes the owner of the goods. But in the case of services, we do not find this. The users have only an access to services. They cannot own the service.  
For example: a consumer can use personal care services or medical services or can use a hotel room or swimming pool. However, the ownership remains with the providers.  
According to Philip Kotler, "A service is an activity or benefit that one party can offer to another that is essentially intangible and does not result in the ownership of anything" From this it is clear that the ownership is not affected in the process of selling the services.

**Question 2. Explain the functions of commercial banks with an example of each.**

**Answer:** The main functions of commercial banks are accepting deposits from the public and advancing them loans.

However, besides these functions there are many other functions which these banks perform. All these functions can be divided under the following heads:

1. Accepting deposits; 2. Giving loans;

3. Overdraft; 4. Discounting of Bills of Exchange;  
5. Investment of Funds; 6. Agency Functions.

**1. Accepting Deposits:**

The most important function of commercial banks is to accept deposits from the public.

Various sections of society, according to their needs and economic condition, deposit their savings with the banks.

For example, fixed and low income group people deposit their savings in small amounts from the points of view of security, income and saving promotion. On the other hand, traders and businessmen deposit their savings in the banks for the convenience of payment.

Therefore, keeping the needs and interests of various sections of society, banks formulate various deposit schemes. Generally, there are three types of deposits which are as follows:

**(i) Current Deposits:**

The depositors of such deposits can withdraw and deposit money whenever they desire. Since banks have to keep the deposited amount of such accounts in cash always, they carry either no interest or very low rate of interest. These deposits are called Demand Deposits because these can be demanded or withdrawn by the depositors at any time they want. Such deposit accounts are highly useful for traders and big business firms because they have to make payments and accept payments many times in a day.

**(ii) Fixed Deposits:**

These are the deposits which are deposited for a definite period of time. This period is generally not less than one year and, therefore, these are called as long term deposits. These deposits cannot be withdrawn before the expiry of the stipulated time and, therefore, these are also called as time deposits.

These deposits generally carry a higher rate of interest because banks can use these deposits for a definite time without having the fear of being withdrawn.

**(iii) Saving Deposits:**

In such deposits, money up to a certain limit can be deposited and withdrawn once or twice in a week. On such deposits, the rate of interest is very less. As is evident from the name of such deposits their main objective is to mobilise small savings in the form of deposits. These deposits are generally done by salaried people and the people who have fixed and less income.

**2. Giving Loans:**

The second important function of Commercial Banks is to advance loans to its customers.

Banks charge interest from the borrowers and this is the main source of their income.

Banks advance loans not only on the basis of the deposits of the public rather they also advance loans on the basis of depositing the money in the accounts of borrowers. In other words, they create loans out of deposits and deposits out of loans. This is called as credit creation by Commercial Banks.

Modern banks give mostly secured loans for productive purposes. In other words, at the time of advancing loans, they demand proper security or collateral. Generally, the value of security or collateral is equal to the amount of loan. This is done mainly with a view to recover the loan money by selling the security in the event of non-refund of the loan.

At times, banks give loan on the basis of personal security also. Therefore, such loans are called unsecured loan. Banks generally give following types of loans and advances:

**(i) Cash Credit:**

In this type of credit scheme, banks advance loans to its customers on the basis of bonds, inventories and other approved securities. Under this scheme, banks enter into an agreement with its customers to which money can be withdrawn many times during a year. Under this set lip banks open accounts of their customers and deposit the loan money. With this type of loan, credit is created.



**(ii) Demand Loans:**

These are such loans that can be recalled on demand by the banks. The entire loan amount is paid in lump sum by crediting it to the loan account of the borrower, and thus entire loan becomes chargeable to interest with immediate effect.

**(iii) Short-term Loan:**

These loans may be given as personal loans, loans to finance working capital or as priority sector advances. These are made against some security and entire loan amount is transferred to the loan account of the borrower.

**3. Over-Draft:**

Banks advance loans to its customer's up to a certain amount through over-drafts, if there are no deposits in the current account. For this, banks demand a security from the customers and charge very high rate of interest.

**4. Discounting of Bills of Exchange:**

This is the most prevalent and important method of advancing loans to the traders for short-term purposes. Under this system, banks advance loans to the traders and business firms by discounting their bills. In this way, businessmen get loans on the basis of their bills of exchange before the time of their maturity.

**5. Investment of Funds:**

The banks invest their surplus funds in three types of securities—Government securities, other approved securities and other securities. Government securities include both, central and state governments, such as treasury bills, national savings certificate etc.

Other securities include securities of state associated bodies like electricity boards, housing boards, debentures of Land Development Banks, units of UTI, shares of Regional Rural banks etc.

**6. Agency Functions:**

Banks function in the form of agents and representatives of their customers. Customers give their consent for performing such functions. The important functions of these types are as follows:

- Banks collect cheques, drafts, bills of exchange and dividends of the shares for their customers.
- Banks make payment for their clients and at times accept the bills of exchange: of their customers for which payment is made at the fixed time.
- Banks pay insurance premium of their customers. Besides this, they also deposit loan installments, income tax, interest etc. as per directions.
- Banks purchase and sell securities, shares and debentures on behalf of their customers.
- Banks arrange to send money from one place to another for the convenience of their customers.

**Question 3. Write a detailed note on various facilities offered by Indian Postal Department.**

**Answer:** Indian Post and Telegraph Department provides various postal services all over India. India has been divided into 22 postal circles for this. There are 1,54,149 post offices in India. It has 5,64,701 letter boxes, which transmits 1575 crore mails every year. 5,01,716 villages have a public telephone and 26000 post offices are connected through the network. It links major 97 countries across the world. It provides speed post facility for over 1000 destinations in India. Facilities of postal department are broadly divided into:

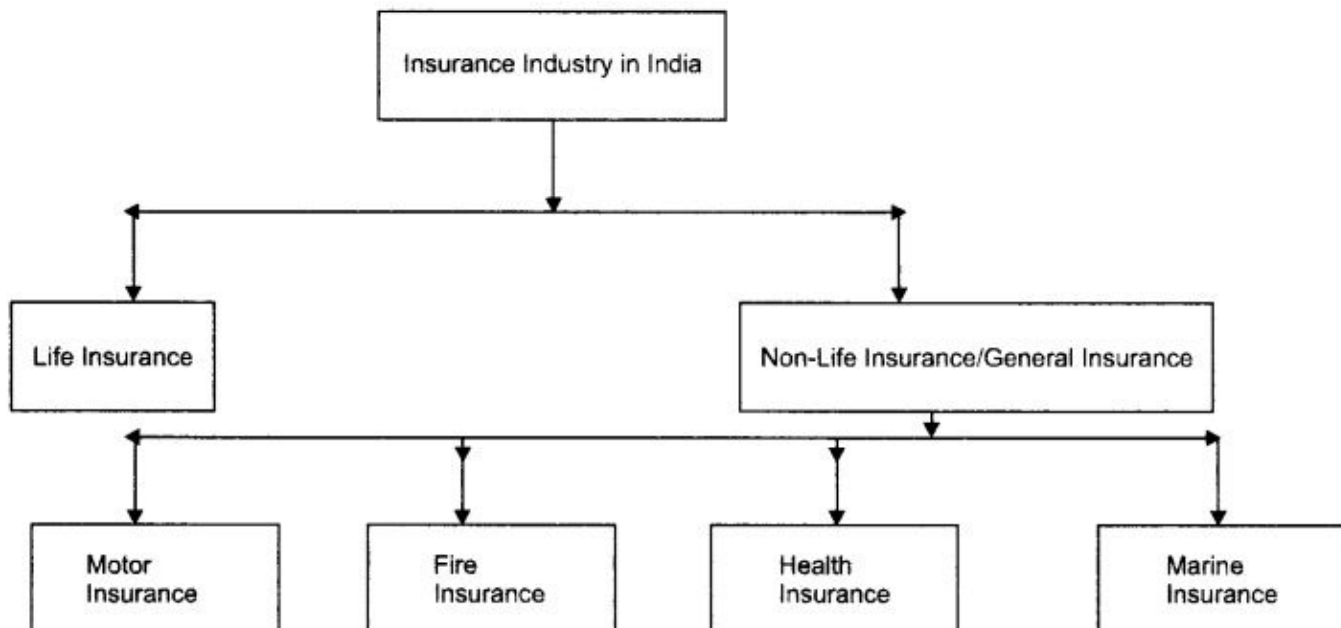
- **Financial Facilities:** Post and Telegraph Department provides financial services using post office's saving schemes like Public Provident Fund, Kisan Vikas Patra, National Saving

Certificate, normal retail banking functions of monthly income schemes, recurring deposit account, savings account, time deposits and money order facility etc.

- **Mail Facilities:** It consists of parcel facilities which consists of transmission of articles from one place to another which can be registered and insured. It also provides facilities for greeting post, (a range of delightful greeting card on all occasions) and Media Post (a way for Indian corporate to advertise their brands through aerograms, telegrams and letterboxes).
- **International Money Transfers:** It enables money transfer from 185 countries in collaboration with Western Union Money Transfer.
- **Passport Facilities:** It has joint hands with Ministry of External Affairs and accepts application for passport.
- **Speed Post:** It has more than 1000 destination in India. It covers 97 major countries of the world.
- **E-Bill Post:** It is the latest addition in facilities by Indian Post whereby it collects bill payment across the counter for BSNL and Bharti Airtel.

**Question 4. Describe various types of insurance and exercise the nature of risks protected by each type of insurance.**

**Answer:** There are many types of insurance. Some of them are shown with the help of diagram given below:



Type of Insurance	Meaning	Type of Risk Covered
<b>Life Insurance</b>	Life Insurance is a contract, under which the insurer in consideration of a premium, agrees to pay a specified amount on the death of the assured, or on the expiry of a certain fixed period, whichever is earlier.	It provides protection to the family at the premature death or gives adequate amount at old age when earning capacity is reduced.

<b>Fire Insurance</b>	Fire Insurance is a contract whereby the insurer, in consideration of the premium paid, undertakes to compensate the insured for any loss that may result due to the occurrence of fire.	Protects the goods against the risk of fire.
<b>Marine Insurance</b>	Marine Insurance is a contract of insurance under which the insurer undertakes to indemnify the insured in the manner and to the extent thereby agreed against marine losses.	Protects the goods against the risk of loss in sea voyage.
<b>Health Insurance</b>	Health Insurance policy is a contract between an insurer and an individual or group, in which the insurer agrees to provide specified health insurance at an agreed upon price (the premium).	Protects against unseen health problems.
<b>Motor Vehicle Insurance</b>	It is a contract whereby the insurer agrees to indemnify the insured, in consideration of a fixed premium, for a loss caused by theft, fire, accident, earthquake etc.	It protects the value of motor vehicles against risk of theft, accident and fire etc. It also covers the owner's liability to compensate who are killed or insured through negligence of the motorist.
<b>Burglary Insurance</b>	It is a contract whereby the insurer agrees to indemnify the insured, in consideration of a fixed premium, of loss due to theft, burglary, house breaking and acts of similar nature.	It covers the risk of loss due to theft, burglary, house breaking and acts of similar nature.

<b>Cattle Insurance</b>	It is a contract whereby a sum of money is secured to the assured in the event of death of animals like bulls, buffaloes, cows and heifers.	It covers risk of death of cattle due to accident, disease or pregnancy.
<b>Crop Insurance</b>	It is a contract to provide financial support to farmers in case of crop failure due to drought or flood.	It covers all risks of loss or damages to the crop.
<b>Sports Insurance</b>	It assures a comprehensive cover available to amateur sportsmen covering their sporting equipment, personal effects, legal liability and personal accident risks.	It is available to following sports: angling, badminton, cricket, golf, lawn tennis, squash, use of sporting gun etc.

**Question 5. Explain in detail the warehousing services.**

**Answer: Primary warehousing services include the following:**

1. **Consolidation:** Warehouse receives and consolidates goods from different production stations and dispatches it to customer on a single transportation shipment.
2. **Break the Bulk:** Warehouse breaks the bulk received according to the requirements of the client.
3. **Stock Piling:** The next function of warehousing is the seasonal storage of goods to select business.

### **Secondary Functions of a Warehouse**

1. **Protection of goods:** A warehouse provides protection to goods from loss or damage due to heat, dust, wind and moisture, etc. It makes special arrangements for different products according to their nature. It cuts down losses due to spoilage and wastage during storage.
2. **Risk Bearing:** Warehouses take over the risks incidental to storage of goods. Once goods are handed over to the ware housekeeper for storage, the responsibility of, these goods passes on to the ware housekeeper. Thus, the risk of loss or damage to goods in storage is borne by the warehouse keeper. Since it is bound to return the goods in good condition, the warehouse becomes responsible for any loss, theft or damage etc., thus, it takes all precautions to prevent any mishap.
3. **Financing:** When goods are deposited in any warehouse, the depositor gets a receipt, which acts as a proof about the deposit of goods. The ware houses can also issue a document in favour of the owner of the goods, which is called warehouse-keeper's warrant. This warrant is a document of title and can be transferred by simple endorsement and delivery. So while the goods are in custody of the ware housekeeper, the businessmen can obtain loans from banks and other financial institutions keeping this warrant as security. In some cases, warehouses also give advances of money to the depositors for a short period keeping their goods as security.
4. **Processing:** Certain commodities are not consumed in the form they are produced. Processing is required to make them consumable. For example, paddy is polished, timber is seasoned, and fruits are ripened, etc. Sometimes warehouses also undertake these activities on behalf of the owners.



5. **Grading and branding:** On request warehouses also perform the functions of grading and branding of goods on behalf of the manufacturer, wholesaler or the importer of goods. It also provides facilities for mixing, blending and packaging of goods for the convenience of handling and sale.

## **MORE QUESTIONS SOLVED**

### **I. Multiple Choice Questions**

**Question 1. Which of the following is an example of E-banking?**

- (a) EFT (b) Online banking  
(c) ATM id) All of the above

**Question 2. Who can get an overdraft from a bank?**

- (a) A Current Account Holder (b) A Saving Account Holder  
(c) A Fixed Deposit Account Holder (d) A Recurring Deposit Account Holder

**Question 3. Give full form of ATM.**

- (a) Automatic Tele Money (b) Any Time Money  
(c) Automatic Teller Machine (d) Automatic Transfer Money

**Question 4. In which type of insurance, interest must exist only at the time of insurance?**

- (a) Life Insurance (b) Marine Insurance  
(c) Fire Insurance (d) All of the above

**Question 5. Which of the following companies offer DTH services in our country?**

- (a) Reliance (b) Idea  
(c) Tata sky (d) All of the above

**Question 6. Name the type of banking under which ATM, credit card and EFT facilities are available.**

- (a) Internet Banking (b) E-banking  
(c) Modern Banking (d) Online Banking

**Question 7. VSAT stands for:**

- (a) Very Small Aperture Terminal (b) Vidyut Supply and Transport  
(c) Very Small Application Terminal (d) Video Screening Aperture Terminal

**Question 8. Name the controlling authority of telecom services in India,**

- (a) TRAI (b) SEBI  
(c) RBI (d) IRDA

**Question 9. In which of the insurance policy loss cannot be measured?**

- (a) Life Insurance (6) Marine Insurance  
(c) Fire Insurance (d) All of the above

**Question 10. To which insurance, principle of indemnity is not applicable? (a) Life Insurance (b) Marine Insurance**

- (c) Fire Insurance (d) All of the above

**Question 11. Speed post in India connects major countries of the world.**

- (a) 120 (b) 140  
(c) 97 (c) 82

**Question 12. Sports insurance is not available for:**

- (a) Professional Sportsmen (b) Non-professional Sportsmen  
(c) Rural Area Sportsmen (d) Urban Area Sportsmen

**Question 13. FCI, STC, CWC are examples of:**

- (a) Bonded Warehouses (b) Government Warehouses  
(c) Private Warehouses (d) Cooperative Warehouses

**Question 14. It is the duty of the insured to make an effort for minimization of loss. It is**

the principle of:

(a) Utmost Good Faith (b) Contribution

(c) Mitigation (d) Insurable Interest

**Question 15.** Insurer must have some pecuniary interest in the subject matter of interest. It is the principle of:

(a) Mitigation (b) Contribution

(c) Utmost Good Faith (d) Insurable Interest

**Answers:**

1. (d) 2. (a) 3. (c) 4. (a) 5. (d)

6. (b) 7. (a) 8. (a) 9. (a) 10. (a)

11. (c) 12. (a) 13. (b) 14. (c) 15. (d)

## II. Short Answer Type Questions

**Question 1.** What is the difference between goods and services?

**Answer:**

Basis	Goods	Services
Meaning	Goods is a physical product which can be delivered to a buyer and involves the ownership from seller to customer.	Services are those separately identifiable, essentially intangible activities which provide satisfaction of wants, and are not necessarily linked to the sale of a product or another service.
Nature	A physical object.	An activity or process.
Intangibility	It is tangible like books.	It is intangible. For example; teaching by a teacher.
Inconsistency	Homogeneous.	Heterogeneous.
Inseparability	It can be separated from its owner.	It can't be separated from its owner.
Inventory	It has inventory.	It has no inventory.
Involvement	Participation of customers is not there in production. For example, manufacturing a car.	Participation of customers is there. For example, transportation is not possible unless the person who has to go is involved.

**Question 2.** Explain the functions of e-banking.

**Answer:** E-banking means banking transactions carried out with the help of computer systems (i.e., banking over the internet).

1. **Electronic Fund Transfer (EFT):** Under this system, a bank transfers wages and salaries directly from the company's account to the account of employees of the company.
2. **Automatic Teller Machine (ATM):** It refers to an electronic terminal that allows people with plastic card to perform simple banking transactions like withdrawal of cash 24 x 7 without any help of human teller.
3. **Debit Card:** It refers to a plastic card that allows the bank to take money from the customer's account and transfer it to a seller's account.

4. **Credit Card:** It refers to a plastic card that allows the customer to buy now and pay back the loaned amount to bank at a future date.
5. **Online Banking:** Under this system, when the customer gives instruction on his computer, the bank computer transfers money from customer's account to biller's account.

**Question 3. What do you mean by mode of transport? Name different modes of transport.**

**Answer:** Modes Of Transport: Modes of transport can also be called as means of transport or transport mode or transport modality. It is a general term used to specify the different kinds of transport facilities that are used by people to move from one place to the other and also to shift the goods from one place to other.

When more than one mode -of transport is used by a person for transportation then it can be described as a multi-model transport.

Generally there are four modes of transport that uses different types of vehicle, infrastructure and operation. Each mode of transport has its own advantages and disadvantages. The person will choose their mode of transport based on the cost, capability, routes and speed.

The general modes of transport are as follows:

1. Human powered transport;
2. Animal powered transport;
3. Roadways;
4. Waterways;
5. Railways;
6. Airways;
7. Other modes like pipe line, sewage, cable cars.

**Question 4. Write short notes on different types of marine insurance.**

**Answer:** Different types of marine insurance are as follows:

- **Cargo Insurance:** Cargo insurance caters specifically to the cargo of the ship and also pertains to the belongings of a ship's voyagers.
- **Hull Insurance:** Hull insurance mainly caters to the torso and hull of the vessel along with all the articles and pieces of furniture in the ship. This type of marine insurance is mainly taken out by the owner of the ship in order to avoid any loss to the ship in case of any mishaps occurring.
- **Liability Insurance:** Liability insurance is that type of marine insurance, where compensation is sought to be provided to any liability, occurring on account of a ship crashing or colliding and on account of any other induced attacks.
- **Freight Insurance:** Freight insurance offers and provides protection to merchant vessels' corporations which stand a chance of losing money in the form of freight in case the cargo is lost due to the ship meeting with an accident. This type of marine insurance solves the problem of companies losing money because of a few unprecedented events and accidents occurring.

**Question 5. What are different types of warehouses?**

**Answer:** Different types of warehouses are as follows:

1. **Public Warehouse:** It is operated in accordance with the law for the purpose of storing goods for other people at profit. Sometimes a large amount of goods arrives in part when it is not convenient for the importer to take it into his custody. During such periods these goods have to be stored somewhere. Similarly, even in trade they have to be stored between the time they are made and the time they are required for use. A public warehouse provides facilities for storing all such goods. It thus renders many useful services to the trade. It enables smaller sellers to carry regional stocks. This factor is very important in competitive markets.

2. **Private Warehouse:** This type of warehouse belongs to the owner of goods, usually a wholesaler, who stored his goods. This is in order to supply to retailers in future. Goods are produced in large quantities in anticipation of future demand and for the unknown customers. The ultimate wholesaler finds it necessary to purchase goods in advance in large bulk and to store them for future supply.
3. **Bonded Warehouses:** It is one which is licensed to accept imported goods for storage before payment of customs duties. By storing his goods in a bonded warehouse the importer gains some control without paying the duty. The goods in bonded warehouses are under the strict supervision of customs officers and before the owner can interfere with them, previous permission is necessary.
4. **Government Warehouse:** This type of warehouse is mainly located at the important sea ports and in most cases is owned by the Dock Authorities. The general public can also use this group of warehouse on payment of fixed charges. If a customer cannot pay the rent within the specified period or time, then the authority can recover the rent by disposing of the goods

### III. Long Answer Type Questions

#### Question 1. Explain different types of life insurance policies.

**Answer:** The life insurance policies are of many types. The principal types of policies are discussed below:

1. **Whole life Policy:** Under this policy premiums are paid throughout life and the sum insured becomes payable only at the death of the insured. The policy remains in force throughout the life of the assured and he continues to pay the premium till his death. This is the cheapest policy as the premium till his death. This is the cheapest policy as the premium charged is the lowest under this policy. This is also known as 'ordinary life policy'. This policy is suitable to persons who want to provide for payment of estate duty, make bequeathments for charitable purposes and to provide for their families after their death.
2. **Children's Endowment Policy:** This policy is taken by the person for his or her children to meet the expenses of education or marriage. The agreement states that a certain sum of money will be paid by the insurer when the children attain a particular age. There will be no need of paying premium if the person entering into the contract dies before maturity.
3. **Endowment Policy:** It runs only for a limited period or up to a particular age. Under this policy the sum assured becomes payable if the assured reaches a particular age or after the expiry of a fixed period called the endowment period or at the death of the assured whichever is earlier. The premium under this policy is to be paid up to the maturity of the policy, i.e., the time when the policy becomes payable. Premium is naturally a little higher in the case of this policy than the whole life policy. This is a very popular policy these days as it serves the dual purpose of family and old age pension.
4. **Double Endowment Policy:** Under this policy the insurer agrees to pay to the assured double the amount of the insured sum if he lives on beyond the date of maturity of the policy. This policy is suitable for persons with physical disability who are otherwise not acceptable for other classes of assurance at the normal tabular rates. Premiums are to be paid for a selected term of years or until death, if earlier.
5. **Joint Life Policy :** This policy covers the risk on two lives and is generally available to partners in business. Policies are however, issued on the lives of husband and wife under specified circumstances. Sum assured becomes payable at the end of the selected term or on the death of either of the two lives assured, if earlier.
6. **Fixed term (marriage) Endowment Policy and Education Annuity Policy:** It is a policy suitable for making provisions for the marriage or education of children. Premiums are payable for a selected term or till prior death. The benefits are payable for selected term or till



prior death. The benefits are payable only at the end of selected term. In case of the marriage endowment, the sum assured is paid in lump sum, but in case of the educational annuity, it is paid in equal half- yearly installments over a period of five years.

7. **Annuities :** It is a policy under which the insured amount is payable to the assured by monthly or annual installments after he attains a certain age. The assured may pay the premium regularly over a certain period or he may pay the premium regularly over a certain period or he may pay a lump sum of money at the outset. These policies are useful to persons who wish to provide a regular income for themselves and their dependants.



**Question 2. What is the difference between life, fire and marine insurance?**

**Answer:** It is summarized in the table given below:

<b>Basis</b>	<b>Life Insurance</b>	<b>Fire Insurance</b>	<b>Marine Insurance</b>
<b>Subject Matter</b>	Subject matter of insurance is human life.	Subject matter of insurance is physical property or assets.	Subject matter of insurance is ship, cargo or freight.
<b>Purpose</b>	Protection and investment both.	Protection only.	Protection only.
<b>Insurable Interest</b>	It must be present at the time of acquiring the policy and it is not necessary at the time of maturity.	It must be present at the time of contract and also when claim falls due.	It must be present at the time when claim falls due.
<b>Policy Amount</b>	It can be any amount.	It can't be more than the value of subject matter.	It can't be more than market value of goods.
<b>Duration</b>	It is taken for long duration like ranging from 5-30 years or whole life.	It is taken for one year.	It is taken for one year or period of voyage or mixed.
<b>Indemnity</b>	It is not based on principle of indemnity.	It is based on principle of indemnity.	It is based on principle of indemnity.
<b>Measurement of Loss</b>	Not possible	Possible	Possible
<b>Surrender Value</b>	It has a surrender value, i.e., it can be surrendered before maturity.	It does not have a surrender value.	It does not have a surrender value.
<b>Contingency of risk</b>	Element of risk is certain because amount has to be paid either on death or on maturity whichever is earlier.	Element of risk is uncertain as mishappening may not take place.	Element of risk is uncertain as mishappening may not take place.

**Question 3. Write a short note on GATS.**

**Answer:** The creation of the GATS was one of the landmark achievements of the Uruguay be came Round, whose results entered into force in January 1995. While services currently account for over 60 per cent of global production and employment, they represent no more than 20 per cent of total trade (BOP basis). This—seemingly modest—share should not be underestimated, however. Many services, which have long been considered genuine domestic activities, have increasingly become internationally mobile. This trend is likely to continue, owing to the introduction of new transmission

technologies (e.g., electronic banking, tele-health or tele-education services), the opening up in many countries of long entrenched monopolies (e.g. voice telephony and postal services), and regulatory reforms in hitherto tightly regulated sectors such as transport. Combined with changing consumer preferences, such technical and regulatory innovations have enhanced the “tradability” of services and, thus, created a need for multilateral disciplines.

All WTO members, some 140 economies at present, are at the same time members of the GATS and, to varying degrees, have assumed commitments in individual service sectors.

The GATS schedule largely follows a classification. It classifies services into 12 sectors which are as follows:

1. Business services;
2. Communication services;
3. Construction and related engineering services;
4. Distribution services;
5. Educational services;
6. Environmental services;
7. Financial services;
8. Health related and social services
9. Tourism and travel related services;
10. Recreational, cultural and sporting services;
11. Transport services;
12. And other services.

**Question 4. Write a short note on Indian insurance sector.**

**Answer:** The health of the insurance sector reflects a country's economy. This sector not only generates long term funds for infrastructure development, but also increases a country's risk taking capacity. India's economic growth since the turn of the century is viewed as a significant development in the global economy. This view is helped in no small part by a booming insurance industry.

The future of the Indian insurance sector looks bright. The sector which stood at a strong US\$ 72 billion in 2012 has the potential to grow to US\$ 280 billion by 2020. This growth is driven by India's favourable regulatory environment which guarantees stability and fair play. This environment has given rise to an insurance market which encourages foreign investors to tap into the sector's massive potential.

Ever since the Indian government liberalised the insurance sector in 2000 and opened the doors for private participation, the sector has become stronger. The resultant competition has provided the consumer with a never-before-seen range of products and providers, and also enhanced service levels markedly. Consistent growth in the insurance sector depends on a few factors. Some of these are:

1. **Effective distribution channels:** The efficiency and cost of the various distribution strategies used by companies are significant to their success in the insurance business. This particularly holds true for the retail business.
2. **Focus on overall financial inclusion:** As time evolves, so must the approach of the insurance sector in India. The objective of the insurance sector should ideally be to offer a broader range of activities to a wider populace.
3. **Consumer needs and preferences:** The growth of India's insurance industry can be attributed to product innovation, dynamic distribution channels, and vibrant publicity and promotional campaigns run by insurance companies. Benefits attached to the products and the manner in which they are delivered (through various marketing tie-ups) have helped bring customers and insurance companies closer to each other and made the latter more relevant.

4. **Health Insurance is an up-and-coming segment in this sector:** Currently, it caters for 10 per cent of the overall US\$ 30 billion healthcare expenditure in India. Consequently, there is plenty of scope for players in this area.
5. **The life insurance segment contributes** about 4 per cent to India's gross domestic product (GDP) in terms of total premiums underwritten annually. There are 23 private companies in the segment. The state owned Life Insurance Corporation (LIC) dominates the field, with about 71 per cent of the market share, according to Insurance Regulatory and Development Authority (IRDA).

#### IV. Higher Order Thinking Skills (HOTS)

**Question 1. Manju obtained a life insurance policy of her husband. After 5 years, she divorced her husband. After one year of divorce, her husband died in a car accident. Can she claim the amount of policy from the insurance company?**

**Answer:** Yes, she can claim because in life insurance insurable interest has to be present at the time of affecting the policy but need not be present at the time when the claim falls due.

**Question 2. A person gets his stock of goods insured, but he hides the fact that the electricity board has issued him statutory warning letter to get his factory's wiring changed later on, the factory catches fire due to short circuit. Can he claim compensation? State the name of "Principle".**

**Answer:** No, he cannot claim the compensation because the principle of utmost good faith is not followed. According to this principle, it is the duty of the insurer and insured to voluntarily make full accurate disclosure of all facts, material to the insurance contract.

**Question 3. Anju has taken a loan from Avi against the security of his factory. Can Avi take a fire insurance policy of that factory?**

**Answer:** No, she cannot. Because in case of fire insurance, insurable interest has to be present both at the time of affecting the policy and also when the claim falls due.

#### V. Value Based Questions

**Question 1. A person took an insurance policy and did not disclose that he is a patient of cancer. Which value is missing in this case?**

**Answer:** Honesty is missing in this case and the principle of utmost good faith is violated and hence the person's beneficiary cannot get the claim for his policy.

**Question 2. There are three types of services: Business Services, Social Services and Personal Services. Which of the services in your opinion are of utmost importance and why?**

**Answer:** In my opinion, these services are complementary to each other and hence, they have their own importance. I can't say that tourism or recreation (Personal Service) is less important than services of a charitable hospitals (Social Service) or vice-versa. Similarly I can't say that banking (Business Service) is less important than services of restaurants (Personal Service) or vice-versa. Still if I have to choose one, I will select social services because:

- They benefit to a larger section of society.
- They are sometimes provided without a payment in lieu.
- They have long lasting effects on our society and economy.



# NCERT SOLUTIONS For Class 11 Business Studies

## <http://freehomedelivery.net/Solutions> Chapter 5

### Emerging Modes of Business

#### Class 11 Business Studies Solutions Chapter 5 Emerging Modes of Business

NCERT SOLUTIONS For Class 11 Business Studies <http://freehomedelivery.net/Solutions> Chapter 5  
Emerging Modes of Business

#### I. Multiple Choice Questions

Tick mark (✓) the most appropriate answer to the following questions:

**Question 1. e-commerce does not include:**

- (a) A business's interactions with its suppliers
- (b) A business's interactions with its customers
- (c) Interactions among the various departments within the business
- (d) Interactions among the geographically dispersed units of the business

**Question 2. Outsourcing:**

- (a) Restricts only to the contracting out of Information Technology Enabled Services . (TIES)
- (b) Restricts only to the contracting out of non-core business
- (c) Includes Contracting out of manufacturing and RandD as well as services processes -both core and non-core, but restricts only to domestic territory
- (d) Includes off-shoring

**Question 3. The payment mechanism typical to e-business**

- (a) Cash on delivery!CoD) (b) Cheques
- (c) Credit and Debit Cards (d) E-cash

**Question 4. A Call Centre handles:**

- (a) Only in-bound voice based business (b) Only out-bound voice based business
- (c) Both voice based and non-voice based business (d) Both customer facing and back-end business

**Question 5. It is not an application of e-business:**

- (a) Online bidding (b) Online procurement
- (c) Online trading (d) Contract RandD

**Answer:**

1. (c) 2. (b) 3. (d) 4. (d) 5. (d)

#### II. Short Answer Type Questions

**Question 1. State any three differences between E-business and traditional business.**

**Answer:** The differences between e-business and traditional business can be summarized as below:

1. **Logistics:** The logistics of e-business typically have lesser constraints than traditional business. E-businesses are not limited to venue; they can be located anywhere and still serve the same customer. Their product capacity is "infinite" in that they are not limited to the space of a brick-and-mortar store. E-businesses mainly depend on shipping methods to deliver and receive items, while traditional stores conduct an instant exchange. This timing difference can

be a significant factor for some consumers. For example, refunds would typically take much longer to process for e-businesses than in a neighborhood store.

2. **Human Resources:** The two types of business differ in talent recruitment. E-businesses significantly emphasize technology and hire more people from the web design and development fields. In some cases, every employee may be required to have a technical background or receive in-house training for basic web development. On the other hand, traditional businesses are more diverse in hiring for non-technical positions, such as sales representatives and display managers.
3. **Marketing and Finance:** In marketing for traditional business, marketers can focus on all five human senses to influence the sale. For example, maintaining a proper display keeps the product aesthetically appealing. Consumers can also physically touch the product in a traditional store; this is particularly vital for physically sensitive items such as clothes. E-businesses typically have to rely mainly on sight. The physical display is replaced with digital images. The inability to touch and test the product first hand is replaced with technical text to visualize the details of the product; online retailers may also have the ability to present many more choices because they do not need to have the physical product on hand. The major financial difference between e-business and traditional business is cost. E-businesses usually have lesser start up and operational costs, buying an online domain is much cheaper than renting land and building facilities and buying equipment.
4. **Management:** E-business management is typically flatter than traditional management. A flat company happens when there are few levels in between top management and the entry-level employee. In most E-businesses, low level management, such as store managers and division managers, is unnecessary. Instead, E-businesses expand horizontally by hiring external consultants and contract web development positions. These entities specialize in a business service, such as e-commerce setup and online marketing. They may work for the company but are not necessarily included in or affected by management decisions.

### **Question 2. How does outsourcing represent a new mode of business?**

**Answer:** Outsourcing represents a new mode of business. It is fast becoming an emerging mode of business. Firms have started increasingly outsourcing one or more of their processes which can be efficiently and effectively carried on by others. Outsourcing can be qualified as emerging mode of business because its acceptance is increasing as a fundamental business policy and philosophy, as opposed to the earlier philosophy of doing it all by yourself.

### **Question 3. Describe briefly any two applications of E-business.**

**Answer:** Two applications of E-business are discussed below:

1. **e-Procurement:** It involves internet based sales transactions between business firms including both, “reverse auctions” that facilitate online trade between a single business purchaser and many sellers, and, digital market places that facilitate online trading between multiple buyers.
2. **e-Delivery:** It includes electronic delivery of computer software, photographs, videos, books (e-journals) and other multimedia content to the other’s computer. It also includes rendering of legal, accounting, medical and other consulting services electronically. In fact, internet provides the firms with the opportunities for outsourcing of a host of Information Technology Enabled Services (ITES).

### **Question 4. What are the ethical concerns involved in outsourcing?**

**Answer:** Following are the major ethical concerns involved in outsourcing:

1. **Confidentiality:** When a company outsources any of its functions, it has to share a lot of information and knowledge with outsourcing partner. He may not preserve the confidentiality. If company adopts outsourcing of complete processes or products, there is further risk that outsourcing partner may start his own business which may increase competition.
2. **Sweat Shopping:** The firms which opt for outsourcing aim at lowering their costs, try to get maximum benefit from the low cost manpower of the host countries. Secondly, such works are outsourced which do not build much of competency and ability of outsourcing partners. So, they build blue collar workers by handing over doing skills rather than creating white collar workers by transferring thinking skills.
3. **Using Child Labour and not following Labour Laws:** Outsourcing is engaging child labour and women in the factories. Moreover, there exists wage discrimination on the basis of sex of the worker. Workers are exploited by giving less than minimum wages.
4. **Resentment in the Countries:** When MNCs contract out manufacturing, marketing, accounting, R and D etc. to developing countries, it may create resentment in home country. The people from developed countries may not like that the jobs which they could get have been transferred to developing nations for cost cutting.

**Question 5. Describe briefly the data storage and transmission risks in E-business.**

**Answer:** In the present century, information is acting as power. If the relevant information of the business reaches into wrong hands, it may create a lot of loss for the company concerned. There is a risk of en route being stolen or modified by wrong people for their selfish motives. It is exposed to the risk of VIRUS and hacking. VIRUS stands for Vital Information Under Seize. Installing and timely updating anti virus programmes and scanning the files and disks with them provides protection to the files, folders and systems from the attack of virus.

Another risk involved is interception of data in the course of transmission. To protect data against this, cryptography is used. Cryptography refers to the art of protecting information by transforming it into an unreadable format called 'cyphertext'. Thereafter only those who have a secret key can decrypt the message into 'plaintext'. It is like coding and decoding.

### III. Long Answer Type Questions

**Question 1. Why are E-business and outsourcing referred to as the emerging modes of business? Discuss the factors responsible for the growing importance of these trends.**

**Answer:** E-business and outsourcing are referred to as emerging modes of business. Prefix 'emerging' puts emphasis on the fact that these businesses are in the process of development. These changes are happening here and now, and, that these changes are likely to continue. In fact, three changes are taking place most strongly:

- **Digitization:** The conversion of text, sound, images, video and other content into a series of ones and zeroes that can be transmitted electronically.
- **Outsourcing:** Contracting out non core activities to outside firms.
- **Internationalisation and globalisation:** More and more foreign companies are entering into India and sending Asian and Indian companies becoming MNCs. Therefore, E-business and outsourcing referred to as the emerging modes of business.

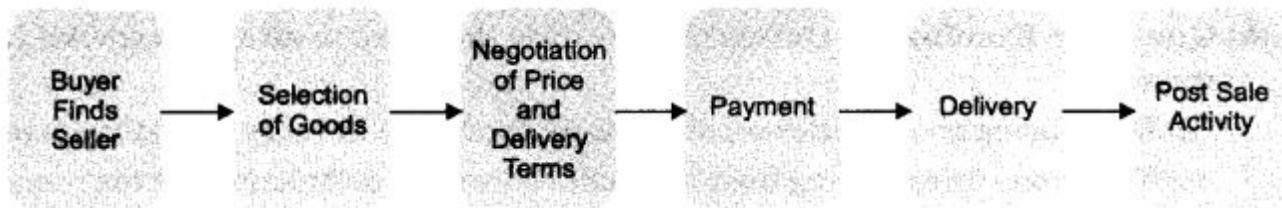
**Following factors are responsible for the growing importance of these trends:**

- **Improvement in Information Technology:** With the improvement in information technology and emergence of internet the process of outsourcing and e-business is on an expansionary path.

- **More and More Interactive Websites:** Websites are becoming more and more interactive. It is removing the problem of 'low touch'.
- **Improvement in Communication Technology:** Communication technology is continually evolving and increasing the speed and quality of communication through internet.
- **Diffusion of E-Commerce in all nooks and corners of the country:** In order to diffuse e-commerce in all nooks and corners, India has undertaken about 150 such projects. It is also growing importance of these trends.
- **Global Competitive Pressures for higher quality products:** Due to adoption of new economic policy of 1991 in India, there has been an increase in competitive pressure from giant sized MNCs and global enterprises.
- **Ever Demanding Consumers:** There is increasing demands from consumers for high quality products at minimum cost. Therefore, e-business and outsourcing are being chosen as newer options. But e-business and outsourcing are not emerging out of compulsion but also out of choice because of its benefits to consumers as well as producers.

**Question 2. Elaborate the steps involved in online trading.**

**Answer:** Operationally, following steps are involved in online trading:



1. **Registration:** First step in online trading is registration with the online trader by filling up a registration form. With registration buyer has opened an account with online trader. A password is created for the account which protects account and shopping cart which can be misused otherwise.
2. **Placing an Order:** An account holder can drop the items in the shopping cart. Shopping cart is an online record of what a person has picked up while browsing the online store. Once being sure of what a person wants to buy, one can check out and choose his payment options.
3. **Payment Mechanism:** In online trading payment may be made in any of the following ways:
  - **Cash On Delivery:** Under this, the payment for goods ordered online may be made in cash at the time of physical delivery of the goods.
  - **Cheque:** Another option is that the online vendor may arrange for the pickup of the cheque from the customer's end. Upon realization, goods may be delivered.
  - **Net Banking Transfer:** These days banks provide facility to the customers for electronic transfer of funds using internet. Therefore, a buyer can also make use of net banking money transfer to pay for the goods ordered.
  - **Credit or Debit Cards:** These are also called plastic money. These cards are most popularly used in payment for online transactions. To accept credit card as an online payment type, the seller first needs a secure means of collecting credit card information from its customer. Payments through credit cards can be processed either manually, or through online authorization system like SSL Certificate.
  - **Digital Cash:** It is a kind of electronic currency which exists only in cyberspace. It has no real physical properties, but offers the ability to use real currency in an electronic format. For this, the buyer has to deposit cash in bank account which issues equivalent digital cash to the person which can be used for online trading. It is more secure than credit or debit cards.



### Question 3. Evaluate the need for outsourcing and discuss its limitations.

**Answer:** Outsourcing has emerged as a way of doing business due to global competitive pressures for higher quality products at lower costs, ever demanding customers and emerging technologies. Need for outsourcing can be understood from the benefits which are given below:

- **Focusing of Attention:** Business firms are realizing the importance of focusing on core areas where they have distinct ability and core competence and contracting out the rest of the activities to their outsourcing partners. A business organization needs to decide its core areas and non-core areas. Once they outsource non-core areas, they can focus their attention on selected activities. It will increase efficiency and effectiveness.
- **Quest for Excellence:** Outsourcing enables the firms to attain excellence in two ways:  
(a) By focusing on activities selected, their excellence in those activities increases.  
(b) They excel by extending their capabilities through contracting out the remaining activities to them who excel in them.
- **Cost Reduction:** In the age of globalization, cost reduction is of vital importance to survive in the market. Division of labour not only enhances quality but also reduces cost. For example, India is preferred as an outsourcing destination because of cost factors.
- **Growth through alliance:** When some activities are outsourced then these alliance partners invest for the outsourced activities. Business can be expanded by same amount of investible funds as now these funds are to be invested in limited number of activities.
- **Fillip to Economic Development:** Outsourcing stimulates entrepreneurship, employment and exports in the host countries. For example, in India there has been remarkable growth in entrepreneurship, employment and exports that today India is an undisputed leader in software development and IT enable services.

But outsourcing is not an unmixed blessing. It has its own limitations. Some of which are discussed below:

- **Confidentiality:** When a business opts for outsourcing, it has to share a lot of vital information and knowledge. This information may be leaked by the outsourcing partner. It may be against the outsourcing firm. It is also possible that the outsourcing partner starts a business of same line after getting such information.
- **Ethical Concerns:** Many a time, outsourcing makes use of child labour and violates labour laws to reduce costs. They also discriminate in wages on the basis of sex.
- **Sweat Shopping:** A firm which goes in for outsourcing actually transfers 'doing' skills rather than 'thinking' skills. Therefore, they do not create skilled manpower in developing countries but just take maximum benefit of low cost labour by transferring non intellectual tasks.
- **Resentment in their Home Countries:** Outsourcing is being disliked by people in developed countries because the jobs which they could get are being transferred to developing countries through outsourcing. The problem is still more severe if there is problem of unemployment in home country of outsourcing firm.

### Question 4. Discuss the salient aspects of B2C commerce.

**Answer:** In this, both the parties involved are business firms and therefore, it has been named as B2B i.e., business to business. Historically, the term e-commerce originally meant for facilitation of B2B transactions using Electronic Data Interchange (EDI) technology to send and receive commercial documents like purchase orders and invoices. Salient aspects of B2B Commerce:

1. **Need:** Creation of utility requires a business to contact with a number of other businesses which

- May be suppliers
- May act as channel of distribution.
- Different middlemen in different locations;
- Changing production as per specifications of the customer.

2. **Benefits:**

- It strengthens and improves the distribution system of a firm. For example, each consignment of goods from a warehouse and the stock in hand can be monitored and replenishments and reinforcements can be set in motion as and when needed.
- A customer's specifications can be routed through the dealers to the factory so that there may be customized production.
- B2B E-commerce expedites the movement of information and documents.
- It also expedites money transfers.

3. **Example:** The manufacture of an automobile requires assembly of a large number of components which in turn are being manufactured elsewhere. To reduce dependence on a single vendor, the automobile factory cultivates more than one vendor for each of the components. A network of computers is used for placement of orders, controlling production and delivery of components and making payments.

**Question 5. Discuss the limitations of electronic mode of doing business. Are these limitations severe enough to restrict its scope? Give reasons for your answer.**

**Answer:** The limitations of electronic mode of doing business are given below:

- **Low personal Touch:** It lacks the warmth of interpersonal interactions. Therefore, such products which need personal touch like beauty products, garments, fashion accessories etc. can't be traded through e-business.
- **Mismatch between order giving/taking speed and order fulfillment speed:** Sometimes websites take a long time to open which may frustrate the user. Even after giving or taking order, it takes enough time to give physical delivery of goods. It also plays on the patience of the customer.
- **Knowledge of technology is must:** For e-commerce both the parties need fairly high degree of familiarity with the world of computers. It divides the society into two parts i.e; one who are familiar with digital technology and other who are not.
- **Increased risk due to parties being unknown to each other:** When two parties are involved in e-business, they are unaware of personal identities of each other. They do not even know the locations of the parties involved. It makes e-business risky. There may also be problems of virus and hacking.
- **People Resistance:** People are resistant to change their ways and adopt new technology. Change is perceived as a source of stress and insecurity by many.
- **Ethical Concerns:** These days companies use an electronic eye to keep track of the websites being used by employees, computer files that they use, their e-mal accounts etc. It is not ethical.

But in spite of these limitations, e-business is the way. No, these limitations are not severe enough to restrict its scope.

- **Improvement in Information Technology:** With the improvement in information technology and emergence of internet the process of outsourcing and e-business is on an expansionary path. Anti virus and improved security measures are increasing to make e-business more secure and safer option.

- **More and more Interactive Websites:** Websites are becoming more and more interactive. It is removing the problem of 'low personal touch'.
- **Improvement in Communication Technology:** Communication technology is continually evolving and increasing the speed and quality of communication through internet so that customer does not get frustrated in processing the order.
- **Diffusion of E-Commerce in all nooks and corners of the country:** An order to diffuse e-commerce in all nooks and corners, India has undertaken about 150 such projects. It is increasing the number of people acquainted with digital technology. We can conclude that e-business will continue to stay and reshape the businesses, governance and economies.

## MORE QUESTIONS SOLVED

### I. Multiple Choice Questions

**Question 1. E-business and E-commerce are:**

- (a) Synonyms (b) Antonyms  
(c) Former is wider than latter (d) Former is narrow than latter.

**Question 2. When was Electronic Data Interchange (EDI) standardised?**

- (a) 1984 (b) 1995  
(c) 2000 (d) 1999

**Question 3. In B2B, B2C, C2C etc B and C stand for:**

- (a) Business and Corporate (b) Bidding and Customer  
(c) Business and Customer (d) Business and Consumer

**Question 4. When parties involved in the electronic transactions are from within a given business firm, it is called:**

- (a) B2B Commerce (b) Intra B Commerce  
(c) C2C Commerce (d) B2C Commerce

**Question 5. When a firm transacts with its employees, it is referred to as:**

- (a) B2B Commerce (b) B2E Commerce  
(c) C2C Commerce (d) B2C Commerce

**Question 6. Work from home using internet is covered under:**

- (a) Online Networking (b) Virtual Private Network  
(c) Electronic Data Exchange (d) Paypal

**Question 7. Which of the following is a benefit of e-business?**

- (a) Less Risky (b) Less Technological Requirements  
(c) Convenience (d) All of the above

**Question 8 Which of the following is not an application of e-business?**

- (a) E-procurement (b) e-bidding  
(c) e-delivery (d) All of the above

**Question 9. Which of the following can be used only for e-business?**

- (a) Cheques (b) Credit Card  
(c) Debit Card (d) E-cash

**Question 10. About 95% of online consumer transactions are executed through:**

- (a) Cheques (b) Credit Card  
(c) Debit Card (d) E-cash

**Question 11. When a customer claims that he has made payment but the seller does not get it, it is called:**

- (a) Default on Delivery (b) Default on Order Taking  
(c) Bad Debts (d) Default on Payment

**Question 12. Which of the following is used to handle data storage risk?**

- (a) VIRUS (b) Hacking

(c) Cryptography (d) All of the Above

**Question 13.** ——— is the largest captive BPO unit in India for providing certain kinds of services to the parent company in the United States as well as to its subsidiaries in other countries.

(a) Infosys (b) General electric (GE)

(c) Accenture (d) None of these

**Question 14.** BPO ———cost and———— excellence.

(a) Reduces, Reduces (b) Increases, Increases

(c) Reduces, Increases (d) Increases, Reduces

**Question 15.** In India ———— and ——— are referred to as emerging modes of business.

(a) E-Business and E-Commerce (b) Outsourcing and E-business

(c) Outsourcing and E-Commerce (d) Online Trading and Networking.

**Answers:**

1. (c) 2. (a) 3. (d) 4. (b) 5. (b)

6. (b) 7. (c) 8. (d) 9. (d) 10. (b)

11. (d) 12. (c) 13. (b) 14. (c) 15. (c)

## II. Short Answer Type Questions

**Question 1.** Differentiate between traditional business and e-business.

**Answer:** Differences between traditional business and e-business is summarized below:

Basis	Traditional Business	e-business
1. Formation	Difficult	Simple
2. Physical presence	Required	Not required
3. Location requirement	Market	None
4. Cost of setting up	High	Low/no requirement of physical facility
5. Shape of Organizational Structure	Vertical due to hierarchy or chain of command	Horizontal due to directness of command and communication

6 Opportunity for inter personal touch	More	Less
7. Ease of expansion	More	Less
8. Nature of contact with the suppliers and customers	Indirect through intermediaries	Direct

**Question 2.** Write a short note on the scope of e-business.

**Answer:** Scope of e-business is very wide. It is summarized below:

1. **B2B Commerce:** Business to Business—Both the parties are business firms, e.g. Manufacturer of an automobile requires assembly of a large number of components which are being manufactured by different firms; Maruti Udyog, Bajaj Auto etc. use B2B commerce.

2. **B2C Commerce:** Business to Customer—Transaction taking place between business and individual customers. It facilitates promotion of products on line. e.g. music or film. Companies sell products and services on line to customer e.g. Amul.com sell Amul products online.
3. **Intra – B. Commerce:** Parties involved are from within a given business firm. It makes it possible for the marketing department to interact constantly with the production department to get information about customer requirement.
4. **C2C Commerce:** Consumer to consumer—Business originates from the consumer and the ultimate destination is also consumer. Its area of application is the formation of consumer forum, e.g. selling used books over the internet.

**Question 3. Write a short note on the history of e-commerce.**

**Answer:** The origin of e-commerce dates back to electronic media like telephone, fax, compact disc, cable and personal computer etc. These electronic media had several limitations like speed, accuracy, secrecy, geographical distance, authenticity etc. Business transactions were carried out using electronic devices. Let us look at the history chronologically.

1. In 1984, EDI or Electronic data interchange was standardized through ASC X12. It guaranteed that companies will be able to complete transactions with each other reliably.
2. In 1992, 'Compuserve' offered online retail products to its customers.
3. In 1994, Netscape arrived which provided a simple browser to surf the internet and launched a safe online transaction technology called Secure Socket Layer (SSL).
4. In 1995 two of the biggest names in e-commerce were launched namely, amazon.com and ebay.com.
5. In 1998, Digital Subscriber Line was launched.
6. In 1999, retail spending over the internet reached \$820 billion dollar as per business.com.
7. In 2000, the USA government extended moratorium on internet taxes till 2005.

**Question 4. Differentiate between e-commerce and e-business.**

**Answer:** E-business and e-commerce are terms that are sometimes used interchangeably and sometimes they're used to differentiate one vendor's product from another. But the terms are different, and that difference matters to today's companies.

**Definition of E-Commerce**

E-commerce is "any transaction completed over a computer-mediated network that involves the transfer of ownership or rights to use goods and services," defines the U.S. Census Bureau.

Transactions aren't required to have a price and include both sales and items like free downloads. E-commerce includes transactions made on the internet, Intranet, Extranet, World Wide Web, by e-mail and even by fax.

**Definition of E-Business**

E-business is broader than e-commerce; including the transaction based e-commerce businesses and those who run traditionally but cater to online activities as well. An e-business can run any portion of its internal processes online, including inventory management, risk management, finance, human resources. For a business to be e-commerce and e-business, it must both sell products online and handle other company activities or additional sales offline.

- E-commerce covers outward-facing processes that touch customers, suppliers and external partners, including sales, marketing, order taking, delivery, customer service, purchasing of raw materials and supplies for production and procurement of indirect operating expense items, such as office supplies. E-business includes e-commerce but also covers internal



processes such as production, inventory management, product development, risk management, finance, knowledge management and human resources.

- E-business strategy is more complex, more focused on internal processes, and aimed at cost savings and improvements in efficiency, productivity and cost savings than e-commerce.
- Scope of e-business is wider than e-commerce.

### **Question 5. What is digital divide? How is it relevant in context of e-business?**

**Answer:** It is division of society on the basis of familiarity with digital technology and non-familiarity with digital technology. The digital divide causes a significant problem in many struggling parts of the world. "As of 2003, only seven per cent of the world's 6.4 billion people have had access to the World Wide Web" [Ryder M, 2005]. The parts of the world that have a predominant amount of internet access is the Western World, the United States, Europe and Northern Asia, whereas access is more restricted in the poorer less developed parts of the world such as Africa, India and southern parts of Asia. These poorer nations are unable to afford the initial start up cost to be able to invest into technology to allow their nation to be able to have and maintain internet access. This puts these countries at a competitive and economic disadvantage. This is due to the fact that it impacts on society at many levels. By a country not having internet access, it means that schools are unable to teach IT skills and take advantage of the vast amount of information available on the web. With the lack of IT skills people from these countries are unable to compete at an international level.

### **Question 6. Explain various payment mechanisms under e-business.**

**Answer:** Various payment mechanisms under e-business are described below:

- **Cash on Delivery:** Under this, the payment for goods ordered online may be made in cash at the time of physical delivery of the goods.
- **Cheque:** Another option is that the online vendor may arrange for the pickup of the cheque from the customer's end. Upon realization, goods may be delivered.
- **Net Banking Transfer:** These days banks provide facility to the customers for electronic transfer of funds using internet. Therefore, a buyer can also make use of net banking money transfer to pay for the goods ordered.
- **Credit or Debit Cards:** These are also called plastic money. These cards are most popularly used in payment for online transactions. To accept credit card as an online payment type, the seller first needs a secure means of collecting credit card information from its customer. Payments through credit cards can be processed either manually, or through an online authorization system like SSL Certificate.
- **Digital Cash:** It is a kind of electronic currency which exists only in cyberspace. It has no real physical properties, but offers the ability to use real currency in an electronic format. For this the buyer has to deposit cash in bank account which issues equivalent digital cash to the person which can be used for online trading. It is more secure than credit or debit cards.

### **Question 7. Explain the measures taken to protect the security and safety of e-transactions.**

**Answer:** Following measures are taken to protect security and safety of e-transactions:

1. **Cryptography:** According to Pete Loshin, "It means use of such measures so as to keep the information out of the hand of anyone but its intended recipient. "Even if the message is intercepted the meaning shall not be apparent unless the interceptor is able to decode. This technique makes use of codes and cyphers.
2. **Password:** The parties to an e-commerce transaction must use the password. Password is a code fed in computer by the user. It can be in alphabets or numeric or alpha-

numeric characters. Unless a person feeds in the password, system shall neither respond nor give effect to the transactions. Therefore, one must keep a password. .

3. **Cookies:** Cookies are very similar to creating ID in telephones that provide telecallers with such relevant information as the customer's name, address and previous purchase payment record.
4. **Creating Keys:** Key is a secret algorithm. Only the person who has the key can read the data.

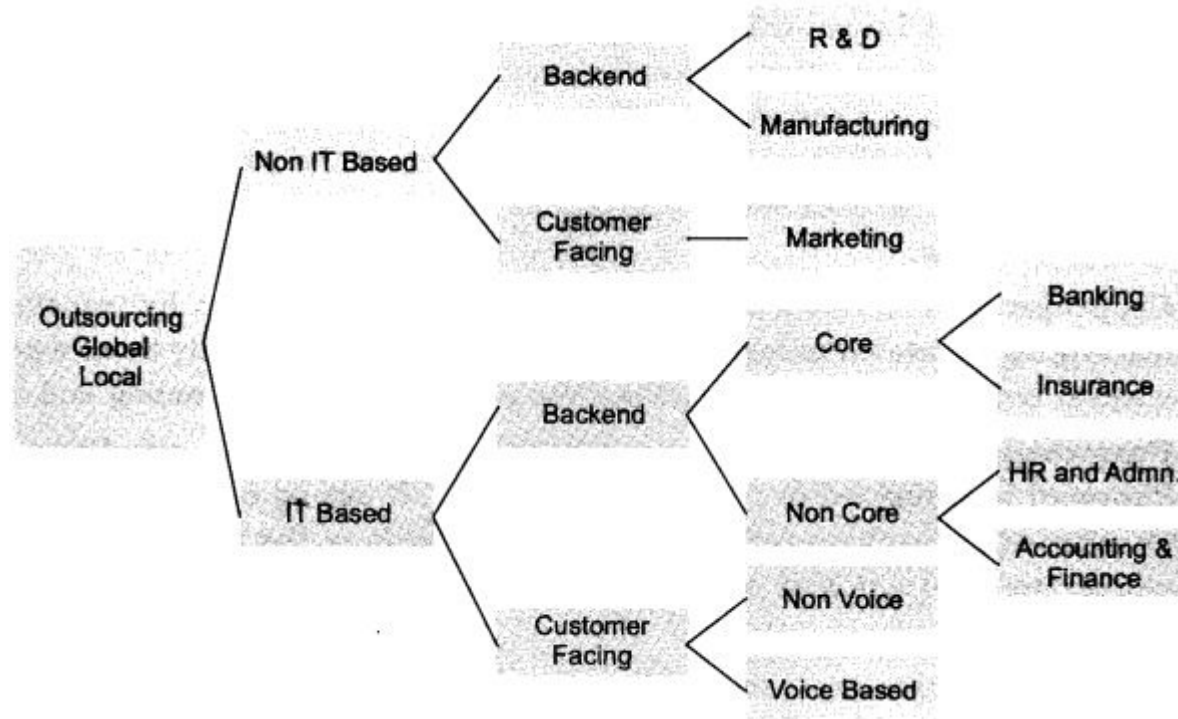
### Question 8. What resources are required for successful implementation of e-business?

**Answer:** Three m's are required for setting up any business: men, money and machines: For e-business some additional sources are required. It needs a website with allotted cyberspace. More is the cyberspace, more is the cost of website and vice-versa. Space requirement depends on scale of operations and how interactive a website is.

### III. Long Answer Type Questions

#### Question 1. Show the anatomy of outsourcing.

**Answer:** Anatomy of outsourcing has been shown with the help of chart given below:



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#### Question 2. What are the threats to e-transactions? Which measures have been devised for their protection?

**Answer:** There are many threats to e-transactions. Risk here is referring to probability of any mishappening that can result into financial, reputational or psychological losses to the parties involved in the transaction. It includes:

##### 1. Transaction risks: It can be of three types:

- Default on Order Taking or Giving: Seller denies that the customer ever placed the order or customer denies that he ever placed the order.
- Default on Delivery: It happens when either goods are delivered at a wrong address or wrong goods are delivered.
- Default on Payment: Seller does not get the payment for the goods delivered but customer claims that he has made the payment.

2. **Data Storage and Transmission Risks:** Data stored in the systems and en route is exposed to a number of risks. Major two risks are related to virus and hacking. Virus is a program which replicates itself on the other computer systems. The effect of computer viruses can range from mere annoyance in terms of some on-screen display (level -1 virus), disruption of functioning (level-2 virus) damage to target data files (level-3 virus) to complete destruction of the system.(level-4 virus). Hacking refers to unauthorized logging into the account and misusing it for selfish purposes or for fun only. Antivirus can help to protect files from virus and cryptography is used for protection against hacking.
3. **Risks of threat to Intellectual Property and Privacy:** Once an information is uploaded on internet, it loses privacy and IPRs. It becomes difficult to protect it from being copied and being accessible to one and all.

**The following measures have been devised for their protection:**

1. **Secure Socket Layer (SSL):** It was designed by Netscape for use in electronic commerce for transactions involving confidential information like credit card numbers. SSL uses a system of public and private key authentication combined with schemes to verify electronic signatures. Public key is the password that the sender uses to encrypt the data and the private key is used by the receiver of a message to decrypt the data.
2. **Cryptography:** It refers to the art of protecting information by transforming it (encrypting it) into an unreadable format called 'cyphertext'. Only those who possess a secret key can decrypt the message into plain text. It is like coding and decoding.
3. **Password:** The parties to an e-commerce transaction must use the password. Password is a code fed in computer by the user. It can be in alphabets or numeric or alpha-numeric characters. Unless a person feeds in the password, system shall neither respond nor give effect to the transactions. Therefore, one must keep a password.
4. **Cookies:** Cookies are very similar to creating ID in telephones that provide telecallers with such relevant information as the customer's name, address and previous purchase payment record.
5. **Anti-virus:** There are anti-viruses which remove any type of virus from the system.

#### **IV. Higher Order Thinking Skills (HOTS)**

##### **Question 1. "E-commerce is the need of the hour." Comment.**

**Answer:** In this century, lifestyle has undergone a drastic change. People have everything except time. Using e-commerce they can buy and sell almost everything at your doorstep with the magic of e-commerce in the 21st century which will be known for information revolution. E-commerce has changed your lifestyles entirely because you don't have to spend time and money in travelling to the market. You can do your e-payments with the help of e-commerce.

There is no time barrier in selling the products. One can log on to the internet even at midnight and can sell the products at a single click of mouse. E-commerce reduces delivery time and labor cost.

Thus it has been possible to save the time of both-the vendor and the consumer.

**Its need is clear from its benefits given below:**

1. **Exploitation of New Business:** Broadly speaking, electronic commerce emphasizes the generation and exploitation of new business opportunities and to use popular phrases: "generate business value" or "do more with less"
2. **Enabling the Customers:** Electronic Commerce is enabling the customer to have an increasing say in what products are made, how products are made and how services are delivered (movement from a slow order fulfillment process with little understanding of what is

taking place inside the firm, to a faster and explore open process with customers having greater control.

3. **Improvement of Business Transaction:** Electronic Commerce endeavors to improve the execution of business transaction over various networks.
4. **Effective Performance:** It leads to more effective performance i.e., better quality, greater customer satisfaction and better corporate decision making.
5. **Greater Economic Efficiency:** We may achieve greater economic efficiency (lower cost) and more rapid exchange (high speed, accelerated, or real-time interaction) with the help of electronic commerce.
6. **Execution of Information:** It enables the execution of information laden transactions between two or more parties using interconnected networks. These networks can be a combination of 'plain old telephone system' (POTS), Cable TV, leased lines and wireless. Information based transactions are creating new ways of doing business and even new types of business.
7. **Facilitating of Network Form:** Electronic Commerce is also impacting business to business interactions. It facilitates the network form of organization where small flexible firms rely on other partner, companies for component supplies and product distribution to meet changing customer demand more effectively. Hence, an end to end relationship management solution is a desirable goal that is needed to manage the chain of networks linking customers, workers, suppliers, distributors and even competitors. The management of "online transactions" in the supply chain assumes a central roll.

**Question 2. "E-commerce is giving way to paperless society and government is supporting it." Substantiate.**

**Answer:** It is right to say that E-commerce is giving way to paperless society. Government is also formulating laws to help in this creation. It is clear from the laws formulated under IT Act, 2000:

1. **Legal recognition of electronic records:** Where any law provides that information or any other matter shall be in writing or in the typewritten or printed form, then, notwithstanding anything contained in such law, such requirement shall be deemed to have been satisfied if such information or matter is rendered or made available in an electronic form; and accessible so as to be usable for a subsequent reference. For example, a company can send notice for AGM using e-mail.
2. **Retention of electronic records:** Where any law provides that documents, records or information shall be retained for any specific period, then, that requirement shall be deemed to have been satisfied if such documents, records or information are retained in the electronic form. For example, if results are preserved in electronic form it will work.
3. **Legal recognition of digital signatures:** Where any law provides that information or any other matter shall be authenticated by affixing the signature or any document shall be signed or bear the signature of any person, hence notwithstanding anything contained in such law, such requirement shall be deemed to have been satisfied, if such information or matter is authenticated by means of digital signature affixed in such a manner as may be prescribed by the Central Government.
4. **Use of electronic records and digital signatures in Government and its agencies:** Where any law provides for the filling of any form, application or any other document with any office, authority, body or agency owned or controlled by the appropriate government in a particular manner; the issue or grant of any license, permit, sanction or approval by whatever name called in a particular manner; the receipt or payment of money in a particular manner, then, notwithstanding anything contained in any other law for the time being in force, such requirement shall be deemed to have been satisfied if such filing, issue,



grant, receipt or payment, as the case may be, is effected by means of such electronic form as may be prescribed by the appropriate government. All these provisions of IT Act, 2000 are helping us to move towards a paperless society.

### **Question 3. Discuss utility of E Commerce in:**

**(a) Health,**

**(b) Education,**

**(c) Governance,**

**Answer: (a) Changes in Health:** E-health is following the same path, with electronic patient records slowly being introduced and health insurance schemes starting to refund e-health services. This will be a user driven development as it is more likely that the users will be able to adapt to e-health much faster than the healthcare system can deliver it.

This will clear the way for a whole new e-health industry, worth billions of dollars. One has to look at some of the e-health systems linked to the high end private hospitals in the USA to see what is in store. They use their e-health facilities as a major marketing tool to attract customers, not just to the actual hospital, but to all the other facilities around it. The add on revenues are significant.

**(b) Progress in e-education:** It is moving at an enormous pace and already some schools are limiting the number of printed textbooks – some are going totally e-book. With over a million children now with laptops it is only a matter of time before the education system to switch over. The savings in books and other printed material alone will pay for this digital revolution. South Korean schools will be entirely e-book-based by 2015.

**(c) Governance:** Many e-government services on offer around the world already provide citizens with relatively sophisticated services and the establishment of a fiber based broadband network may see governments improve and broaden the range of web services even further. In addition, mobile services are being incorporated in service offerings and computing is becoming integrated. The Internet of Things (IoT) and M2M wifi also impact upon this sector. Those who are still talking about broadband as an end in itself; do not understand the situation. Broadband is simply the tool that will further enable and advance the digital economy.

### **V. Value Based Questions**

#### **Question 1. Which values are of utmost importance while we get involved in e-business?**

**Answer:** Following values are of utmost importance when we get involved in e-business:

- **Confidentiality:** We must keep information of our clients confidential.
- **Business ethics:** Electronic eye should not be kept for personal usage. Its use must be minimized only for critical situations and in critical areas.
- **No Undesirable Information:** Our website must not advertise or promote any such thing which is not desirable from society point of view.
- **Take all safety precautions:** We must take safety precautions to ensure safety of data and to protect against risks of data storage.

#### **Question 2. Hackers lack certain values. Which are these?**

**Answer:** It will not be wrong to say that hackers lack certain values:

- They do not value the importance of other persons privacy.
- They are keen to use others efforts for their selfish means and even for fun.
- They wish to get many things without putting an effort for it using short cuts and illegal means. But remember in exceptional cases, hacking is also used to find criminals and to solve criminal cases.



# **NCERT SOLUTIONS For Class 11 Business Studies**

## **<http://freehomedelivery.net/Solutions> Chapter 6 Social Responsibilities of Business and Business Ethics**

### **Class 11 Business Studies Solutions Chapter 6 Social Responsibilities of Business and Business Ethics**

NCERT SOLUTIONS For Class 11 Business Studies <http://freehomedelivery.net/Solutions> Chapter 6 Social Responsibilities of Business and Business Ethics

#### **I. Multiple Choice Questions**

**Question 1. Social responsibility is**

- (a) Same as legal responsibility (b) Broader than legal responsibility**
- (c) Narrower than legal responsibility (d) None of them**

**Question 2. If business is to operate in a society which is full of diverse and complicated problems, it may have**

- (a) Little chance of success (b) Great chance of success**
- (c) Little chance of failure (d) No relation with success or failure**

**Question 3. Business people have the skills to solve**

- (a) All social problems (b) Some social problems**
- (c) No social problems (d) All economic problems**

**Question 4. That an enterprise must behave as a good citizen is an example of its responsibility towards**

- (a) Owners (b) Workers**
- (c) Consumers (d) Community**

**Question 5. Environmental protection can best be done by the efforts of**

- (a) Business people (b) Government**
- (c) Scientists (d) All the people**

**Question 6. Carbon monoxide emitted by automobile directly contributes to**

- (a) Water pollution (b) Noise pollution**
- (c) Land pollution (d) Air Pollution**

**Question 7. Which of the following can explain the need for pollution control?**

- (a) Cost savings (b) Reduced risk of liability**
- (c) Reduction of health hazards (d) All of them**

**Question 8. Which of the following is capable of doing maximum good to society?**

- (a) Business success (b) Laws and regulations**
- (c) Ethics (d) Professional management**

**Question 9. Ethics is important for**

- (a) Top management (b) Middle-level managers**
- (c) Non-managerial employees (d) All of them**

**Question 10. Which of the following alone can ensure effective ethics programme in a business enterprise?**

- (a) Publication of code
- (b) Involvement of employees
- (c) Establishment of compliance mechanisms
- (d) None of them

**Answers:**

1. (b) 2. (a) 3. (b) 4. (d) 5. (d)  
6. (d) 7. (c) 8. (c) 9. (d) 10. (c)

## II. Short Answer Type Questions

**Question 1. What do you understand by social responsibility of business? How is it different from legal responsibility?**

**Answer:** Social responsibility of business refers to its obligation to take those decisions and perform those actions which are desirable in terms of the objective and values of our society. It refers to the obligation of business towards various social groups like employees, consumers, investors, government etc. In the words of H. R. Bowen, "Social responsibility of business is to pursue those policies, to make those decisions or to follow those lines of action which are desirable in terms of the objectives and values of our society"

Legal responsibility is the responsibility that a business has by virtue of law. Differences between Social and Legal Responsibility.

- Legal responsibility is compulsory under any of the laws, acts and constitution. Social responsibility is not backed by legal provisions.
- Legal responsibility is compulsion while social responsibility is a choice.
- Many a time, legal responsibility is fulfilled in the name of social responsibility.
- There are no punishments for organizations not following their social responsibility but legal action can be taken against organizations not following their legal responsibility.

**Question 2. What is environment? What is environmental pollution?**

**Answer:** By environment, we mean our surroundings, which have an impact on our lives. It is the sum total of the surroundings and resources, including both biotic resources (i.e., living creatures such as plants and animals) and abiotic resources (i.e., non-living things, such as air, water and land) that affect our existence and quality of life. However, because of the rapid increase in population and industrialisation, the excessive use of resources has resulted in their degradation and depletion. Also, the discharge of harmful substances into the environment has contributed towards pollution. Environmental pollution can be classified into the following four types.

1. **Air Pollution:** It is caused by the emission of harmful gases into the atmosphere.
2. **Water Pollution:** It is caused by the discharge of industrial and household wastes into the rivers, thereby degrading the quality of water.
3. **Land Pollution:** This is caused by dumping toxic wastes on land, which in turn damages it, making it unfit for agriculture.
4. **Noise Pollution:** It is caused by the noise from factories and vehicles, which may cause serious health problems such as loss of hearing or mental disorders.

**Question 3. What is business ethics? Mention the basic elements of business ethics.**

**Answer:** Business ethics refers to the values and principles that govern the behaviour of individuals in an organisation such that the business activities are desirable from the viewpoint of society. The main purpose of business ethics is to guide managers and other employees to perform their jobs in a manner that is socially acceptable.

The following are some of the elements of business ethics.

1. **Top management commitment:** Top-level officers, such as CEO's and senior managers, must strongly follow the ethical codes and guide the other employees in adopting such behaviour.
2. **Publication of a code:** Enterprises must clearly define the ethical code of conduct, which would include quality standards, laws governing production and health and safety standards for the employees.
3. **Establishment of compliance mechanism:** In addition to standards, an enterprise must also devise a mechanism through which compliance with the code of conduct can be measured.
4. **Involvement of employees at all levels:** The successful implementation of ethical standards requires the involvement of all the employees at all levels.
5. **Measurement of results:** Although it is difficult to measure the end results of implementation of ethical standards, the top management should take steps to measure the degree of compliance with the ethical codes.

**Question 4. Briefly explain (a) Air pollution, (b) Water pollution, and (c) Land pollution.**

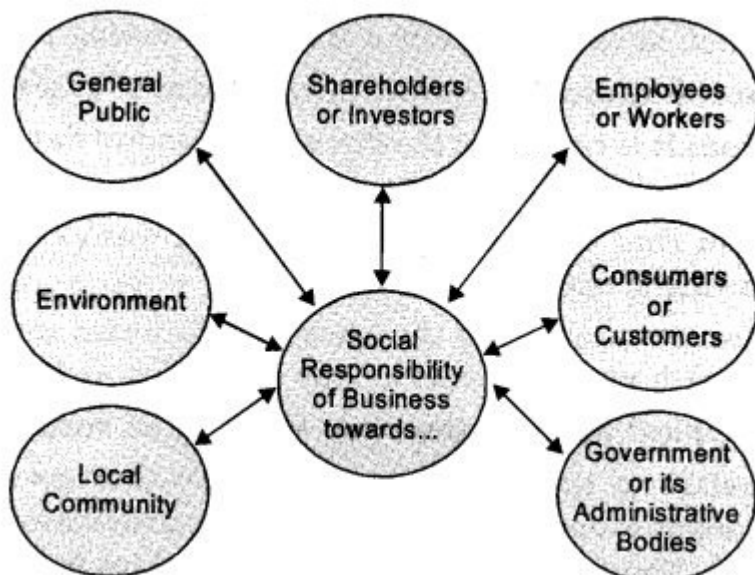
**Answer: (a) Air Pollution:** This kind of pollution is caused by the emission of harmful gases into the atmosphere. Smoke and chemicals emitted by factories and vehicles degrade the air quality and causes air pollution.

**(b) Water Pollution:** Discharge of industrial and household wastes into rivers, streams or lakes causes degradation of the water quality. Over time, the increase in water pollution often results in the deaths of several animals and poses serious threats to human beings.

**(c) Land Pollution:** This is caused due to the dumping of toxic materials and wastes on land, which in turn damages the quality of land, making it unfit and unproductive for agriculture and crop plantation.

**Question 5. What are the major areas of social responsibility of business?**

**Answer:** Major areas for social responsibility of business are given below:



*ARE WITH YOU.....*

- Shareholders or investors who contribute funds for business.
- Employees and others that make up its personnel.
- Consumers or customers who consume and/or use its outputs (products and/or services).
- Government and local administrative bodies that regulate its commercial activities in their jurisdictions.

- Members of a local community who are either directly or indirectly influenced by its activities in their area.
- Surrounding environment of a location from where it operates.
- The general public that makes up a big part of society.

### III. Long Answer Type Questions

#### Question 1. Build up arguments for and against social responsibilities.

##### Answer: Arguments for Social Responsibility:

1. **Justification for Existence and Growth:** Although the main motive of any business is profit but the prosperity and growth of business is not possible without a continuous service to the society. Therefore, it is justified for a business to assume social responsibility.
2. **Avoidance of Government Regulation:** Businessmen can avoid the problem of government regulations by assuming social responsibilities voluntarily which helps to reduce the need for new laws.
3. **Maintenance of Society:** Those people who do not get a return for their hardships get indulged in anti-legal activities. Therefore, it is advisable for business enterprises to assume their social responsibilities.
4. **Long Term Interest of the Firm:** If consumers, workers, shareholders, government officials feel that they are not getting what they deserve, they start to withdraw their hands from business. It may prove more expensive for an enterprise.
5. **Availability of Resources with Business:** A business enterprise has effective human and financial resources to solve many of the social problems.
6. **Converting Problems into Opportunities:** Business can make risky situations useful by using their efficiency.
7. **Better Environment for Doing Business:** Business system should do something to meet needs before it is confronted with a situation when its own survival is endangered.
8. **Holding Business responsible for Social Problems:** Environmental pollution, unsafe workplaces, corruption in public institutions and discriminatory practices in employment are some of the problems which have caused due to business enterprises.

##### Arguments against Social Responsibility:

1. **Violation of Profit Maximization:** As per this argument, business enterprises claim that our objective is profit maximization. Business can reduce its cost and raise profits and then only it can meet its social responsibility.
2. **Lack of Social Skills:** Business enterprises neither have skill nor experience to solve all types of social problems. Therefore, it should be handled by specialized agencies.
3. **Burden on Consumers:** Many of the social responsibilities cost a lot and its burden falls on consumers only.
4. **Lack of Broad Public Support:** Business cannot operate successfully because of lack of cooperation and confidence on behalf of public to business enterprises.

#### Question 2. Discuss the forces which are responsible for increasing concern of business enterprises towards social responsibility.

**Answer:** The following are the forces which are responsible for increasing the concern of business enterprises for social responsibility.



- **Threat of Public Regulation:** The government is meant to safeguard the interests of society. Thus, in case the government feels that a business enterprise is behaving in a manner that is not socially desirable, then it can regulate the operations of that enterprise accordingly.
- **Pressure of Labour Movement:** The increase in capital mobility over time has increased the pressure on business enterprises to pay attention to the welfare of workers, by providing them with healthy working conditions along with good remuneration.
- **Impact of Consumer Consciousness:** As consumers today are aware of their rights and responsibilities, they take their decisions more rationally. Thus, business enterprises are made to work more efficiently and produce better products at reasonable rates to satisfy their customers.
- **Development of Social Standards:** Business enterprises are not merely profit-making entities. For their long-term growth and existence, they require fulfilling the new standards of social welfare.
- **Development of Business Education:** The spread of education over time has made consumers, investors, employees and owners aware of social problems, thereby making them more sensitive to social issues.
- **Relationship Between Social Interest and Business Interest:** No business enterprise can work in isolation from society. Thus, there should be a balance between business interests and social interests, such that the business can grow by doing the maximum good to society.
- **Development of a Professional Managerial Class:** Every business professional pursues the goal of profit maximization. But today's professional managers make efforts to satisfy the interests of all members of society.

**Question 3. 'Business is essentially, a social institution and not merely a profit making activity.' Explain.**

**Answer:** The primary objective of any business enterprise is profit maximization. This is because profit acts as a measure of success and at the same time is the main source of income for an enterprise. Also, profits are often used to finance the expansion projects of a business enterprise. However, it is argued that business enterprises are not merely profit-making entities. They are considered as social institutions, too, as they are created by society. As every business makes use of society's resources in terms of human and physical capital, it cannot work in isolation from society. Its operations are affected by social problems such as unemployment and poverty. Thus, a need arises to create a balance between the business interests and social interests of a business enterprise, such that it can grow by doing the maximum good to society. Hence, we can say that a business enterprise is a social institution and not merely a profit-making entity. In this regard, the following are some of the responsibilities that must be **fulfilled by an enterprise:**

- Paying taxes on time.
- Paying fair wages to employees.
- Supplying quality products at reasonable prices to customers.
- Cooperating with the government in solving social problems, such as unemployment, poverty and illiteracy.

**A business has some responsibility towards:**

- Shareholders or investors who contribute funds for business.
- Employees and others that make up its personnel.
- Consumers or customers who consume and/or use its outputs (products and/or services).
- Government and local administrative bodies that regulate its commercial activities in their jurisdictions.



- Members of a local community who are either directly or indirectly influenced by its activities in their area.
- Surrounding environment of a location from where it operates.
- The general public that makes up a big part of society.

#### **Question 4. Why do the enterprises need to adopt pollution control measures?**

**Answer:** Pollution control is necessary for preserving and improving the quality of environmental resources. As business activities such as production, transportation, distribution, storage and consumption are often assumed to cause the maximum destruction to society's resources, a need arises for adopting pollution control measures. Following are some of the reasons why business enterprises need to adopt pollution control measures,

- **Reduced health hazards:** Pollutants in the environment cause diseases such as cancers and respiratory problems. Thus, pollution control measures will not only help in reducing the incidence of diseases but also help people enjoy a good and healthy life.
- **Reduced risk of liability:** Enterprises are often held responsible for polluting the environment and are asked to compensate. Pollution control helps in reducing the risk of such liabilities.
- **Cost savings:** Efficient pollution control mechanisms help in reducing the cost of waste disposal and the cost of cleaning up production plants. This in turn helps firms to reduce their costs.
- **Improved public image:** An increase in the education level has made people more aware about environmental problems. As a result, they have started realising the need to protect the environment. Thus, business enterprises which adopt pollution control measures enjoy a good reputation in the society.
- **Other social benefits:** Pollution control helps a firm to enjoy various other benefits such as cleaner surroundings, better quality of life for its employees as well as owners and increased availability of good quality resources.

#### **Question 5. What steps can an enterprise take to protect the environment from the dangers of pollution?**

**Answer:** Various business activities such as production, transportation and consumption of goods often result in over exploitation of natural resources. Thus, it is the responsibility of every business enterprise to control discharge of pollutants into the environment. The following steps can be taken by the business enterprises to control pollution.

- **Control by top managers:** The top management of every organisation should be committed to creating, developing and maintaining a work culture conducive to environmental protection and pollution prevention.
- **Control by employees:** Employees at all the levels of an organisation should be committed to keeping the environment clean and protected.
- **Better technology:** Enterprises should employ good and superior technologies of production and use scientific techniques for waste disposal. This will ensure environmental protection and pollution control.
- **Follow rules:** Enterprises must conform to the rules and regulations enacted by the government for the prevention of environmental pollution.
- **Increased awareness:** By conducting workshops and training programmes, business enterprises must make an effort to spread awareness among its employees of the need to conserve the environment.

- **Assessment programmes:** An efficient mechanism for the periodic assessment of pollution control programmes may also be adopted, in order to weigh their costs and benefits.

**Question 6. Explain the various elements of business ethics.**

**Answer:** Business ethics can be defined as the code of conduct that a business must follow, such that it takes up only those activities that are desirable from the viewpoint of society. The purpose of business ethics is to guide managers and other employees in an organisation in performing their jobs in a manner that is socially acceptable. Business ethics should be followed in the day-to-day working of a business enterprise. The following are some of the elements of business ethics.

- **Commitment by top management:** Top-level officers, such as the CEO's and other higher level managers, must sincerely follow the ethical code of conduct. They should also guide other employees in their organisation in adopting the code.
- **Publication of a code:** An enterprise must clearly define the ethical code of conduct to be followed in the organisation. The code should include quality standards for work, laws governing production and employee's health and safety standards.
- **Establishment of compliance mechanism:** In addition to setting performance standards, an enterprise must also devise a mechanism through which it can measure the actions of individual employees. This should be done in order to confirm whether the ethical standards are being met.
- **Involvement of employees at all levels:** The successful implementation of ethical standards depends to a large extent on the involvement of employees at different levels. This is because it is the employees who actually implement the ethical codes.
- **Measurement of results:** Although it is difficult to measure the end results of implementation of ethical standards, the top management should take steps to monitor compliance. Also, it must take serious action against any unethical behaviour in the organisation.

**MORE QUESTIONS SOLVED**

*WE ARE WITH YOU.....*

**I. Very Short Answer Type Questions**

**Question 1. Define corporate social responsibility.**

**Answer:** Corporate social responsibility is a comprehensive set of policies, practices and programmes which are integrated into business operations, supply claims, and decision making process throughout the company, wherever the company does business and includes responsibility for current actions as well as past and future actions.

**Question 2. What is the relation between ethics and moral values?**

**Answer:** Ethics refer to the entire body of moral values which a society attaches to the actions of human beings.

**Question 3. What do you mean by the principles derived from social values which guide and govern the conduct of businessmen?**

**Answer:** Business ethics are principles derived from social values which guide and govern the conduct of businessmen.

**Question 4. Mention two responsibilities of business towards customers.**

**Answer:** Supply of right quality of goods and proper precaution against adulteration.

**Question 5. Give any two reasons supporting social responsibilities.**

**Answer:** (i) It is in long term interest of the business.  
(ii) It is justified for growth and existence of business.

**Question 6. Give any two reasons against social obligation.**

**Answer:** (i) It violates the goal of profit maximization (ii) Its burden falls on consumers.

**Question 7. Name any two factors which affect the ethical behaviour of a business.**

**Answer:** Awareness amongst people, overall environment of the area where business is located.

**Question 8. Define pollution.**

**Answer:** Pollution is change in the physical, chemical and biological characteristics, air, land and water.

**Question 9. Give any one point of difference between ethics and law.**

**Answer:** Ethics are self-imposed while laws are imposed by an external governing authority.

**Question 10. Do businessmen have skill to tackle social problems?**

**Answer:** Yes, businessmen have skills to tackle some but not all social problems.

**Question 11. What is environmental pollution?**

**Answer:** When the quality of environment degrades due to mixture of unwanted elements in it, it is called environmental pollution.

**Question 12. What is the reality of social responsibilities?**

**Answer:** In reality, social responsibility takes form of lip service only. There is no genuine effort from a business. Many a time firms play their legal roles in the name of social responsibility.

**Question 13. What is code of ethics?**

**Answer:** An enterprise must clearly define the ethical code of conduct to be followed in the organisation. The code should include quality standards for work, laws governing production and employee's health and safety standards.

**Question 14. Give any one difference between ethics and law.**

**Answer:** Business ethics refer to the socially determined moral principles which should govern business activities. Laws are determined by the legal bodies of a country.

## **II. Short Answer Type Questions**

**Question 1. What are the core objectives of social responsibility of business?**

**Answer:** The core objectives of social responsibility of business are as follows:

1. It is a concept that implies a business must operate (function) with a firm mindset to protect and promote the interest and welfare of society.
2. Profit (earned through any means) must not be its only highest objective else contributions made for betterment and progress of a society must also be given a prime importance.
3. It must fulfill its social responsibilities honestly in regard to the welfare of society in which it operates and whose resources and infrastructures it makes use of to earn huge profits.
4. It should never neglect (avoid) its responsibilities towards society in which it flourishes.

**Question 2. What are the obligations of a business in the name of social responsibility?**

**Answer:** The social responsibility of business comprises of the following obligations:

- A business must give a proper dividend to its shareholders or investors.
- It must provide fair wages and salaries with good working conditions.
- It must provide a regular supply of good quality goods and/or services to its consumers/customers at reasonable prices.
- It must abide by all government rules and regulations, support its business related policies and should pay fair taxes without keeping any delays or dues.
- It must also contribute for the betterment of a local community by doing generous activities like building schools, colleges, hospitals, etc.
- It must take immense care to see that its activities neither directly nor indirectly create havoc on the vitality of its surrounding environment.
- It should maintain a stringent policy to curb or control pollution in regard to contamination of air, water, land, sound and radiation leakages. It must hire experienced professional individuals who are experts in their respective fields.
- It should also offer social-welfare services to the general public.

**Question 3. Name any four elements of business ethics.**

**Answer:** Business ethics can be defined as the code of conduct that a business must follow, such that it takes up only those activities that are desirable from the viewpoint of society. The purpose of business ethics is to guide managers and other employees in an organisation in performing their jobs in a manner that is socially acceptable.

The following are some of the elements of business ethics.

- Top-level officers, such as the CEO's and other higher level managers, must sincerely follow the ethical code of conduct. They should also guide other employees in their organisation in adopting the code.
- An enterprise must clearly define the ethical code of conduct to be followed in the organisation. The code should include quality standards for work, laws governing production and employee's health and safety standards.
- In addition to setting performance standards, an enterprise must also devise a mechanism through which it can measure the actions of individual employees. This should be done in order to confirm whether the ethical standards are being met.
- The successful implementation of ethical standards depends to a large extent on the involvement of employees at different levels. This is because it is the employees who actually implement the ethical codes.
- Although it is difficult to measure the end results of implementation of ethical standards, the top management should take steps to monitor compliance. Also, it must take serious action against any unethical behaviour in the organisation.

**Question 4. Explain the obligations of business towards owners and investors.**

**Answer:** It is the responsibility of a business to pay attention on the maintenance and expansion of returns for all of its shareholders on important management issue, and constantly strives to improve its business performance and financial structure. The company's dividend policy calls for maintaining stable dividends, and Casio determines the allocation of profit by taking into account all factors such as profit levels, financial position, the dividend pay out ratio, and future business development and forecasts.



**Question 5. How can a business enterprise improve its public image by performing social responsibilities?**

**Answer:** Public relations is a potent tool for shaping consumer perception and building a company's image. Corporations that actively promote their social responsibility activities often take steps to publicise these efforts through the media. Getting the word out about corporate donations, employee volunteer programmes, or other CSR initiatives is a powerful branding tool that can build publicity for you in both online and print media.

**Question.6. What obligation does a businessman have towards the government?**

**Answer:** Social responsibility of business towards government's regulatory bodies or agencies is quite sensitive from the license point of view. If permission is not granted or revoked abruptly, it can result in huge losses to an organization. Therefore, compliance in this regard is necessary. Furthermore, a business must also function within the demarcation of rules and policies as formulated from time to time by the government of state or nation. It should respect laws and abide by all established regulations while performing within the jurisdiction of state. Some examples of activities a business can do in this regard:

- Paying fair taxes on time,
- Following labor, environmental and other laws, etc.
- Seeking permissions wherever necessary,
- Licensing an organization,

If laws are respected and followed, it creates goodwill of business in the eyes of authorities. Overall, if a government is satisfied it will make favourable commercial policies, which will ultimately open new opportunities and finally benefit the organization sooner or later.

**Question 7. Give any four reasons against the social responsibilities of business.**

**Answer:** Arguments against social responsibility

1. **Violation of Profit Maximisation:** As per this argument, business enterprises claim that our objective is profit maximisation. Business can reduce its cost and raise profits and then only it can meet its social responsibility.
2. **Lack of Social Skills:** Business enterprises neither have skill nor experience to solve all types of social problems. Therefore, it should be handled by specialised agencies.
3. **Burden on Consumers:** Many of the social responsibilities cost a lot and its burden falls on consumers only.
4. **Lack of Broad Public Support:** Business cannot operate successfully because of lack of cooperation and confidence from public to business enterprises.

**Question 8. What are the responsibilities of business towards employees and customers?**

**Answer:** Social responsibility of business towards its employees: It is important because they are the wheels of an organization. Without their support, the commercial institution simply can't function or operate.

If a business takes care of the needs of its human resource (for e.g. office staff, employees, workers, etc.) wisely, it will boost the motivation and working spirit within an organization. A happy employee usually gives his best to the organization in terms of quality labour and timely output than an unsatisfied one. A pleasant working environment helps in improving the efficiency and productivity of working people. A

good remuneration policy attracts new talented professionals who can further contribute to its growth

and expansion. Thus, if personnel are satisfied, then they will work together very hard and aid in increasing the production, sales and profit.

**Social responsibility of business towards its consumers or customers:** It matters a lot from sales and profit point of view. Its success is directly dependent on their level of satisfaction. Higher their rate of satisfaction, greater is the chances to succeed.

If a business rolls out good-quality products and/or delivers better quality services that too at reasonable prices, then it is natural to attract lots of customers. If the quality- price ratio is maintained well and consumers get worth for their money spends, this will surely satisfy them. In the long run, customer loyalty and retention will grow, and this will ultimately lead to profitability.

### **Question 9. Describe the obligations of business towards owners and shareholders .**

**Answer:** Social responsibility of business towards its shareholders or investors is most important of all other obligations.

If a business satisfies its investors, they are likely to invest more money in a project. As a result, more funds will flow in and the same can be utilized to modernise, expand and diversify the existing activities on a larger scale. Happy financiers can fulfill the rising demand of funds needed for its growth and expansion.

1. They need to give a fair return to shareholders.
2. They need to give true and fair information to shareholders.
3. They need to give them proper opportunity to participate.

### **Question 10. Which eight problems have been identified by the United Nations which cause damage to natural environment?**

**Answer:** Following eight problems have been identified by the United Nations which cause damage to natural environment:

1. Ozone depletion
2. Global warming
3. Fresh water quality and quantity
4. Deforestation
5. Land degradation
6. Solid and hazardous waste
7. Water pollution
8. Danger to biological diversity.

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### **III. Long Answer Type Questions**

#### **Question 1. Social responsibility is not an area of business. Do you agree? Justify.**

**Answer:** It can be justified by considering case for and case against social responsibility:

The case in favour of taking up social responsibilities.

1. **Existence and growth:** Business enterprises exist to make profits by providing goods and services to consumers. Thus, we can say that their long-term growth prospect depends not only on their profits but also on how efficiently they serve the society. Therefore, taking up social responsibilities supports the existence and growth of a business enterprise.
2. **Avoidance of government intervention:** Business enterprises should always work in line with society's values and ethics. This would help them fulfill their social responsibilities, which in turn would make them less prone to government intervention.
3. **Better environment for doing business:** Businesses make use of society's resource of human capital. Thus, by providing employment to people, they help solve the social problems of unemployment and poverty, thereby creating a favorable environment for business.

**The case against taking up social responsibilities:**

1. **Violation of profit maximization objectives:** It is argued that a business enterprise exists to make a profit. Thus, if it engages itself in solving social problems, then it may not have enough resources to meet its primary objective of profit maximization.
2. **Burden on consumers:** It is argued that when a business enterprise is engaged in solving social problems such as environment pollution and unemployment, its expenditures increase. This increased financial burden is ultimately passed on to the consumers in the form of higher prices of products.
3. **Lack of social skills:** Business persons are basically trained to solve business- related problems such as minimizing cost, maximizing profits and increasing sales. However, they are not specialised in solving social problems. Thus, it is argued that social problems must be solved only by specialised agencies, which have the required training and skills.

## **Question 2. Explain the need for social responsibility.**

**Answer:** Need of social responsibility is essentially a moral question because it can be answered differently by different people depending on what is right and what is wrong for a person. Social responsibility is needed to be followed because:

1. **Showing a true commitment:** The most successful corporate social responsibility programmes integrate these two types of CSR together to show a true commitment to a cause. For example, a company that uses sustainable materials in their products, donates financial resources to environmental causes, and allows employees to take paid time off for volunteering at environmental charities would be showing a true commitment to the environment that goes beyond any single CSR initiative.
2. **Social media visibility:** One of the reasons that corporations should have visible CSR campaigns is due to the importance and prevalence of social media. Corporations that want to protect their brand understand that social media is an integral part of public perception. When a corporation exercises social responsibility in the form of fund raising or setting up employee giving programmes, using social media to promote these actions helps to create a positive branding environment and it is a great way to engage with your audience on a deeper level that goes beyond your products or services.
3. **Public relations benefits:** Public relations is a potent tool for shaping consumer perception and building a company's image. Corporations that actively promote their social responsibility activities often take steps to publicise these efforts through the media. Getting the word out about corporate donations, employee volunteer programmes, or other CSR initiatives is a powerful branding tool that can build publicity for you in both online and print media.
4. **Government relations:** Corporations that put an emphasis on corporate social responsibility typically have an easier experience when dealing with politicians and government regulators. In contrast, businesses that present a reckless disregard for social responsibility tend to find themselves finding off various inquiries and probes, often brought on\*at the insistence of public service organizations. The more positive the public perception is that a corporation takes social responsibility seriously, the less likely it is that activist groups will launch public campaigns and demand government inquiries against it.
5. **Building a positive workplace environment:** Finally, one of the greatest benefits of promoting social responsibility in the workplace is the positive environment you build for your employees. When employees and management feel they are working for a company that has a true conscience, they will likely be more enthusiastic and engaged in their jobs. This can build a sense of community and teamwork which brings everyone together and leads to happier, more productive employees.

### **Question 3. What is corporate social responsibility? Is it similar to business ethics?**

**Answer:** The World Business Council for Sustainable Development in its publication Making Good Business Sense by Lord Holme and Richard Watts, used the following definition. Corporate Social Responsibility is the continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as of the local community and society at large. The same report gave some evidence of the different perceptions of what this should mean from a number of different societies across the world.

**Definition:** CSR is about capacity building for sustainable livelihoods.

It respects cultural differences and finds the business opportunities in building the skills of employees, the community and the Government from Ghana, through to CSR is about business giving back to society from the Philippines.

Traditionally in the United States, CSR has been defined much more in terms of a philanthropic model. Companies make profits, unhindered except by fulfilling their duty to pay taxes. Then they donate a certain share of the profits to charitable causes. It is seen as tainting the act for the company to receive any benefit from the giving. It is not same as business ethics. Business ethics is a personal concept and is wider in many senses than CSR.

### **Question 4. Why should a business do any thing for society at large?**

**Answer:** The term “Corporate Social Responsibility” is still widely used even though related concepts, such as sustainability, corporate citizenship, business ethics, stakeholder management, corporate responsibility, and corporate social performance, are vying to replace it. In different ways, these expressions refer to the ensemble of policies, practices, investments, and concrete results deployed and achieved by a business corporation in the pursuit of its stakeholders’ interests. There is no single CSR business case—no single rationalisation for how CSR improves the bottom line. Over the years, researchers have developed many arguments. In general, these arguments can be grouped based on approach, topics addressed, and underlying assumptions about how value is created and defined. According to this categorization, CSR is a viable business choice as it is a tool to:

- implement cost and risk reductions;
- gain competitive advantage;
- develop corporate reputation and legitimacy; and
- seek win-win outcomes through synergistic value creation.

### **Question 5. Explain the reality of social responsibility.**

**Answer:** In reality, social responsibility receives only lip service. Some business houses fulfill its legal responsibility in the name of social responsibility. There are some factors and reasons which have forced and persuaded business organizations to fulfill their social responsibility which are as follows:

1. **Threat of public regulation:** India is a democracy where Government is expected to be welfare state. If any business organization acts in a socially irresponsible manner, then an action may be taken against them to safeguard people’s interest. In reality, business houses do not assume their social responsibility on their own but due to threat of public action.
2. **Pressure of labour movement:** In the last century, labour movement for extracting gains for the working class throughout the world has become powerful. Labour laws are also followed not out of a sense of social responsibility but because of increasing pressure of labour movement.
3. **Impact of consumer consciousness:** Consumers are also becoming aware of their rights since enactment of Consumer Protection Act, 1986. Under this Act, consumers are entitled to file a case if he is cheated in any ways.



4. **Development of social standard for business:** As per new social standards, a business is considered to be legitimate only if it fulfills its social responsibilities. No business can be done in isolation with the society. The performance of a business is judged on social standards.
5. **Development of business education:** Nowadays businessmen are professionally qualified due to changing pattern of form of business. It is also making it socially more responsible. Education has made people more conscious as employees, customers, investors and owners.
6. **Relationship between social interest and business interest:** Businessmen are able to find that social interest and business interest are correlated. The concept which existed earlier that no business can grow without exploitation of others does not exist any more.
7. **Development of professional, managerial class:** Professional management is also educated of the benefits it can get by fulfilling its social responsibility. Professional managers are more interested in satisfying a multiple group of interest groups in society for running their enterprises successfully than attaining goal of profit maximization only.

**Question 6. “A business owes certain obligations towards different groups.” Identify those groups and explain the obligation of business towards those groups.**

**Or**

**Explain social responsibility of a business towards different interest groups.**

**Answer:** Social responsibility of government towards different groups is explained below:

1. **Shareholders or investors:** Social responsibility of business towards its shareholders or investors is most important of all other obligations.  
If a business satisfies its funders, they are likely to invest more money in a project. As a result, more funds will flow in and the same can be utilised to modernize, expand and diversify the existing activities on a larger scale. Happy financiers can fulfill the rising demand of funds needed for its growth and expansion.
2. **Personnel:** Social responsibility of business towards its personnel is important because they are the wheels of an organization. Without their support, the commercial institution simply can't function or operate.  
If a business takes care of the needs of its human resource (for e.g. of office staff, employees, workers, etc.) wisely, it will boost the motivation and working spirit within an organization. A happy employee usually gives his best to the organization in terms of quality labour and timely output than an unsatisfied one. A pleasant working environment helps in improving the efficiency and productivity of working people. A good remuneration policy attracts new talented professionals who can further contribute in its growth and expansion. Thus, if personnel are satisfied, then they will work together very hard and aid in increasing the production, sales and profit.
3. **Consumers or customers:** Social responsibility of business towards its consumers or customers matters a lot from sales and profit point of view. Its success is directly dependent on their level of satisfaction. Higher their rate of satisfaction greater is the chances to succeed. If a business rolls out good-quality products and/or delivers better quality services that too at reasonable prices, then it is natural to attract lots of customers. If the quality-price ratio is maintained well and consumers get worth for their money spends, this will surely satisfy them. In the long run, customer loyalty and retention will grow, and this will ultimately lead to profitability.
4. **Government:** Social responsibility of business towards government's regulatory bodies or agencies is quite sensitive from the license's point of view. If permission is not granted or revoked abruptly, it can result in huge losses to an organization. Therefore, compliance in this regard is necessary.  
Furthermore, a business must also function within the demarcation of rules and policies as

formulated from time to time by the government of state or nation. It should respect laws and abide by all established regulations while performing within the jurisdiction of state.

Some examples of activities a business can do in this regard:

- (a) Licensing an organization,
- (b) Seeking permissions wherever necessary,
- (c) Paying fair taxes on time,
- (d) Following labour, environmental and other laws, etc.
- (e) If laws are respected and followed, it creates goodwill of business in the eyes of authorities.

Overall, if a government is satisfied it will make favourable commercial policies, which will ultimately open new opportunities and finally benefit the organization sooner or later.

Therefore, satisfaction of government and local administrative bodies is equally important for legal continuation of business.

5. **Local community:** Social responsibility of business towards the local community of its established area is significant. This is essential for smooth functioning of its activities without any agitations or hindrances.

A business has a responsibility towards the local community besides which it is established and operates from. Industrial activities carried out in a local area affect the lives of many people who reside in and around it. So, as a compensation for their hardship, an organization must do something or other to alleviate the intensity of suffering.

- (a) As a service to the local community, a business can build.
- (b) A trust-run hospital or health centre for local patients.
- (c) A primary and secondary school for local children.
- (d) A diploma and degree college for local students.
- (e) An employment centre for recruiting skilled local people, etc.

Such activities to some extent may satisfy the people that make local community and hence their changes of agitations against an establishment are greatly reduced. This will ensure the longevity of a business in the long run.

6. **Environment:** Social responsibility of business with respect to its surrounding environment can't be sidelined at any cost. It must show a keen interest to safeguard and not harm the vitality of the nature. A business must take enough care to check that its- activities don't create a negative impact on the environment. For example, dumping of industrial wastes without proper treatment must be strictly avoided. Guidelines as stipulated in the environmental laws must be sincerely followed. Lives of all living beings are impacted either positively or negatively depending on how well their surrounding environment is maintained (naturally or artificially). Humans also are no exception to this. In other words, health of an environment influences the health of our society. Hence, environmental safety must not be an option else a top priority of every business.
7. **Community:** Finally, social responsibility of business in general can also contribute to make the lives of people a little better.
8. **Some examples of services towards public include:** (a) Building and maintaining devotional or spiritual places and gardens for people,
- (b) Sponsoring the education of poor meritorious students,
  - (c) Organizing events for a social cause, etc.
  - (d) Such philanthropic actions create a goodwill or fame for the business organization in the psyche of general public, which though slowly but ultimately pay off in the due course of time.

#### IV. Higher Order Thinking Skills (HOTS)

**Question 1. "Like an individual, business enterprise should also be a loyal citizen to the state." Discuss.**

**Answer:** It has been rightly said that like an individual, a business enterprise should also be a loyal citizen to the state. Therefore, it has to be kept in mind.

- Social needs of our country while deciding on what goods and services are to be produced. Therefore, a businessman in India must prefer necessities to cosmetics and dog food in a country like India where 26% people are below poverty line.
- Production of liquor, tobacco and other undesirable products should be avoided.
- Production method should be used. If a country is labour abundant, the business should give preference to labour intensive techniques.

**Question 2. Describe the reality of social responsibilities of a company.**

**Answer:** The biggest problem with CSR is not that it has limitations, nor is it concerning its questionable ability to sufficiently address the problems it intends to ameliorate. Rather, it is the fact that it takes people to a completely wrong direction. For many large corporations, CSR is primarily a strategy to divert attention away from the negative social and environmental impacts of their activities. In the Asian context, CSR mostly involves activities like adopting villages for what they call a 'holistic development', in which they provide medical and sanitation facilities, build school and houses, and helping villagers become self-reliant by teaching them vocational and business skills. Such corporate strategies have been effectively hegemonic, providing a strong legitimacy and license for corporations to sustain the exploitation of human and natural resources. More importantly, it leads people to wrongly assume that the business houses, and not the states, are responsible for citizens' basic rights to better education, clean water, healthcare, etc. It disciplines the uninformed poor motivating them to behave in ways that make state regulation obsolete, while leaving them at the mercy of market forces.

**Question 3. Business ethics and social responsibility are not synonyms but are closely related. Substantiate.**

**Answer:** Business ethics and social responsibility are the words that are almost used as a common parlance interchangeably. While social responsibility is self explanatory, ethics is a word that puts one in a dilemma. Social responsibility looks clearly defined and demarcated. Companies have a policy of social responsibility known as Corporate Social Responsibility whereby they commit to follow their businesses in such a way so as to benefit the community at large. But ethics is a loose term that is dependent upon a person's conscience. There are certain differences between the two and the two are not overlapping completely.

**Business Ethics**

To understand business ethics, first we need to understand and spell out clearly the word 'ethics'. Derived from ancient Greek word ethos, ethics has come to mean moral character. Ethical behaviour is what is good or right. Ethical senses always make use of good, bad, right and wrong. Applying this definition to business, we come to a conclusion that though the primary objective of any business or company is to maximize by the decisions taken by the company for the operation of business. Business ethics is the behaviour of any business that it indulges in its dealings with the community or society. For some, making money is all they are interested in, and this is capitalism in its dirtiest form. These people are least concerned with the bad effects of their business practices and the harm they are doing to the society at large. When companies do not engage in good business ethics, they are penalised by the law. But such cases are rare and the profits of companies engaging in unethical behaviour are far more than these punitive fines.

**Social Responsibility**

Man is a social animal and cannot live in isolation. He is expected to behave in a manner that is socially and morally acceptable to others. The same applies to businesses. Though the primary objective of any business is to earn maximum profits for the owners and shareholders, it is also

expected to conduct its operations in a manner that it fulfills its social obligations also. For example, though it is not binding on any private sector company to provide employment to the disabled or weaker sections of the society, it is considered to be a part of the social responsibility of the company to absorb people from such sections of the society. Similarly though there is not written law to compel a company to engage in acts to do something to reduce pollution or to do something for the betterment of environment, taking up projects to clean up environment are considered to be a part of the social responsibility of the company. Difference between Business Ethics and Social Responsibility Though business ethics and social responsibility seem to be overlapping, there has always been a contradiction between the two.

1. Companies, though they are committed to be socially responsible for their behaviour have been found to be engaging in acts that cannot be called ethical.
2. What is good for the society is sometimes not good for the business, and what is good for the business is almost always not good for the society.
3. If the society is conscious, it responds in such a way that businesses are forced to behave responsibly. The same applies to the administration and the judiciary of any country.
4. For example, selling of liquor and tobacco in any society is not against business ethics though it may be against the principles of social responsibility. The same applies to lotteries and gambling. But it is certainly against business ethics as well as against social responsibility to entice minors to engage in smoking and drinking.

## **V. Value Based Questions**

**Question 1. If you start a business, which objective will be of utmost importance to you and why?**

**Answer:** If I start my own business, my social objectives will be of utmost importance to me because:

- It will create employment opportunities in the economy. I will make use of such methods which are desirable from society point of view.
- It will help me to provide good quality product at reasonable prices to my customers.
- It will keep environment pollution free.
- When I will concentrate on these objectives. It will satisfy my consumers and employees. Consumer satisfaction will lead to improvement in my goodwill and market standing. Employee satisfaction will lead to increase in productivity. These two factors will increase profits in the long run automatically.

**Question 2. What do you mean by the principle derived from social values which guide and govern the conduct of businessmen? Explain the factors governing these principles and values.**

**Answer:** Social Return on Investment (SROI) is a principle based method for measuring extra-financial value (i.e., environmental and social value not currently reflected in conventional financial accounts) relative to resources invested. It can be used by any entity to evaluate impact on stakeholders, identify ways to improve performance, and enhance the performance of investments. A network was formed in 2006 to facilitate the continued evolution of the method. Over 570 practitioners globally are members of the SROI Network.

The SROI method as it has been standardized by the SROI Network provides a consistent quantitative approach to understanding and managing the impact of a project, business, organisation, fund or policy. It accounts for stake holders views of impact, and puts financial 'proxy' values on all those impacts identified by stakeholders which do not typically have market values. The aim is to include the values of people that are often excluded from markets in the same terms as used in markets, that is money, in order to give people a voice in resource allocation decisions.



Some SROI users employ a version of the method that does not require that all impacts be assigned a financial proxy. Instead the “numerator” includes monetized, quantitative but not monetized, qualitative, and narrative types of information about value. Benefits that cannot be Monetized: There will be some benefits that are important to stakeholders but which cannot be monetized. An SROI analysis should not be restricted to one number, but seen as a framework for exploring an organization’s social impact, in which monetization plays an important but not an exclusive role. Focus on Monetization: One of the dangers of SROI is that people may focus on monetization without following the rest of the process, which is crucial to proving and improving. Moreover, an organisation must be clear about its mission and values and understand how its activities change the world – not only what it does but also what difference it makes. This clarity informs stakeholder engagement. Therefore, if an organisation seeks to monetize its impact without having considered its mission and stakeholders, then it risks choosing inappropriate indicators; and as a result the SROI calculations can be of limited use or even misconstrued.

**Needs considerable Capacity:** SROI is time and resource, intensive. It is most easily used when an organisation is already measuring the direct and longer term results of its work with people, groups, or the environment.

**Some outcomes not easily associated with monetary value:** Some outcomes and impacts (for example, increased self-esteem, improved family relationships) cannot be easily associated with a monetary value. In order to incorporate these benefits into the SROI ratio proxies for these values would be required. SROI analysis is a developing area and as SROI evolves it is possible that methods of monetizing more outcomes will become available and that there will be increasing number of people using the same proxies.

**Question 3. “The business is responsible for aggravating pollution, so it becomes the moral duty of businessmen to take some positive steps for controlling this problem.” In the light of this statement explain the role of businessmen in checking pollution.**

**Answer:** The statement is perfectly correct. In this regard, a businessman can play the following role:

- He may ensure that he makes use of eco friendly methods of production as far as possible.
- He may ensure that in case any pollution occurs, the waste is discharged in proper manner as per the provisions of pollution control boards.
- He may also create awareness amongst employees on how can they minimize this pollution by initiating workshops, seminars etc.

# **NCERT SOLUTIONS For Class 11 Business Studies**

## **<http://freehomedelivery.net/Solutions> Chapter 8 Sources of Business Finance**

### **Class 11 Business Studies Solutions Chapter 8 Sources of Business Finance**

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#### **I. Multiple Choice Questions**

Tick (✓) the correct answer out of the given alternatives:

Question 1. Equity shareholders are called:

- (a) Owners of the company
- (b) Partners of the company
- (c) Executives of the company
- (d) Guardian of the company

Question 2. The term 'redeemable' is used for

- (a) Preference shares
- (b) Commercial paper
- (c) Equity shares
- (d) Public deposits

Question 3. Funds required for purchasing current assets is an example of

- (a) Fixed capital requirement
- (b) Ploughing back of profits
- (c) Working capital requirement
- (d) Lease financing

Question 4. ADRs are issued in

- (a) Canada
- (b) China
- (c) India
- (d) USA

Question 5. Public deposits are the deposits that are raised directly from

- (a) The public
- (b) The directors
- (c) The auditors
- (d) The owners

Question 6. Under the lease agreement, the lessee gets the right to

- (a) Share profits earned by the lessor
- (b) Participate in the management of the organization
- (c) Use the asset for a specified period
- (d) Sell the assets

Question 7. Debentures represent

- (a) Fixed capital of the company
- (b) Permanent capital of the company
- (c) Fluctuating capital of the company
- (d) Loan capital of the company

Question 8. Under the factoring arrangement, the factor

- (a) Produces and distributes the goods or services
- (b) Makes the payment on behalf of the client

(c) Collects the client's debt or account receivables

(d) Transfer the goods from one place to another

**Question 9. The maturity period of a commercial paper usually ranges from**

(a) 20 to 40 days (b) 60 to 90 days

(c) 120 to 365 days (d) 90 to 364 days

**Question 10. Internal sources of capital are those that are**

(a) Generated through outsiders such as suppliers

(b) Generated through loans from commercial banks

(c) Generated through issue of shares

(d) Generated within the business

**Answers:**

1. (a) 2. (a) 3. (c) 4. (d) 5. (a)

6. (c) 7. (d) 8. (c) 9. (d) 10. (d)

## **II. Short Answer Type Questions**

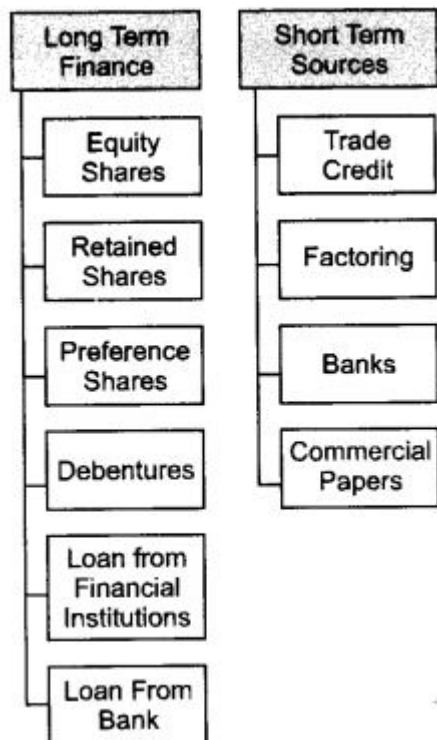
**Question 1. What is business finance? Why do businesses need funds? Explain.**

**Answer:** Business is concerned with production and distribution of goods and services for the satisfaction of need of society. A business cannot function unless adequate funds are made available to it. The need of fund arises from the stage when an entrepreneur makes a decision to start a business. Some funds are needed immediately. The financial need of a business can be categorized in the following ways:

- **Fixed Capital Requirements:** In order to start business, funds are required to purchase fixed assets like land and building, plant and machinery, and furniture and fixtures. This is known as fixed capital requirement of an enterprise.
- **Working Capital Requirements:** The financial requirements of an enterprise do not end with the procurement of fixed assets. No matter how small or large business, it needs funds for its day-to-day operations. This is known as working capital of an enterprise which is used for holding current assets like stock, bill receivable, current expenses etc. Therefore, a business needs funds to meet its fixed as well as working capital requirements.

**Question 2. List sources of raising long-term and short term finance.**

**Answer:** Sources of raising long term and short term finance are shown in the chart given below:



**Question 3. What is the difference between internal and external sources of raising funds? Explain.**

**Answer:** The differences between internal and external sources of raising funds are summarized in the table given as follows:

Basis	Internal Sources	External Sources
Meaning	Internal sources of capital are those sources that are generated within the business.	External sources of raising funds are those which are outside the business.
Example	Ploughing back of profits, equity shares	Financial institutions, loans from banks, preference shares, debentures, public deposits, lease financing, commercial papers, trade credit, factoring
Reliability	It is more reliable.	It is less reliable.

**Question 4. What preferential rights are enjoyed by preference shareholders? Explain.**

**Answer:** Following preferential rights are enjoyed by the preference shareholders:

- They get dividend at a fixed rate and dividend is given on these shares before any dividend on equity shares.
- When company winds up, preference shares are paid before equity shares.



- Preference shares also have a right to participate in excess profits left after payment being made to equity shares.
- They also have a right to participate in the premium at the time of redemption. In lieu of these preferential rights, their voting rights are taken i.e. they are not eligible for voting.

**Question 5. Name any three special financial institutions and state their objectives.**

**Answer:** Given below are three financial institutions along with their objectives:

1. **Industrial Credit and Investment Corporation of India (ICICI):** It came into existence in 1955 as a public limited company under the Companies Act, 1956. **Objective:** ICICI assists the expansion and modernisation of industrial enterprises exclusively in the private sector. The corporation has also encouraged the participation of foreign capital in the country.
2. **Industrial Development Bank of India (IDBI):** It came into existence in 1964 under the Industrial Development Bank of India Act, 1964. **Objective:** Its objective was to coordinate the activities of other financial institutions including commercial banks. The bank performed three types of functions namely, assistance to other financial institutions, direct assistance to industrial concerns and promotion and coordination of financial technique service.
3. **Life Insurance Corporation of India (LIC):** It came into existence in 1956 under the LIC Act 1956 after nationalising 245 existing insurance companies. **Objective:** It mobilises the community saving in the form of insurance premia and makes it available to industrial concerns. Both public as well as private, in the form of direct loan and underwriting of an subscription to shares and debentures.

**Question 6. What is the difference between GDR and ADR? Explain.**

**Answer:** Global Depository Receipts (GDRs): GDR is an instrument issued by a company to raise funds in some foreign currency and is listed and traded on a foreign stock exchange. American Depository Receipts (ADRs): The depository receipts issued by the company in the USA are called American Depository Receipts.  
GDR and ADR are similar to each other except:

- GDR can be issued to anyone but ADRs can be issued only to an American citizen.
- GDR can be listed and traded in stock exchange of any country but ADRs can be listed and traded only in the stock exchange of USA.

### III. Long Answer Type Questions

**Question 1. Explain trade credit and bank credit as sources of short term finance for business enterprises.**

**Answer:** Trade Credit: Trade credit is the credit extended by the trader to another to purchase goods and services. It facilitates the purchase of supplies without immediate payment. In books of accounts they are shown as “creditors’ or ‘ills payable’.

**Merits of Trade Credit**

- It is a convenient and continuous source of finance.
- It is readily available.
- It helps in promoting sales of an organization.
- If an organization wants to expand its inventory level so as to meet expected rise in demand, it may use trade credit.
- It does not demand any security.

## Demerits of Trade Credit

- When easy and flexible trade credit is available, it may induce the firm to indulge in over trading.
- Trade credit can meet only limited financial needs. Funds required for inventory can be met through it but not others like plant and machinery, land and building or salaries of employees etc.

**Bank Credit:** Borrowings from banks are an important source of finance to companies. Bank lending is still mainly short term, although medium-term lending is quite common these days.

### Short term lending may be in the form of:

- An overdraft, which a company should keep within a limit set by the bank. Interest is charged (at a variable rate) on the amount by which the company is overdrawn from day to day.
- A short-term loan, for up to three years.
- Medium-term loans are loans for a period of three to ten years.

The rate of interest charged on medium-term bank lending to large companies will be a set margin, with the size of the margin depending on the credit standing and risk of the borrower. A loan may have a fixed rate of interest or a variable interest rate, so that the rate of interest charged will be adjusted every three, six, nine or twelve months in line with recent movements in the Base Lending Rate.

### Merits of Bank Credit

- **Economical:** Rate of interest charged by banks is quite nominal and is therefore economical.
- **Maintains business secrecy:** Banks maintain secrecy of the business. They do not disclose the information shared to any third party.
- **Less formalities:** As compared to issue of shares, debentures or accepting public deposits, it has less legal formalities..
- **Flexible source:** It can be increased or decreased as per the requirements of the business. It is not so that once a loan is taken it can't be reduced.

### Limitations of Bank Credit

- Short-term financing: It does not provide loans for long term as shares and debentures do.
- Difficult procedure: As compared to commercial papers and trade credit, it involves many legal and paper formalities. It makes its procedure difficult.
- Restrictive clauses: Bank credit has many restrictive clauses which includes mortgage on company's assets or ineligibility to raise funds from specific sources.

### Question 2. Discuss the sources from which a large industrial enterprise can raise capital for financing modernisation and expansion.

**Answer:** A large industrial enterprise can raise capital from the following sources.

1. **Equity Shares:** Equity shares are the most important source of raising long term capital by a company. They represent the ownership of a company and therefore, the capital raised by issue of these shares is called owner's funds. These shareholders do not get a fixed dividend. They get according to the earnings of the company. They receive what is left after all other claims on the

company's income and assets have been settled. They enjoy the reward and also bear the risk of ownership. They have voting rights. Using their voting rights, they get participation in management of the company.

2. **Preference Shares:** Preference shareholders are called so because they enjoy some preferential rights over equity shares. They get dividend at a fixed rate and dividend is given on these shares before any dividend on equity shares. When company winds up, preference shares are paid before equity shares. Preference shares also have a right to participate in excess profits left after payment being made to equity shares. They also have a right to participate in the premium at the time of redemption. In lieu of these preferential rights, their voting rights are taken i.e. they are not eligible for voting. Preference shares have some characteristics of equity shares as well as debentures. They are safer investment with stable return from investor's point of view and free from control from owner's point of view.
3. **Debentures:** Debenture is an acknowledgement by a company that the company has borrowed certain amount from the debenture holder which it promises to pay on a specific date. It is an important source for raising long term debt capital. Debentures bear a fixed rate of interest. In recent times, issue of zero interest debentures has also become popular which do not carry any explicit rate of interest. But they are issued at discount and redeemed at a premium or at par. It is the return on the debenture. Public issue of debentures requires that issue of debentures should be rated by a credit rating agency like CRISIL (Creditrating and Information Services of India Limited).
4. **Loans from Financial Institutions:** The government has established many financial institutions like LIC, IDBI, ICICI etc all over the country to provide finance to these organizations. These institutions are established by central and state government both. These institutions provide owned capital as well as borrowed capital for long term and short term requirements. They provide financial and technical advice and consultancy to business firms. Obtaining loan from a financial institution increases goodwill of a company. These sources are available even during depression. Loans can be repaid in easy instalments.
5. **Loans from Commercial Banks:** Borrowings from banks are an important source of finance to companies. Bank lending is still mainly short term, although medium- term lending is quite common these days. The rate of interest charged on medium- term bank lending to large companies will be a set margin, with the size of the margin depending on the credit standing and risk of the borrower. A loan may have a fixed rate of interest or a variable interest rate, so that the rate of interest charged will be adjusted every three, six, nine or twelve months in line with recent movements in the Base Lending Rate. Short term lending may be in the form of:
  - (i) An overdraft, which a company should keep within a limit set by the bank. Interest is charged (at a variable rate) on the amount by which the company is overdrawn from day to day.
  - (ii) A short-term loan, for up to three years.
  - (iii) Medium-term loans are loans for a period of three to ten years.
6. **Retained Earnings:** For any company, the amount of earnings retained within the business has a direct impact on the amount of dividends. Profit re-invested as retained earnings is profit that could have been paid as a dividend. The management of many companies believes that retained earnings are funds which do not cost anything, although this is not true. However, it is true that the use of retained earnings as a source of funds does not lead to a payment of cash. In practice, the dividend policy of the company is determined by the directors. From their standpoint, retained earnings are an attractive source of finance because investment projects can be undertaken without involving either the shareholders or any outsiders. The use of retained earnings as opposed to new shares or debentures avoids issue costs. The use of retained earnings avoids the possibility of a change in control resulting from an issue of new

shares. Another factor that may be of importance is the financial and taxation position of the company's shareholders. For example, because of taxation considerations, they would rather make a capital profit (which will only be taxed when shares are sold) than receive current income, then finance through retained earnings would be preferred to other methods.

### **Question 3. What advantage does issue of debentures provide over the issue of equity shares?**

**Answer:** Debentures provide following advantages over issue of equity shares.

1. **Voting Rights:** Voting rights are not given to debentures while equity shareholders have voting rights.
2. **Dilution of Controlling Power:** Since voting power is not given, therefore, if funds are raised by issue of debentures then controlling power does not get diluted.
3. **Redeemable:** Debentures are redeemable. Therefore, funds become flexible. When funds are not required permanently but for 5 or 10 years, debentures are more suitable.
4. **Fixed Rate of Interest:** Debentures are to be paid at fixed rate of interest. However, we need to share profits with equity shareholders.
5. **Creditor versus Owner:** Debenture holder is a creditor of the company and cannot take part in the management of the company while a shareholder is the owner of the company. It is the basic distinction between a debenture and a share.
6. **Convertibility:** Shares cannot be converted into debentures whereas debentures can be converted into shares.

### **Question 4. State the merits and demerits of public deposits and retained earnings as methods of business finance.**

**Answer:** Public Deposits: Deposits accepted from public directly by the companies are called public deposits. These deposits generally carry a rate of interest higher than the deposits in commercial banks.

#### **Merits of Public Deposits**

- The procedure of obtaining deposits is simple and does not contain restrictive conditions.
- Cost of public deposits is generally lower than the cost of borrowings from banks and financial institutions.
- Public company usually does not create a charge on the assets of the company.
- As the depositors do not have voting rights, it does not dilute control in the company.

#### **Demerits of Public Deposits**

- It is difficult for a newly established company to be able to get funds from public deposits.
- It is dependent on public response and can't be relied on if financial needs are urgent.
- It is difficult especially when size of deposits is large.

**Retained Earnings:** For any company, the amount of earnings retained within the business has a direct impact on the amount of dividends. Profit re-invested as retained earnings is profit that could have been paid as a dividend.

#### **Merits of Retained Earnings:**



- The management of many companies believes that retained earnings are funds which do not cost anything, although this is not true. However, it is true that the use of retained earnings as a source of funds does not lead to the payment of cash.
- The dividend policy of the company is in practice determined by the directors. From their standpoint, retained earnings are an attractive source of finance because investment projects can be undertaken without involving either the shareholders or any outsiders.
- The use of retained earnings as opposed to new shares or debentures avoids issue costs.
- The use of retained earnings avoids the possibility of a change in control resulting from an issue of new shares.
- Another factor that may be of importance is the financial and taxation position of the company's shareholders. For example, because of taxation considerations, they would rather make a capital profit (which will only be taxed when shares are sold) than receive current income, then finance through retained earnings would be preferred to other methods.

### **Demerits of Retained Earnings:**

- A company must restrict its self-financing through retained profits because shareholders should be paid a reasonable dividend, in line with realistic expectations, even if the directors would rather keep the funds for re-investing.
- At the same time, a company that is looking for extra funds will not be expected by investors (such as banks) to pay generous dividends, nor over-generous salaries to owner-directors.
- Scope of retained earnings is limited by amount of profits. A loss incurring firm has no source called retained earnings.

### **Question 5. Discuss the financial instruments used in international financing.**

**Answer:** Following financial instruments are used in international financing:

1. **Global Depository Receipts (GDRs):** The local currency shares of a company are delivered to the depository bank. The depository bank issues depository receipts against these shares. When these depository receipts are denominated in US \$, they are called GDR. It is a bank certificate issued in more than one country for shares in a foreign company. The shares are held by a foreign branch of an international bank. The shares trade as domestic shares, but are offered for sale globally through the various bank branches. A financial instrument used by private markets to raise capital denominated in either U.S. dollars or Euros. These instruments are called EDRs when private markets are attempting to obtain Euros. It is a negotiable instrument and can be traded freely like any other security. A holder of GDR can convert it into any other security at any time. Holders of GDR are eligible only for capital appreciation and dividend but no voting rights.
2. **American Depository Receipts (ADRs):** When a company in the USA issues depository receipts, they are termed as American Depository Receipts (ADRs). These are bought and sold in stock markets of the USA. They are similar to GDR except that these can be issued only to American citizens and these can be listed and traded on a stock exchange of USA.
3. **Foreign Currency Convertible Bonds (FCCBs):** Foreign Currency Convertible Bonds are equity linked debt securities that are to be converted into equity or depository receipts after a specific period. Foreign Currency Convertible Bonds are listed and traded in Foreign Stock Exchanges. A holder of Foreign Currency Convertible Bonds has the option of converting them into equity shares at a pre-determined price. Foreign Currency Convertible Bonds are issued in foreign currency. Their rate of interest is lower than rate of any other similar non convertible debt instrument.

### **Question 6. What is a commercial paper? What are its advantages and limitations?**

#### **Answer: Commercial Paper:**

- Commercial paper is an unsecured, short-term debt instrument issued by a corporation, typically for the financing of accounts receivable, inventories and meeting short-term liabilities.
- Maturities on commercial paper can range up to 365 days. The debt is usually issued at a discount, reflecting prevailing market interest rates.
- Commercial paper is not usually backed by any form of collateral, so only firms with high-quality debt ratings will easily find buyers without having to offer a substantial discount (higher cost) for the debt issue.

#### **Advantages and Limitations of Commercial Paper Advantages:**

- For the most part, commercial paper is a very safe investment because the financial situation of a company can easily be predicted over a few months.
- Typically only companies with high credit ratings and credit worthiness issue commercial paper. Hence the companies issuing them enjoy (a) the prestige associated with such issuance and (b) the ability to issue large quantum without much hassles like other types of financing which requires restrictions from regulatory bodies.
- Interest rate is generally lower compared to others like bank loans and other types of short term financing

#### **Disadvantage:**

- It does not have any flexibility with regard to repayments.

### **MORE QUESTIONS SOLVED**

#### **I. Very Short Answer Type Questions**

##### **Question 1. Give the full form of GDR and ADR.**

**Answer:** Global Depository Receipts and American Depository Receipts

##### **Question 2. State various sources of long term funds.**

**Answer:** Various sources of long term funds include: Equity shares, preference shares, debentures, retained earnings, loans from financial institutions, loans from commercial banks etc.

##### **Question 3. State various sources of short and medium term funds.**

**Answer:** Short term sources include trade credit, factoring, banks and commercial papers. Middle term credit sources include loans from banks, public deposits, loans from financial institutions and lease financing.

##### **Question 4. What are the preferences given to preference shareholders?**

**Answer:**

1. They get dividend at a fixed rate and dividend is given on these shares before any dividend on equity shares.
2. When company winds up, preference shares are paid before equity shares.
3. Preference shares also have a right to participate in excess profits left after payment being made to equity shares.

4. They also have a right to participate in the premium at the time of redemption.

**Question 5. Name two sources of funds under owner's fund.**

**Answer:** Equity shares and retained earnings

**Question 6. Who are called the owners of a company?**

**Answer:** Equity shareholders are called the owners of the company.

**Question 7. Which deposits are directly raised from the public?**

**Answer:** Public deposits.

**Question 8. What are the two important functions of factors?**

**Answer:** (a) Discounting of bills and collection of the client's receivables.

(b) Providing information to the client on credit worthiness of prospective client.

**Question 9. What is the status of debenture holders?**

**Answer:** Debenture holders are creditors of the company.

**Question 10. In leasing agreement what right is given to lessee?**

**Answer:** The right to use the asset in lieu of specific prepayment for a specific time period.

**Question 11. Preference shares are not suitable for which kind of investors?**

**Answer:** It is not suitable for those investors who want to get a fixed return without failure.

**Question 12. What are Indian depository receipts (IDRs)?**

**Answer:** IDR is an instrument in the form of a depository receipt created by the Indian depository in India against the underlying equity shares of the issuing company.

**Question 13. Name the two Indian companies which have raised money through issue of GDRs.**

**Answer:** WIPRO and ICICI

**Question 14. Who regulates the acceptance of public deposits?**

**Answer:** Reserve Bank of India

**Question 15. What is factoring?**

**Answer:** Factoring is a financial service under which the factor of discounting of the bills of exchange of the clients and collects his debts and also provides him information on credit worthiness of perspective client. He charges fees for the services rendered.

**Question 16. What are retained earnings?**

**Answer:** A company generally does not distribute all its earnings amongst shareholders in the form of dividend. A portion of the net earnings may be retained in the business of use in future. These are called retained earnings.

**Question 17. What are public deposits?**

**Answer:** Public deposits are the deposits raised by organizations directly from the public.

**Question 18. Specify the objective of I.D.B.I.**

**Answer:** Its objective was to coordinate the activities of other financial institutions including

commercial banks. The bank performs three types of functions namely, assistance to other financial institutions, direct assistance to industrial concerns and promotion and coordination of financial technique service.

**Question 19. What do you mean by discounting of bills of exchange?**

**Answer:** Discounting of bills of exchange means that the bank pays the person beforehand at less than face value and receives the payment on maturity equivalent to maturity value. The difference between the amount paid and face value is the return for discounting bills of exchange.

**Question 20. What is a trade credit?**

**Answer:** Trade credit is the credit extended by one trader to another for the purchase of goods and services.

**Question 21. What is debenture?**

**Answer:** A debenture is a document or certificate, which is issued under the common seal of the company, acknowledging its debt to the holders at given terms and conditions.

**Question 22. Why preferences are given to preferential shares?**

**Answer:** They are given some preferences because they are not given the voting rights.

**Question 23. State two factors affecting the fixed capital requirement of a firm.**

**Answer:** Size of business and nature of business.

**Question 24. Why is equity share capital called 'Risk Capital'?**

**Answer:** Equity shareholders get return only when profits are left after paying interest on debentures and fixed return on preference shares. Therefore, it is called risk capital as it bears maximum risk.

**Question 25. State two factors affecting the working capital requirement of a firm.**

**Answer:** Nature of business and speed of sales turnover.

**II. Short Answer Type Questions**

**Question 1. State the meaning of finance. What factors determine working capital and fixed capital requirements of a business?**

**Answer:** No business can be started, run or expanded without finance. There are many sources of finance. Each source has its own merits and demerits. Business needs to choose right source of finance to make the best use of it.

**Business finance refers to the money required for carrying out business activities.**

**Factors determining working capital requirements of a business:**

- **Whether firm is selling goods on credit or cash:** If the firm is selling goods on credit or cash, then its working capital requirements will be more. On the other hand, if it is selling in cash, its working capital requirements will be less.
- **Speed of sales turnover:** A firm whose sales process gets converted into cash soon will have lesser working capital requirements and a firm whose sales process gets converted into cash in delay will have more working capital requirements.
- **Size and scale of business:** If business is operating at a larger scale then working capital requirements will be more. On the other hand, if size and scale of operations is small, its working capital requirements will be less.

**Factors determining Fixed Capital Requirements**



- **Size and scale of business:** If business is operating at a larger scale then fixed capital requirements will be more. On the other hand, if size and scale of operations is small, its fixed capital requirements will be less.
- **Technology:** A firm using labour intensive method needs lesser fixed capital and a firm using capital intensive methods needs more fixed capital.

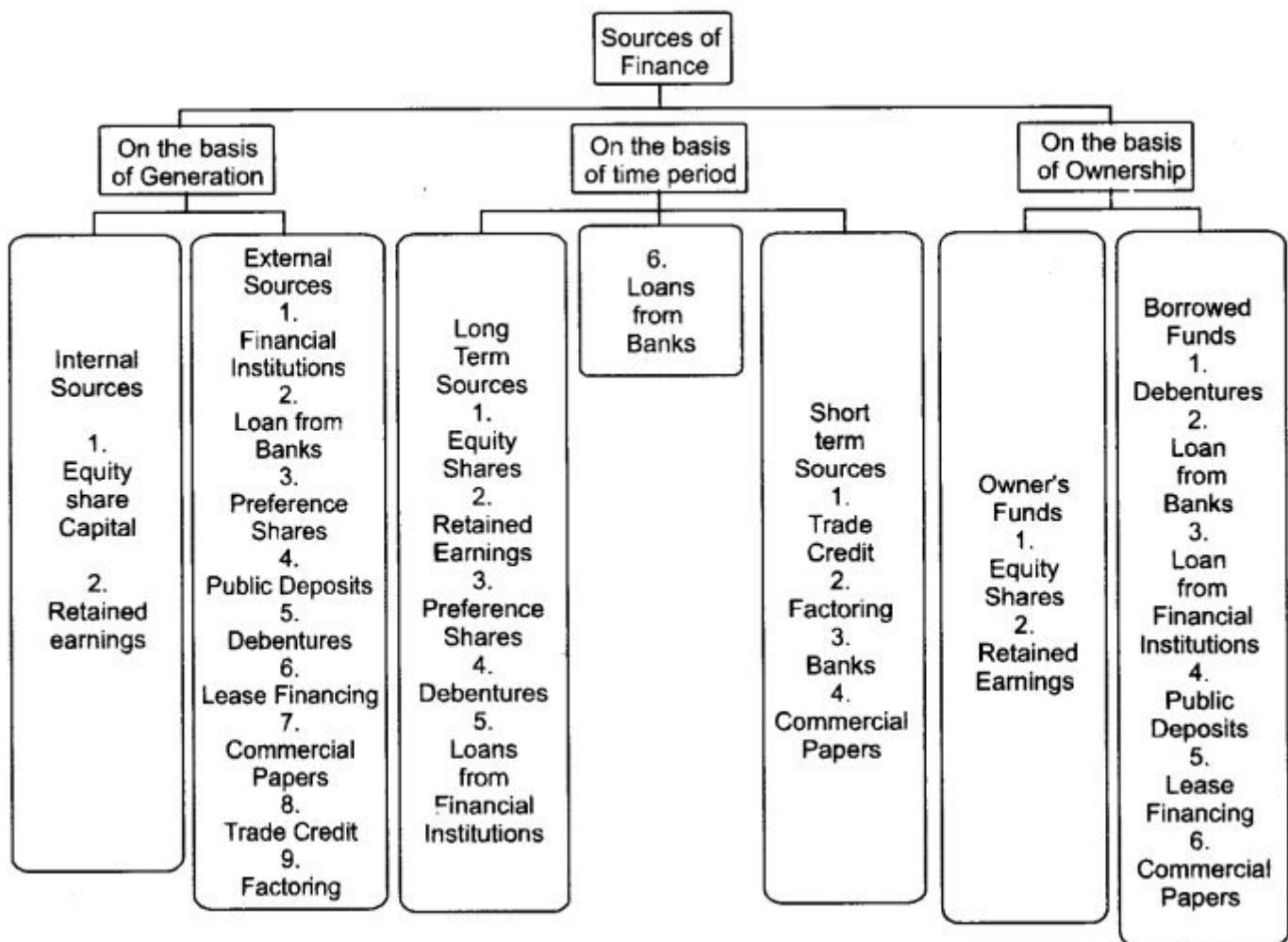
### Question 2. Why does business enterprise need finance?

**Answer:** A business needs finance because:

1. Business is concerned with production and distribution of goods and services for the satisfaction of needs of society. There are four factors required for any production: land, labour, capital and entrepreneur. All these factors need to be paid for their services.
2. No business can be carried without availability of adequate funds.
3. As soon as a decision is taken to start a business, requirement of funds initiates.
4. Finance is called 'life blood of a business'.
5. It is very important to assess financial needs of the organization and the identification of various sources of finance.

### Question 3. List different types of finance.

**Answer:**



**Question 4. Differentiate between:****(a) Fixed Capital and Working Capital****(b) Short Term Finance and Long Term finance****(c) Owner's Funds and Borrowed Funds****(d) Internal Sources and External Sources****Answer:** (a) Fixed Capital and Working Capital

<b>Basis</b>	<b>Fixed Capital</b>	<b>Working Capital</b>
<b>Meaning</b>	In order to start business, funds are required to purchase fixed assets like land and building, plant and machinery, furniture and fixtures etc. It is called fixed capital.	A business needs funds for its day to day operations. This is known as working capital of an enterprise.
<b>Use</b>	It is used to create basic and fundamental structure of business.	It is used for holding current assets such as stock of material, cash in hand, bills receivable and for meeting current expenses like salaries, electricity bill, rent etc.

**(b) Short Term Finance and Long Term Finance**

<b>Basis</b>	<b>Long Term Finance</b>	<b>Short Term Finance</b>
<b>Meaning</b>	Long term finance fulfils the financial requirements of an enterprise for a period exceeding 5 years.	Short term finance fulfils requirements of an enterprise for a period not exceeding one year.
<b>Use</b>	It is used of requiring fixed assets like equipment, plant and machinery etc.	It is used to meet working capital needs.
<b>Example</b>	Shares, debentures, Long term borrowing and Loans from Financial Institutions.	Trade credit, loans from commercial banks, commercial papers etc.

**(c) Owner's Funds and Borrowed Funds**

<b>Basis</b>	<b>Owner's Funds</b>	<b>Borrowed Funds</b>
<b>Meaning</b>	Owner's funds means funds that are provided by the owners of an enterprise.	Borrowed funds refer to the funds raised through loans and borrowings.
<b>Duration</b>	Owner's funds remain in business for a longer duration.	It is in business for shorter duration.
<b>Refund</b>	It is not required to be refunded.	It is required to be refunded.
<b>Example</b>	Equity shares, retained earnings.	Debentures, trade credit, loans, public deposits etc.

(d) Internal and External Sources

Basis	Internal Sources	External Sources
Meaning	Internal sources of funds are those that are generated within the business.	External sources of funds are those sources which lie outside an organization.
Duration	Internal sources remain in business for a longer duration.	It is in business for shorter duration.
Example	Equity shares, retained earnings	Debentures, Trade credit loans, public deposits etc.

**Question 5. Preference shares are preferred by company but not by investors. Why?**

**Answer:** Preference shares have a fixed percentage dividend before any dividend is paid to the ordinary shareholders. As with ordinary shares a preference dividend can only be paid if sufficient distributable profits are available, although with 'cumulative' preference shares the right to an unpaid dividend is carried forward to later years. The arrears of dividend on cumulative preference shares must be paid before any dividend is paid to the ordinary shareholders.

**From the company's point of view, preference shares are advantageous in the following ways:**

1. Dividends do not have to be paid in a year in which profits are poor, while this is not the case with interest payments on long term debt (loans or debentures).
2. Since they do not carry voting rights, preference shares avoid diluting the control of existing shareholders while an issue of equity shares would not.
3. Unless they are redeemable, issuing preference shares will lower the company's gearing. Redeemable preference shares are normally treated as debt when gearing is calculated.
4. The issue of preference shares does not restrict the company's borrowing power, at least in the sense that preference share capital is not secured against assets in the business.
5. The non-payment of dividend does not give the preference shareholders the right to appoint a receiver, a right which is normally given to debenture holders.

However, dividend payments on preference shares are not tax deductible in the way that interest payments on debt are. Furthermore, for preference shares to be attractive to investors, the level of payment needs to be higher than for interest on debt to compensate for the additional risks.

**For the investor, preference shares are less attractive than loan stock because:**

1. They cannot be secured on the company's assets.
2. The dividend yield traditionally offered on preference dividends has been too low to provide an attractive investment compared with the interest yields on loan stock in view of the additional risk involved.

**Question 6. What are the differences between Equity Shares and Preference Shares?**

**Answer:** Differences between Equity shares and Preference shares are as follows:



<b>Basis of Difference</b>	<b>Equity Shares</b>	<b>Preference Shares</b>
1. Payment of dividend	Equity dividend is paid after paying the preference shares dividend.	Preference dividend are paid prior to equity shares dividend.
2. Refund of capital	Equity share is refunded only after refund of preference share capital.	Preference shareholder has prior right to refund the capital over equity capital.
3. Rate of dividend	Rate of dividend may over the year in equity shares.	Rate of dividend is fixed in preference shares.

4. Arrears of dividend	Dividend cannot be accumulated in equity share	Arrears of dividend may be accumulated in preference shares.
5. Convertibility	It is not convertible.	It is convertible.
6. Redeemability	It is not redeemable.	It is redeemable.
7. Voting Right	Every shareholder enjoys voting right on general meeting.	Preference shareholders have no such voting rights.

**Question 7. Write a short note on the features of GDRs.**

**Answer:** GDRs have following features:

- A bank certificate issued in more than one country for shares in a foreign company. The shares are held by a foreign branch of an international bank. The shares trade as domestic shares, but are offered for sale globally through the various bank branches.
- A financial instrument used by private markets to raise capital denominated in either U.S. dollars or Euros.
- Holders of GDR are eligible only for capital appreciation and dividend but no voting rights.
- These instruments are called EDRs when private markets are attempting to obtain Euros.
- It is a negotiable instrument and can be traded freely like any other security.
- A holder of GDR can convert it into any other security at any time.

**Question 8. Name zones of the Lessors and Lessees in India.**

**Answer:** The Lessors

- Specialised Leasing Companies'
- Banks and Bank Subsidiaries
- Specialised Financial Institutions
- Manufacturer Lessors The Lessees
- Public Sector Undertakings
- Mid Market Companies
- Consumers
- Government Departments and Authorities



**Question 9. Classify internal and external sources on the basis of time.**

**Answer:**

	<b>Short-Term</b>	<b>Medium-Term</b>	<b>Long-Term</b>
<b>Internal Sources</b>	Retained Profits Selling Assets Working Capital	Retained Profits	Investing Extra Cash

<b>External Sources</b>	Overdrafts Trade Credit Government Grants Donations Sponsorships  Debt Factoring Leasing Hire Purchase Venture Capitalists Preferred Shares	Government Grants Sponsorship Leasing Hire Purchase Bank Loans and Mortgages  Venture Capitalists	Ordinary Shares Government Grants Leasing Hire Purchase  Bank Loans and Mortgages Debentures
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**Question 10. What is factoring? Discuss its pros and cons.**

**Answer:** Debtors are the people who owe money to a business. Debt factoring is a financial service that allows a business to raise funds based on the value owed to them by their debtors. Example: Receiving 80% of debtors outstanding debt on selling fabric abroad.

**Advantages:**

1. It reduces the probability of bad debt-debtors.
2. Non-recourse factoring allows for insurance against bad debts.
3. Companies don't have to chase up their own debtors.
4. Immediate sources of finance.

**Disadvantages:**

1. Without non-recourse factoring the company will still have to absorb losses.
2. It is expensive.

### III. Long Answer Type Questions

**Question 1. Explain different types of preference shares which can be issued by a company.**

**Answer:** Different types of preference shares are discussed below:

1. **Cumulative and Non-cumulative:** The preference shares which enjoy the right to accumulate unpaid dividends in future years if it is not paid during a year are termed as cumulative preference shares. On the contrary, a non-cumulative preference share is one in which dividend is not accumulated if it is not paid in the particular year. .

2. **Participating and Non-participating Preference Shares:** Those preference shares which have a right to participate in further surplus of a company's shares which after dividend at certain rate has been paid on equity shares are called participating preference shares. Those preference shares which do not have a right to participate in further surplus of a company's shares which after dividend at certain rate has been paid on equity shares are called non-participating preference shares.
3. **Convertible and Non-convertible Preference Shares:** Those preference shares which can be converted into equity shares within a specified period of time are called convertible preference shares. On the contrary, preference shares which cannot be converted into equity shares within a specified period of time are called non-convertible preference shares.

**Question 2. Describe in brief the features of equity shares.**

**Answer:** Equity shares are the most important sources of raising long term capital by a company. They represent the ownership of a company and therefore, the capital raised by issue of these shares is called owner's funds. Features of equity shares:

- **Voting Rights:** They have voting rights and hence they are the owners of the business.
- **Participation in Management:** Using their voting rights, equity shares holders get a right to participate in company's management.
- **Return:** These shareholders do not get a fixed dividend. They get according to the earnings of the company. They receive what is left after all other claims on the company's income and assets have been settled.
- **Risk:** They enjoy the reward and also bear the risk of ownership. Therefore, it is also called risk capital.
- **Permanent Capital:** Equity capital serves as permanent capital as it is to be repaid only at the time of liquidation of a company.
- **No charge on assets of the company:** Funds can be raised though equity issue without creating any charge on the assets of a company. The assets of a company are therefore, free to be mortgaged for the purpose of borrowings, if the need be.
- **More Costly:** The cost of equity shares is generally more as compared to the cost of raising funds through other sources.

**Question 3. Differentiate between a share and a debenture.**

**Answer:** Following are the main differences between a debenture and a share:

1. Debenture holder is a creditor of the company and cannot take part in the management of the company while a shareholder is the owner of the company. It is the basic distinction between a debenture and a share.
2. Debenture holders will get interest on debentures and will be paid in all circumstances, whether there is profit or loss will not affect the payment of interest on debentures. Shareholder will get a portion of the profits called dividend which is dependent on the profits of the company. It can be declared by the directors of the company out of profits only.
3. Shares cannot be converted into debentures whereas debentures can be converted into shares.
4. Debentures will get priority in getting the money back as compared to shareholder in case of liquidation of a company.
5. There are no restrictions on the issue of debentures at a discount, whereas shares at discount can be issued only after observing certain legal formalities.
6. Convertible debentures which can be converted into shares at the option of debenture holder can be issued whereas shares convertible into debentures cannot be issued.

7. There can be mortgage debentures i.e. assets of the company can be mortgaged in favor of debenture holders. But there can be no mortgage shares. Assets of the company cannot be mortgaged in favor of shareholders.

**Question 4. What are retained profits? Discuss their advantages and disadvantages.**

**Answer:** Retained Profits: For any company, the amount of earnings retained within the business has a direct impact on the amount of dividends. Profit re-invested as retained earnings is profit that could have been paid as a dividend. The management of many companies believes that retained earnings are funds which do not cost anything, although this is not true. However, it is true that the use of retained earnings as a source of funds does not lead to a payment of cash. The dividend policy of the company is in practice determined by the directors. From their standpoint, retained earnings are an attractive source of finance because investment projects can be undertaken without involving either the shareholders or any outsiders. The use of retained earnings as opposed to new shares or debentures avoids issue costs. The use of retained earnings avoids the possibility of a change in control resulting from an issue of new shares. Another factor that may be of importance is the financial and taxation position of the company's shareholders. For example, because of taxation considerations, they would rather make a capital profit (which will only be taxed when shares are sold) than receive current income, and then finance through retained earnings would be preferred to other methods.

**Advantages of Retained Earnings**

- The management of many companies believe that retained earnings are funds which do not cost anything, although this is not true. However, it is true that the use of retained earnings as a source of funds does not lead to a payment of cash.
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- Another factor that may be of importance is the financial and taxation position of the company's shareholders. If, for example, because of taxation considerations, they would rather make a capital profit (which will only be taxed when shares are sold) than receive current income, then finance through retained earnings would be preferred to other methods.

**Disadvantages of Retained Earnings**

- A company must restrict its self-financing through retained profits because shareholders should be paid a reasonable dividend, in line with realistic expectations, even if the directors would rather keep the funds for re-investing.
- At the same time, a company that is looking for extra funds will not be expected by investors (such as banks) to pay generous dividends, nor over-generous salaries to owner-directors.
- Scope of retained earnings is limited by amount of profits. A loss incurring firm has no source called retained earnings.

**Question 5. Write a note on international sources of finance.**

**Answer:**

- **Commercial banks:** Commercial banks all over the world extend foreign currency loans for business purposes. For e.g. Standard Chartered emerged as a major source of foreign currency

loans to the Indian industry. The types of loans and services provided by banks vary from country to country.

- **International agencies and Development banks:** These bodies provide long and medium term loans and grants to promote the development of economically backward areas in the world. The more notable among them include International Finance Corporation(IFC), EXIM Bank and Asian Development Bank.
- **International Capital Markets:** Modern organizations including multinational companies depend upon sizeable borrowing in rupees as well as in foreign currency. Prominent financial instruments used for this purpose are:
  1. Global Depository Receipts (GDR's)
  2. American Depository Receipts(ADR's)
  3. Foreign Currency Convertible Bonds(FCCB's)

**Question 6. Explain in detail the types of debenture a company can issue.**

**Answer:** Different types of debentures that a company can issue are described below:

1. **Convertible and Non-convertible Debenture:** Convertible debentures are those debentures that can be converted into equity shares after the expiry of a specified period. On the other hand, non-convertible debentures are those which cannot be converted into equity shares.
2. **Registered and Bearer:** Registered debentures are those which are duly recorded in the register of debentures holders maintained by the company. These can be transferred only through a regular instrument of transfer. In contrast the debentures which are transferable by mere delivery are called bearer debentures.
3. **Secured and Unsecured:** Secured debentures are such which create a charge on the assets of the company, thereby mortgaging the assets of the company. Unsecured debentures on the other hand do not carry any charge or security on the assets of the company.
4. **First and Second:** Debentures that are repaid before other debentures are known as first debentures. The second debentures are those which are paid after the first debentures have been paid back.

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**Question 7. Describe briefly the factors responsible for selecting a source of finance.**

**Answer:** Following factors responsible for selecting a source of finance:

- **Cost:** There are two types of cost viz., the cost of procurement of funds and cost of utilizing the funds. Both these costs should be taken into account while deciding about the source of funds that will be used by an organisation.
- **Form of organisation and legal status:** The form of business organisation and status influences the choice of a source for raising money. A partnership firm cannot raise money by issue of equity shares as these can be issued only by a joint stock company.
- **Risk Profile:** Business should evaluate each of the sources in terms of risk. For example, equity shares are to be repaid only at the time of liquidation of the company. While debentures need to be repaid on maturity date along with interest every six months or annually. Moreover, dividends are to be paid only if there are profits while interest is to be paid in case of loss as well.
- **Financial Strength and Operational Stability:** When the earnings of an organization are not stable, fixed charged funds like preference shares and debentures should be carefully chosen as they add to the fixed financial commitments of an organization.
- **Purpose and Time Period:** Business should select a source of finance according to time period for which funds are required. If funds are needed for short term, then we can make use



of trade credit, commercial papers, bank loan, public deposits, etc but if funds are needed for long run then debentures, preference shares etc. are better.

- **Control:** A particular source of fund may affect the control and power of the owners of management of a firm. For example, equity shares dilute the control as they have voting power while other sources do not have voting power but loans from financial institutions, loans from commercial banks and issue of debentures get mortgaged on assets of the company. It dilutes power in different ways.
- **Effect on Credit Worthiness:** While choosing a source of finance, an organization also needs to consider its effect on credit worthiness. For example, if the company issues secured debentures then it affects the credit worthiness of company for unsecured debentures of the company. Their willingness to extend further loans as credit to the company gets adversely affected.
- **Tax Benefits:** Various sources of finance may also be evaluated in terms of their tax benefits. For example, interest on debentures is tax deductible while dividend on preference shares is not tax deductible. Therefore those organizations which are seeking tax advantage may prefer debentures to preference shares.
- **Flexibility and Ease:** Another factor which determines the choice of a source of finance is how easily it is available i.e. how less the paper formalities are and how flexible it is i.e. how easily its amount and terms can be modified.

#### **Question 8. What is lease financing? Discuss its merits and demerits.**

**Answer:** A lease is a contractual agreement, in which the owner of the asset grants the other party the right to use the asset in return for a periodic payment, but retains the title over the property. The owner of the asset is called lessor and the party who uses the assets is called lessee.

Lessee pays a fixed periodic amount to the lessor. It is called lease rent. When period of lease expires, the asset is returned to the lessor. It is used more frequently with items like computers and electronic items which become obsolete soon. Leasing company (lessor) owns the equipment and hires it out to the customers (lessee pays rental income to hire assets). It is a medium term fund. New companies need expensive equipments to run the business: office, equipment leasing from larger companies like Apple.

#### **Merits of Lease financing**

- It allows the lessee to acquire the asset with lesser investment.
- Simple documentations makes it easier to finance assets.
- Lease rentals get tax advantage as they are deductible for computing taxable profits.
- It reduces initial capital for (new) businesses.
- It provides added service: maintenance and upgrading.
- It makes funds available without diluting the ownership of business.
- The lease agreement does not bring any change in raising capacity of an organization.
- The risk of obsolescence is borne by the lessor.

#### **Demerits of Lease Financing**

- A lessee agreement imposes restrictions on usage of assets. For example, alteration and modification in assets may not be allowed.
- The normal business operations may be affected if lease is not renewed.
- It may result in higher payout obligations in case the equipment is not found useful and the lessee chooses for premature termination of the lease contract.
- It never makes lessee the owner of the asset.

#### **IV. Higher Order Thinking Skills (HOTS)**

**Question 1. Mr. John has ? 1,00,000 for investment purposes. Should he invest in equity shares, preference shares, public deposits or debentures? Justify your answer.**

**Answer:** John's investment depends on many factors:

- If he wants control in the company or participation in management of the company, he should invest in equity shares.
- If he wants some certainty in returns and also wants something extra in case of huge profits, he should invest in preference shares.
- If he wants perfect certainty, he should invest in public deposits or debentures as rate of return is pre fixed.
- He also needs to see if he wants to invest for short term or long term. If he is interested in short term investment, then he should choose public deposits.
- If he is interested in middle term investment, he should invest in preference shares or debentures.
- If he is interested in long term investment, he should invest in equity shares.

**Question 2. As a source of finance retained profit is better than other sources. Do you agree with this view? Give reasons for your answer.**

**Answer:** Yes, we agree. Retained earnings are better than other sources of finance because:

- Retained earnings is a permanent source of funds which an organization can avail of.
- It enhances capacity of the business to absorb unexpected losses.
- It does not involve any explicit cost in the form of interest, dividend or flotation cost.
- It may increase the process of equity shares of a company.
- There is a greater degree of operational freedom and flexibility as the funds are generated internally.

#### **V. Value Based Questions**

**Question 1. Retained earnings are not a good source from the values point of view as it is the right of equity shareholders. Do you agree? Justify your answer.**

**Answer:** Equity shareholders get a return only when profits are left after giving interest to debenture holders and preferential dividend to preference shareholders. In case, no profits are left after it, they do not get a return. Therefore, it is unreasonable to transfer funds to general reserves which are called retained profits if there are exceptionally good profits. They took the risk of uncertain returns. Then it is their right to get exceptional returns in good times. But in good times, it is being retained to plough back into the business. Therefore, it is right to say that retained earnings are not a good source from the values point of view as it is the right of equity shareholders.

**Question 2. Debentures are good from debenture holders point of view but not for business. Do you agree? Explain.**

**Answer:** Debentures are similar to shares, however, debenture holders do not have voting rights on how the business is run.

Debentures have certain merits and demerits from business as well as debenture holders point of view. **These are explained below:**

##### **Advantages to Debenture Holders**

- They receive annual interest/ benefits (VIP status or free passes) regardless of whether or not the business is making money.

### **Disadvantages to Debenture Holders**

- No say in how the business will run.
- Greatly depends on the business' success to reuse it's value.

### **Advantages to Business**

- Provides good long-term finance without losing control of the business.

### **Disadvantages to Business**

- Firm increases the amount of long-term liabilities raising the amount of interest payments to the lenders.



# NCERT SOLUTIONS For Class 11 Business Studies

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### Class 11 Business Studies Solutions Chapter 9 Small Business

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#### I. Short Answer Type Questions

**Question 1. What are the different parameters used to measure the size of business?**

**Answer:** Following parameters may be used to measure the size of business:

- (a) Number of workers employed (b) Size of plant and machinery  
(c) Total output (d) Inventory size

**Question 2. What is the definition used by government of India for Small Scale Industries?**

**Answer:** Government uses the criterion of size of capital employed in plant and machinery to define Small Scale Industries. It is depicted in the table given below:

Type of Industry	Investment Limit (₹)
Small Scale Industry	1 crore (For 71 products it is 5 crores)
Ancillary Industry	1 crore (50% of the output supplied to the parent unit.)
Tiny Enterprise	25 Lakhs
Service and Business (Industry related Enterprise)	10 Lakhs
Women Enterprise	Any of the above (51% of the holding by the women and managed by women)
Export Oriented Units (EOUs)	1 Crore (100% EOUs can sell 25% in domestic markets.)



**Question 3. How would you differentiate between an ancillary unit and a tiny unit?**

**Answer:**

<b>Basis of difference</b>	<b>Ancillary Industrial units</b>	<b>Tiny units</b>
<b>Definition</b>	Industrial units that have to supply a minimum of 50% of their production to their parent industries are termed ancillary industrial units.	Industries that have a maximum investment of ₹ 25 lakh in their plant and machinery are termed as tiny industrial units.
<b>Obligation</b>	Such units have to supply at least 50% of their production to their parent industries.	No such obligations.
<b>Investment limit</b>	The maximum level of investment is ₹ 1 crore.	The maximum level of investment is ₹ 25 lakh.
<b>Examples</b>	Industries engaged in the production of machine parts, tools and other intermediate products.	Business units such as small shops, boutiques, STD (subscriber trunk dialling) booths and photocopy centres.

**Question 4. State the features of cottage industries.**

**Answer:** The following are a few important features of cottage industries.

- **Ownership:** These are rural-based industries owned and operated by individuals who invest their private resources in these units.
- **Level of capital and production techniques:** The amount of capital is very small, and the production techniques are highly labour-intensive and indigenous.
- **Employment:** These industries generally do not hire labour but employ the owners family members.
- **Talent and skills:** Usually, the talent and the skills required for cottage industries are found restricted to particular families. The skills are passed on from one generation to the next. For instance, the art of pottery remains restricted to potter families.
- **Market:** Although the production is primarily carried out for self-consumption, a portion of the output is sold in the local market as well.

## **II. Long Answer Type Questions**

**Question 1. How do small scale industries contribute to the socio-economic development of India?**

**Answer:** Small-scale industries (SSIs) play an important role in ensuring the progress of developing countries such as India. The following points highlight their contribution.

- **Market Share:** SSIs make up 95 per cent of the industrial units in India. They contribute about 40 percent of the 'gross industrial value added' and 45 per cent of India's total exports.
- **Regional Balance:** SSIs produce simple products and use basic technology. In addition, these industries do not require heavy capital investment, and therefore, they can be set up by anyone anywhere across the country. Small units not only benefit the particular region where it is established but also help reduce the regional disparities in industrial development among different regions of a country.

- **Employment Generation:** As SSIs use labour-intensive production techniques, they have a greater employment generation potential than large industries. Moreover, the skills required to perform jobs in SSIs are usually not very specific, which further increases their scope for generating employment.
- **Wide range of Products:** Small scale units produce a large variety of consumer products, such as stationery items, safety matches, handicrafts, vegetables and processed food. Besides, SSIs also produce a few items by using technology, such as calculators, televisions and engineering goods.
- **Customized Goods:** Small industrial units adapt perfectly to specific needs of consumers. As SSIs use simple and highly flexible production techniques, they can provide their customers with goods best suited to the customers tastes and preferences.

## Question 2. Describe the role of small business in rural India?

**Answer:** The following are some of the major roles played by small scale businesses in rural India.

- **They generate employment opportunities:** Cottage and rural industries play a significant role in providing employment opportunities, particularly to people in rural areas. This proves to be a boon especially for the economically weaker sections of the rural society.
- **They enable equitable income distribution:** The capital requirements of small- scale businesses are low, mainly because of their use of labour-intensive production techniques, and this encourages entrepreneurs to start units on a small scale. Small- scale businesses are, therefore, set up all over the country. Many of them providing employment opportunities to people in rural areas. This triggers the redistribution of wealth and income, and enables the equitable distribution of income in rural areas.
- **They help to accelerate growth:** Small-scale businesses have been considered as a major propeller for the acceleration of economic growth and as an employment generator, particularly in the rural and backward areas of India.
- **They mitigate disguised unemployment and alleviate poverty:** Small-scale businesses use labour-intensive production techniques, and are, therefore, able to provide employment to the excess/surplus rural labour. Thus, small-scale businesses remove disguised unemployment from the agriculture sector and at the same time provide livelihood to the rural people. Hence, they contribute to alleviating rural poverty.
- **They facilitate rural development and reduce migration from rural to urban areas:** It is well known that a large number of people migrate from rural to urban areas in search of better employment opportunities and improved living standards. Small-scale businesses help reduce this migration by providing employment opportunities to rural people in their own regions. By doing so, small units also help mitigate the excessive pressure on urban infrastructure.

## Question 3. Discuss the problems faced by small scale industries.

**Answer:** Major problems faced by the small scale industries are: (1) Finance (2) Raw material (3) Idle capacity (4) Technology (5) Marketing (6) Infrastructure (7) Under Utilization of Capacity (8) Project Planning.

Small scale industries play a vital role in the economic development of our country. This sector can stimulate economic activity and is entrusted with the responsibility of realising various objectives i.e., generation of more employment opportunities with less investment, reducing regional imbalances etc. Small scale industries are not in a position to play their role effectively due to various constraints. The various constraints, the various problems faced by small scale industries are as under:

1. **Finance:** Finance is one of the most important problems confronting small scale industries. Finance is the life blood of an organisation and no organisation can function properly in the absence of adequate funds. The scarcity of capital and inadequate availability of credit facilities are the major causes of this problem. Firstly, adequate funds are not available and secondly, entrepreneurs due to weak economic base, have lower credit worthiness. Neither they are having their own resources nor are others prepared to lend them. Entrepreneurs are forced to borrow money from money lenders at exorbitant rate of interest and this upsets all their calculations.

After nationalisation, banks have started financing this sector. These enterprises are still struggling with the problem of inadequate availability of high cost funds. These enterprises are promoting various social objectives and in order to facilitate them working adequate credit on easier terms and conditions must be provided to them.

2. **Raw Material:** Small scale industries normally tap local sources for meeting raw material requirements. These units have to face numerous problems like availability of inadequate quantity, poor quality and even supply of raw material is not on regular basis. All these factors adversely affect the functioning of these units.  
Large scale units, because of more resources, normally come whatever raw material is available in the open market. Small scale units are thus forced to purchase the same raw material from the open market at very high prices. It will lead to increase in the cost of production thereby making their functioning unavailable.
3. **Idle Capacity:** There is under utilization of installed capacity to the extent of 40 to 50 per cent in case of small scale industries. Various causes of this under utilization are shortage of raw material problem associated with funds and even availability of power. Small scale units are not fully equipped to overcome all these problems as is the case with the rivals in the large scale sector.
4. **Technology:** Small scale entrepreneurs are not fully exposed to the latest technology. Moreover, they lack requisite resources to update or modernise their plant and machinery. Due to obsolete methods of production, they are confronted with the problems of less production in inferior quality and that too at higher cost. They are in no position to compete with their better equipped rivals operating modern large scale units.
5. **Marketing:** These small scale units are also exposed to marketing problems. They are not in a position to get first hand information about the market i.e., about the competition, taste, liking, disliking of the consumers and prevalent fashion.

With the result they are not in a position to upgrade their products keeping in mind market requirements. They are producing less of inferior quality and that too at higher costs. Therefore, in competition with better equipped large scale units they are placed in a relatively disadvantageous position.

In order to safeguard the interests of small scale enterprises the Government of India has reserved certain items for exclusive production in the small scale sector. Various government agencies like Trade Fair Authority of India, State Trading Corporation and the National Small Industries Corporation are extending helping hand to small scale sector in selling its products both in the domestic and export markets.

6. **Infrastructure:** Infrastructure aspects adversely affect the functioning of small scale units. There is inadequate availability of transportation, communication, power and other facilities in the backward areas. Entrepreneurs are faced with the problem of getting power connections and even when they are lucky enough to get these they are exposed to unscheduled long power cuts.

Inadequate and inappropriate transportation and communication network will make the working of various units all the more difficult. All these factors are going to adversely affect the

quantity, quality and production schedule of the enterprises operating in these areas. Thus their operations will become uneconomical and unviable.

7. **Under Utilization of Capacity:** Most of the small-scale units are working below full potentials or there is gross under utilization of capacities. Large scale units are working for 24 hours a day i.e., in three shifts of 8 hours each and are thus making best possible use of their machinery and equipment's.

On the other hand, small scale units are making only 40 to 50 percent use of their installed capacities. Various reasons attributed to this gross under utilization of capacities are problems of finance, raw material, power and underdeveloped markets for their products

8. **Project Planning:** Another important problem faced by small scale entrepreneurs is poor project planning. These entrepreneurs do not attach much significance to viability studies i.e., both technical and economical and plunge into entrepreneurial activity out of mere enthusiasm and excitement.

They do not bother to study the demand aspect, marketing problems, and sources of raw materials and even availability of proper infrastructure before starting their enterprises. Project feasibility analysis covering all these aspects in addition to technical and financial viability of the projects, is not at all given due weight age. Inexperienced and incomplete documents which invariably results in delays in completing promotional formalities. Small entrepreneurs often submit unrealistic feasibility reports and incompetent entrepreneurs do not fully understand project details.

Moreover, due to limited financial resources they cannot afford to avail services of project consultants. This results in poor project planning and execution.

9. **Skilled Manpower:** A small scale unit located in a remote backward area may not have problem with respect to unskilled workers, but skilled workers are not available there. Firstly, skilled workers may be reluctant to work in these areas and secondly, the enterprise may not afford to pay the wages and other facilities demanded by these workers. Besides non-availability of entrepreneurs are confronted with various other problems like absenteeism, high labour turnover indiscipline, strike etc. These labour related problems result in lower productivity, deterioration of quality, increase in wastages, and rise in other overhead costs and finally adverse impact on the profitability of these small scale units.

10. **Managerial:** Managerial inadequacies pose another serious problem for small scale units. Modern business demands vision, knowledge, skill, aptitude and whole hearted devotion. Competence of the entrepreneur is vital for the success of any venture. An entrepreneur is a pivot around whom the entire enterprise revolves.

Many small scale units have turned sick due to lack of managerial competence on the part of entrepreneurs. An entrepreneur who is required to undergo training and counseling for developing his managerial skills will add to the problems of entrepreneurs.

Of course, increase in number of units, production, employment and exports of small- scale industries over the years are considered essential for the economic growth and development of the country. It is encouraging to mention that the small-scale enterprises accounts for 35% of the gross value of the output in the manufacturing sector, about 80% of the total industrial employment and about 40% of total export of the country.

#### **Question 4. What measures have the Government taken to solve the problem of finance and marketing in the small scale sector?**

**Answer:** Indian Government created two ministries to promote and develop small scale industries:

1. Ministry of Small Scale Industries. Ministry of Small Scale Industries designs policies, programmes and schemes to promote small scale industries. Small Industries Development



Organization (SIDO) is responsible for implementing and monitoring of various policies and programmes formulated by the ministry.

2. Ministry of Agro and Rural Industries is a nodal agency for coordination and development of village and khadi industries, tiny and micro enterprises in urban as well as rural areas. Its policies are implemented through Khadi and Village Industries Commission (KVIC), Handicrafts Board, Coir Board etc.

The small-scale sector has played a major role in employment generation, regional development and export promotion in India. The Government of India has realized that a lot more can be achieved if the two major bottlenecks that affect the further development of SSIs—inadequate funds and inefficient market penetration—are removed. In pursuit of this objective, the government has established the following agencies.

- **National Bank for Agriculture and Rural Development (NABARD):** It was established in 1982 with the main objective of promoting rural development and integrating the efforts in this direction. This agency is an apex banking body that governs the operations particularly of the rural and 'Gramm' banks. The main focus of NABARD is to provide cheap and easy credit facility to small, cottage and rural industries.
- **Small Industries Development Bank of India (SIDBI):** It was set up to provide direct and indirect financial assistance under different schemes. It caters to the credit and finance requirements of small-scale enterprises.
- **World Association for Small and Medium Enterprises (WASME):** It is an international non-governmental organisation that addresses the problems of small and medium-scale enterprises. It has set up an 'International Committee for Rural Industrialisation' with the aim of designing a model for the growth and development of rural industries.
- **The National Commission for Enterprises in the Unorganised Sector (NCEUS):** It was formed in September 2004 with the objective of improving the efficiency and enhancing the global competitiveness of small scale industries. It focuses on addressing the problems faced by small enterprises, particularly in the unorganised/informal sector.
- **Various Development and Employment Generation Programmes:** Besides establishing the organisations mentioned above, the government has launched various programmes for rural development. Among the important programmes are the Prime Minister's Rozgar Yojana (PMRY), Integrated Rural Development Programme (IRDP) and Training of Rural Youth for Self-Employment (TRYSEM). These programmes are aimed at generating greater employment opportunities, developing rural areas and making the rural people self-reliant.

#### **Question 5. What are the incentives provided by the government for industries in backward and hilly areas?**

**Answer:** It is quite lucrative and feasible for entrepreneurs to establish industries in metropolitan and other developed cities. However, because of numerous factors such as irregular power supply, poor transport and absence of banking facilities, it is extremely difficult for them to set up industries in backward, hilly and tribal areas. As a result, there exists acute regional disparities in development between these areas and the big cities in the country. The Government of India has been making efforts to remove the regional imbalances in development by providing incentives for setting up industries in rural areas. The following are among the incentives offered.

- **Land:** It is a basic requirement for setting up a business unit. In order to encourage the establishment of industries in backward areas, the government provides land plots at

concessional rates, especially to industrialists in backward regions. This makes setting-up industries cheaper.

- **Power:** Power is an essential requirement for the functioning of business enterprises. However, its supply is highly irregular in some parts of India. Therefore, in order to facilitate the setting up of industries in these areas, electricity is supplied at a discounted rate of 50 per cent. In addition, some states exempt such units from any payment during the initial years of operation.
- **Banking and finance:** Due to the poor banking facilities, industries set up in the backward areas face the problem of inadequate credit and finance. As a solution, the government provides loans at a concessional rate and offers subsidies of 10 to 15 per cent for the accumulation of capital assets.
- **Raw Materials:** Resources such as cement, iron and steel are of prime importance for industries. Since these resources are scarce, the government provides them on priority basis to industries located in backward areas.
- **Tax Exemption:** In order to attract entrepreneurs to set up industries in the backward areas, different state governments grant tax exemption to the industries. Thus, the industries are exempted from paying taxes for 5 to 10 years.

## MORE QUESTIONS SOLVED

### I. Very Short Answer Type Questions

**Question 1. Name any two institutions specially set up to promote small scale enterprises.**

**Answer:** SIDBI and SIDO

**Question 2. Give full form of SIDBI.**

**Answer:** Small Industries Development Bank of India

**Question 3. Give full form of NABARD.**

**Answer:** National Bank for Agriculture and Rural Development

**Question 4. Give one feature of Cottage Industries.**

**Answer:** These are rural-based industries owned and operated by individuals who invest their private resources in these units.

**Question 5. Give any two incentives offered by the Government to small scale industries.**

**Answer: (a) Land:** In order to encourage the establishment of industries in backward areas, the government provides land plots at concessional rates, especially to industrialists in backward regions.  
**(b) Power:** Power is an essential requirement for the functioning of business enterprises.

**Question 6. What is the investment limit for SSI?**

**Answer:** Rs. One crore (Rs 5 crore for specified 71 products)

**Question 7. Give any two problems faced by SSI.**

**Answer:** Obsolete technology and lack of marketing facilities

**Question 8. Discuss any two characteristics of SSI.**

**Answer:**

- They are run as sole proprietorship or partnership.
- Normally they use labour intensive methods.

**Question 9. Name the institution which was set up in 1982 to promote integrated rural development.**

**Answer:** National Bank for Agriculture and Rural Development

**Question 10. Name any two units included in SSI category.**

**Answer:** Export oriented units and Ancillary units

**Question 11. What is the role of National Small Industries Corporation for the growth of small business units in India?**

**Answer:** It promotes, provides aid and fosters the growth of small business units in the country. This focuses on the commercial aspects of these functions.

**Question 12. Name the apex bank set up to provide direct and indirect financial assistance to small scale sector.**

**Answer:** Small Industries Development Bank of India

**Question.13. What is the role of District Industries Centre for the growth of small business in India?**

**Answer.** District Industries Centers programme was launched on May 1, 1978 with a view to providing an integrated administrative framework at the district level which looks at the problem of industrialisation in the district.

**Question 14. How much do small industries in India account for the total industrial units?**

**Answer:** 95%

**Question 15. What is the parameter used by the government to identify service enterprise?**

**Answer:** An industry is a micro enterprise if investment in equipment does not exceed Rs 10 lakhs. An industry is a small enterprise if investment in equipment is more than Rs 10 lakhs but does not exceed Rs 2 crore. An industry is a medium enterprise if investment in equipment is more than Rs 2 crore but does not exceed Rs 5 crore.

## **II. Short Answer Type Questions**

**Question 1. Small business is business at small scale. Do you agree? Explain.**

**Answer:** Yes, I agree. Scale of operations can be measured in terms of workers employed, capital invested or total output. Indian Government considers the criterion of capital invested in plant and machinery. Accordingly a business in which investment in plant and machinery is less than 1 core comes under small scale business.

**Question 2. Write a short note on village and small industries sector.**

**Answer:** In India Village and small industries sector' consists of traditional as well as modern small industries. It has eight sub-groups Handlooms, Handicrafts, Coir, Sericulture, Khadi Industries, Village Industries, Small Scale Industries and Power looms. Small industries and power looms come in the category of modern industries and rest are included under traditional industries. Village and small industries together provide the largest employment opportunities in India.

### **Question 3. What is the purpose of NABARD?**

**Answer:** The main functions of NABARD pertain to policy development, coordination, research, training, etc., relating to rural credit. It provides refinance to cooperatives, regional rural banks, etc. Moreover it makes loans and advances to state governments for a period not exceeding more than 20 years to enable them to subscribe directly or indirectly to share the capital of cooperative credit societies.

It also promotes research in agriculture and rural development through its research and development fund. It undertakes inspection of co-operative banks and RRBs and advises the government on related matters. NABARD undertakes monitoring and evolution of the projects financed by it. The NABARD maintains two funds; The National Rural Credit Fund (long-term operations) and the National Rural Credit Fund (Stabilization).

The central and state governments contribute to the fund. The NABARD operates throughout the country through its 16 regional offices located in the capitals of all the major states and 3 sub offices, the paid-up capital of NABARD stood at Rs 2000 crore as on March 31, 2010. The profit after tax amounted to Rs 1558 crore during the year 2009-10 as against Rs 1390 crore during the year 2008-09.

NABARD had a paid-up share capital of Rs 100 crore, since this has been raised through stages to Rs 5,000 crore. The NABARD is empowered to borrow from central government.

It is also permitted to borrow foreign currency. It can also borrow long-term loans from any other authority or organisation or institution approved by the Board. It is empowered to issue bonds, debentures and other financial instruments.

### **Question 4. Explain the role of SIDBI in promoting small scale enterprises.**

**Answer:** Small Industries Development Bank of India (SIDBI). was set up on April 2, 1990 under an Act of Indian Parliament, is the principal financial institution for the promotion, financing and development of the Micro, Small and Medium Enterprise (MSME) sectors and for co-ordination of the functions of the institutions engaged in similar activities.

Financial support is provided by way of refinance to eligible Primary Lending Institutions (PLIs) such as banks, State Financial Corporations (SFCs), State Industrial Development Corporations (SIDCs), State Small Industries Development Corporations (SSIDCs) etc. for onward lending to MSMEs, financial assistance in the form of loans, grants, equity and quasi-equity to Non Government Organisations (NGOs) / Micro Finance Institutions (MFIs) for onlending to micro enterprises and economically weaker sections of society, enabling them to take up income generating activities on a sustainable basis and direct assistance to MSMEs which is channelised through the bank's network of 130 branch offices.

While finance is the basic need of the MSMEs, they also require different non-credit facilities to gain the extra mile in their endeavour to attain international competitiveness. Such requirements are equity capital, credit rating, technology transfer and upgradation, etc. SIDBI has been constantly working on building various institutional mechanisms to cater to the emerging needs of the MSME sector and has set-up various subsidiaries / associates viz.

SIDBI Venture Capital Ltd. (SVCL) is a subsidiary of SIDBI. It was set up in July, 1999. It is an asset management company, presently managing two venture capital funds. Credit Guarantee Fund Trust for Micro and Small Enterprises (CGFTMSE) in July 2000 by Government of India and SIDBI, to provide credit guarantee support to collateral free / third-party guarantee free loans extended by banks and lending institutions for micro and small enterprises (MSEs);

SME Rating Agency of India Ltd. (SMERA) was set up in September 2005, as an MSME dedicated third-party rating agency to provide comprehensive, transparent and reliable ratings and risk profiling.

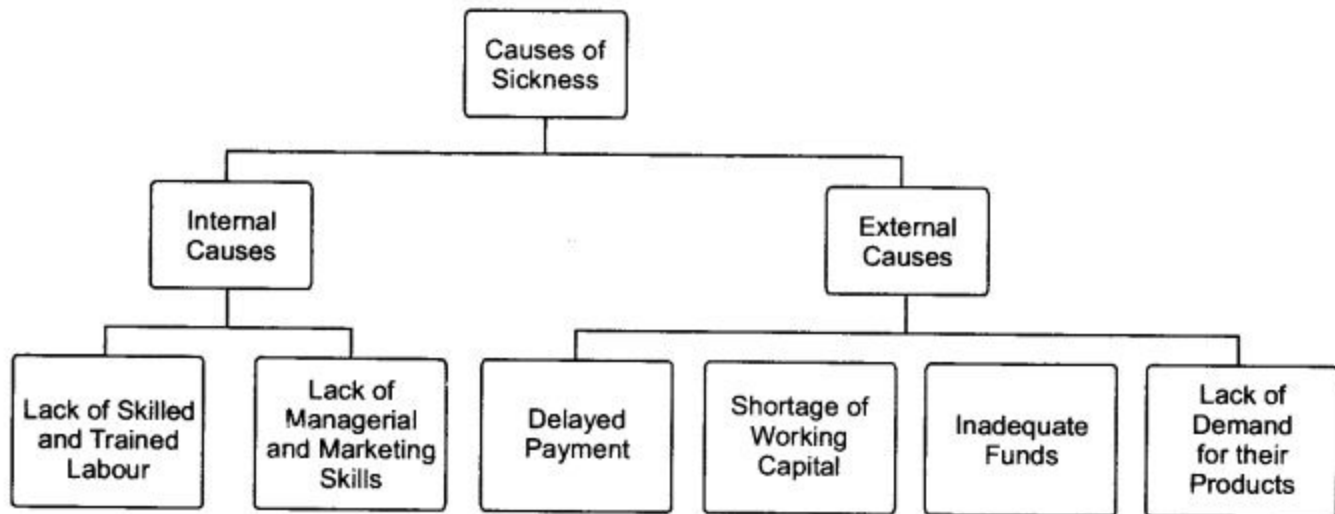
India SME Technology Services Limited (ISTSL), was set up in November 2005. It provides a platform for MSMEs to tap opportunities at the global level for acquisition of modern technologies.



India SME Asset Reconstruction Company Ltd (ISARC) is the country's first MSME focused asset reconstruction company striving for speedy resolution of non-performing assets (NPA) by unlocking the idle NPAs for productive purposes which would facilitate greater and easier flow of credit from the banking sector to the MSMEs

**Question 5. What are the causes of sickness in small industries?**

**Answer:** Causes of sickness in SSIs can be classified into internal as well as external categories.



**Question 6. What is the difference between small scale enterprise and cottage industry?**

**Answer:** “Small Scale Industries are located in urban centers and produce goods with partially or wholly mechanised equipment employing outside labour, small in size, having little capital resources and a small labour force”

“Cottage Industries are mainly rural in character and are generally associated with agriculture involving operations mostly by hands and are carried on in the home either as a whole time or as a part time occupation, primarily with the help of members of the family.”

Difference between the Small-Scale Industries and Cottage Industries:

The differences between the small scale and cottage industries are basically two:

- While small-scale industries are mainly located in urban centres as separate establishments, the cottage industries are generally associated with agriculture and provide subsidiary employment in rural areas.
- While small-scale industries produce goods with mechanised equipment employing outside labour, the cottage industries involve operations mostly by hand which are carried on primarily with the help of the members of the family.

**Question 7. Explain the areas where small businesses feel threatened from global competition.**

**Answer:** Given below are the areas where small businesses feel threatened from global competition:

- It is difficult to maintain quality standards, technological skills, financial credit worthiness, managerial and marketing capabilities of the large industries and MNCs.
- They have to face competition from giant sized MNCs along with medium and large scale enterprises. It brings cut throat competition for them.
- There is limited access to markets of developed countries because of stringent requirements of quality certification like ISO: 9000 etc.

**Question 8. Explain the meaning of small scale industry with its different categories.**

**Answer:** In Indian economy small-scale and cottage industries occupy an important place, because of their employment potential and their contribution to total industrial output and exports. Government of India has taken a number of steps to promote them. However, with the recent measures, small-scale and cottage industries facing both internal competition as well as external competition.

There is no clear distinction between small-scale and cottage industries. However it is generally believed that cottage industry is one which is carried on wholly or primarily with the help of the members of the family. As against this, small-scale industry employs hired labour.

Moreover industries are generally associated with agriculture and provide subsidiary employment in rural areas. As against this, small scale units are mainly located in urban areas as separate establishments.

**Definition:** Small scale industry is defined as a unit in which investment in original value of plant and machinery should not exceed Rs 1.5 crore.

However, to facilitate technology upgradation and enhance competitiveness, the investment limit has been raised to Rs 5 crore in respect of 71 high tech export oriented items in drugs, pharmaceuticals, hand-tools and knitwear sectors, etc.

**Different categories include:**

- Micro and tiny industries
- Women enterprises
- Cottage industries
- Village industries

**Question 9. List out major industry groups in the small sector in India.**

**Answer:** The official definitions of the small scale unit are as follows:

**1. Small-Scale Industries:**

These are the industrial undertakings having fixed investment in plant and machinery, whether held on ownership basis or lease basis or hire purchase basis not exceeding Rs 1 crore.

**2. Ancillary Industries:**

These are industrial undertakings having fixed investment in plant and machinery not exceeding Rs 1 crore engaged in or proposed to engage in,

- (a) The manufacture of parts, components, sub-assemblies, tooling or intermediaries, or
- (b) The rendering of services supplying 30 per cent of their production or services as the case may be, to other units for production of other articles.

**3. Tiny Units:**

These refer to undertakings having fixed investment in plant and machinery not exceeding Rs 23 lakhs. These also include undertakings providing services such as laundry, xeroxing, repairs and maintenance of customer equipment and machinery, hatching and poultry etc. located in towns with population less than 50,000

**4. Small-Scale Service Establishments:**

These mean enterprises engaged in personal or household services in rural areas and town with population not exceeding 50000 and having fixed investment in plant and machinery not exceeding Rs 25 lakhs.

**5. Household Industries:**

These cover artisans, skilled craftsman and technicians who can work in their own houses if their work requires less than 300 square feet space, less than 1 Kw power, less than 5 workers and no pollution is caused. Handicrafts, toys, dolls, small plastic and paper products, electronic and electrical gadgets are some of the examples of these industries.

**Question 10. State the objectives of small business in rural India.**

**Answer:** The objectives of small scale industries are follows:

1. To create more employment opportunities with less investment.
2. To remove economic backwardness of rural and less developed regions of the economy.
3. To reduce regional imbalances.
4. To mobilize and ensure optimum utilization of unexploited resources of the country.
5. To improve standard of living of people.
6. To ensure equitable distribution of income and wealth.
7. To solve unemployment problem.
8. To attain self-reliance.
9. To adopt latest technology aimed at producing better quality products at lower costs.

**Question 11. What are the measures taken by the Government to solve the problem of finance in the small scale sector?**

**Answer:** Following Measures have been taken by the government to solve the problem of finance in small scale sector:

1. **Small Industries Development Bank of India (SIDBI):** It was set up on April 2, 1990 under an Act of Indian Parliament, is the principal financial institution for the promotion, financing and development of the Micro, Small and Medium Enterprise (MSME) sector and for coordination of the functions of the institutions engaged in similar activities. Financial support is provided by way of refinance to eligible Primary Lending Institutions (PLIs) such as banks, State Financial Corporations (SFCs), State Industrial Development Corporations (SIDCs), State Small Industries Development Corporations (SSIDCs) etc. for onward lending to MSMEs, financial assistance in the form of loans, grants, equity and quasi-equity to Non Government Organisations/ Micro Finance Institutions (MFIs) for on-lending to micro enterprises and economically weaker sections of society, enabling them to take up income generating activities on a sustainable basis and direct assistance to MSMEs which is channelised through the bank's network of 130 branch offices.
2. **The National Commission for Enterprises in the Unorganised Sector (NCEUS):** It was established by the Government of India as an advisory body on the informal sector to bring about improvement in the productivity of informal enterprises for generation of large scale employment opportunities on a sustainable basis, particularly in the rural areas. The Commission was mandated to recommend appropriate measures to enhance the competitiveness of the informal sector in the global economy and to link the sector with the institutional framework in areas such as credit, raw material, infrastructure, technology upgradation skill development, and marketing.

**Question 12. Write a short note on WASME.**

**Answer:** World Association for Small and Medium Enterprises (WASME) is a global non-governmental organization head quartered at Noida, India. It has been spearheading the cause and development of Small and Medium Enterprises (SMEs) world over since its inception in 1980. It has emerged, over the years, as one of the most representative, effective and leading international organizations, working towards the promotion of SMEs. The vision behind establishment of WASME was to build a world private community of small business, their supporting and financial institutions as a non-governmental organization, not influenced by any government(s). WASME has members, associates and network partners in different countries across the world. It enjoys consultative/observer status with concerned agencies in UN system such as ECOSOC, UNCTAD,

WIPO, UNIDO, UNICITRAL, UNESCAP, ITC and ILO. It also cooperates actively with several intergovernmental and international organizations such as WCO, OECD, ICSB, APCTT, etc.

**Question 13. Write a short note on SIDO.**

**Answer:** It is the office of the Development Commissioner for Small Scale Industries. SIDO was established in 1954 on the basis of the recommendations of the Ford Foundation. It has over 60 offices and 21 autonomous bodies under its management. These autonomous bodies include Tool Rooms, Training Institutions and Project-cum-Process Development Centres.

**Various services provided by SIDO to the SMEs:**

1. Facilities for testing, toolmenting, training for entrepreneurship development.
2. Preparation of project and product profiles.
3. Technical and managerial consultancy.
4. Assistance for exports.
5. Pollution and energy audits.

SIDO also provides economic information services and advises Government in policy formulation for the promotion and development of SSIs. The field offices also work as effective links between the central and the state governments.

**Question 14. What forms of support is offered to small industries by the government?**

**Answer:** Government offers support to small industries in the following forms:

- Institutional support in respect of credit facilities;
- Provision of developed sites for construction of sheds;
- Supply of machinery on hire purchase system;
- Technical and financial help for technical upgradation;
- Special incentives for setting up of industries in backward areas;
- Provision for training facilities;
- Assistance for domestic and export marketing.

**III. Long Answer Type Questions**

**Question 1. What do you mean by small business? Describe the feature of small scale enterprise.**

**Answer:** plant and machinery should not exceed Rs 1.5 crore. However, to facilitate technology upgradation and enhance competitiveness, the investment limit has been raised to Rs 5 crore in respect of 71 high tech export oriented items in drugs, pharmaceuticals, hand-tools and knitwear sectors, etc. Characteristics of Small-Scale Industries:

1. **Ownership:** Ownership of small scale unit is with one individual in sole- proprietorship or it can be with a few individuals in partnership.
2. **Management and Control:** A small-scale unit is normally a one man show and even in case of partnership the activities are mainly carried out by the active partner and the rest are generally sleeping partners. These units are managed in a personalized fashion. The owner is actively involved in all the decisions concerning business.
3. **Area of Operation:** The area of operation of small units is generally localised catering to the local or regional demand. The overall resources at the disposal of small scale units are limited and as a result of this, it is forced to confine its activities to the local level.



4. **Technology:** Small industries are fairly labour intensive with comparatively smaller capital investment than the larger units. Therefore, these units are more suited for economies where capital is scarce and there is abundant supply of labour.
5. **Gestation Period:** Gestation period is that period after which teething problems are over and return on investment starts. Gestation period of small scale unit is less as compared to large scale unit.
6. **Flexibility:** Small scale units as compared to large scale units are more change susceptible and highly reactive and responsive to socio-economic conditions.  
They are more flexible to adopt changes like new method of production, introduction of new products etc.
7. **Resources:** Small scale units use local or indigenous resources and as such can be located anywhere subject to the availability of these resources like labour and raw materials.
8. **Dispersal of Units:** Small scale units use local resources and can be dispersed over a wide territory. The development of small scale units in rural and backward areas promotes more balanced regional development and can prevent the influx of job seekers from rural areas to cities.

**Question 2. Describe briefly the problems of small scale enterprises.**

**Answer:** Small scale industries in India could not progress satisfactorily due to various problems that they are confronted with while running enterprises. In spite of having huge potentialities, the major problems, small industries face are given below.

1. **Problem of skilled manpower:** The success of a small enterprise revolves around the entrepreneur and its employees, provided the employees are skilled and efficient. Because inefficient human factor and unskilled manpower create innumerable problems for the survival of small industries. Non-availability of adequate skilled manpower in the rural sector poses problem to small-scale industries.
2. **Inadequate Credit Assistance:** Adequate and timely supply of credit facilities is an important problem faced by small-scale industries. This is partly due to scarcity of capital and partly due to weak creditworthiness of the small units in the country.
3. **Irregular Supply of Raw Material:** Small units face severe problems in procuring the raw materials whether they use locally available raw materials or imported raw materials. The problems arise due to faulty and irregular supply of raw materials. Non-availability of sufficient quantity of raw materials, sometimes poor quality of raw materials, increased cost of raw materials, foreign exchange crisis and above all lack of knowledge of entrepreneurs regarding government policy are other few hindrances for small-scale sector.
4. **Absence of Organized Marketing:** Another important problem faced by small-scale units is the absence of organized marketing system. In the absence of organized marketing, their products compare unfavourably with the quality of the product of large-scale units. They also fail to get adequate information about consumer's choice, taste and preferences of the type of product. The above problems do not allow them to stay in the market.
5. **Lack of Machinery and Equipment:** Small-scale units are striving hard to employ modern machineries and equipment in their process of production in order to compete with large industries. Most of the small units employ outdated and traditional technology and equipment. Lack of appropriate technology and equipment create a major stumbling block for the growth of small-scale industries.
6. **Absence of Adequate Infrastructure:** Indian economy is characterized by inadequate infrastructure which is a major problem for small units to grow. Most of the small units and industrial estates found in towns and cities are having one or more problems like lack of power supply, water and drainage problem, poor roads, raw materials and marketing problem.

Thus absence of adequate infrastructure adversely affects the quality, quantity and production schedule of the enterprises which ultimately results in under-utilization of capacity.

7. **Competition from Large-scale Units and Imported Articles:** Small-scale units find it very difficult to compete with the product of large-scale units and imported articles which are comparatively very cheap and of better quality than small units product.
8. **Other Problems:** Besides the above problems, small-scale units have been constrained by a number of other problems also. They include poor project planning, managerial inadequacies, old and orthodox designs, high degree of obsolescence and huge number of bogus concerns. Due to all these problems the development of small- scale industries could not reach a prestigious stage.

### **Question 3. What incentives have been taken by government to promote small scale industries?**

**Answer:** Many incentives are provided both by the central and state governments to promote the growth of small-scale industries and also to protect them from the onslaught of the large-scale sector. Among the various incentives given to small-scale industries the following deserve special mention:

1. **Reservation:** To protect the small-scale industries from the competition posed by large-scale industries, the Government has reserved the production of certain items exclusively for the small-scale sector. The number of items exclusively reserved for the small-scale sector has been considerably increased during the Five Year Plan Periods and now stands at 822. However, prior to the 1997-98 budget the number of items reserved for the small- scale sector stood at 836. The Finance Minister dereserved 14 items in the 1997-98 budget.
2. **Preference in Government Purchases:** The government as well as government Organizations shows preference in procuring their requirements from the small- scale sector. For instance, the Director General of Supplies and Disposals purchases 400 items exclusively from the small-scale sector. The National Small-Scale Industries Corporation assists the SSI units in obtaining a greater share of government and defense purchases.
3. **Price Preference:** The SSI units are given price preference up to a maximum of 15 per cent in respect of certain items purchased both from small-scale and large- scale units.
4. **Supply of Raw Materials:** In order to ensure regular supply of raw materials, imported components and equipment's, the Government gives priority allocation to the small-scale sector as compared to the large-scale sector. Further, the Government has liberalised the import policy and streamlined the distribution of scarce raw materials.
5. **Excise Duty:** In respect of SSI units excise duty concessions are granted to both registered and unregistered units on a graded scale depending upon their production value. Full exemption is granted up to a production value of Rs 30 lakhs in a year and 75 % of normal duty is levied for production value exceeding Rs 30 lakhs but not exceeding Rs 75 lakhs. If the production value exceeds Rs 75 lakhs, normal rate of duty will be levied. ‘
6. **RBI's Credit Guarantee Scheme:** In 1960, the RBI introduced a Credit Guarantee Scheme for small-scale industries. As per the scheme, the RBI takes upon itself the role of a guarantee organisation for the advances which are left unpaid, including interest overdue and recoverable charges. This scheme covers not only working capital but also advances provided for the creation of fixed capital.
7. **Financial Assistance:** Small-scale industries are brought under the priority sector. As a result, financial assistance is provided to SSI units at concessional terms by commercial banks and other financial institutions. With a view to providing more financial assistance to the small scale sector, several schemes have been introduced in the recent past. The Small Industries Development Fund (SIDF) in 1986, National Equity Fund (NEF) in 1987 and the Single Window Scheme (SWS) in 1988.

SIDF provides refinance assistance to small scale and cottage and village industries and the tiny sector in rural areas. NEF provides equity type support to small entrepreneurs for setting up new projects in the tiny/small-scale sector. In 1996, the small-scale sector received 42.3 per cent of the total priority sector advances from public sector banks.

8. **Technical Consultancy Services:** The Small Industries Development Organisation, through its network of service and branch institutes, provides technical consultancy services to SSI units. In order to provide the necessary technical input to rural industries, a Council for Advancement of Rural Technology was set up in October, 1982. The Technical Consultancy Organisation renders consultancy services to SSI units at a subsidised rate. Many financial institutions are also providing subsidies to SSI units for availing of consultancy services. For instance, small entrepreneurs proposing to set up rural, cottage, tiny or small-scale units, can get consultancy services at a low cost from the Technical Consultancy Organizations approved by the All-India and State-level financial institutions. They have to pay only 20% of the fees charged by a Technical Consultancy Organisation. The entire balance of 80% or Rs 5, 000 whichever is lower is subsidized by the Industrial Finance Corporation of India.
9. **Machinery on Hire Purchase Basis:** The National Small Industries Corporation (NSIC) arranges supply of machinery on hire purchase basis to SSI units, including ancillaries located in backward areas which qualify for investment subsidy. The rate of interest charged in respect of technically qualified persons and entrepreneurs coming from backward areas are less than the amount charged to others. The earnest money payable by technically qualified persons and entrepreneurs from backward areas is 10% as against 15% in other cases.
10. **Transport Subsidy:** The Transport Subsidy Scheme, 1971 envisages grant of a transport subsidy to small-scale units in selected areas to the extent of 75 % of the transport cost of raw materials which are brought into and finished goods which are taken out of the selected areas.
11. **Training Facilities:** The Entrepreneurship Development Institute of India, Financial Institutions, Commercial banks, Technical Consultancy organizations, and NSIC provide training to existing and potential entrepreneurs.
12. **Marketing Assistance:** The National Small Industries Corporation (NSIC), the Small Industries Development Organisation (SIDO) and the various Export Promotion Councils help SSI units in marketing their products in the domestic as well as foreign markets. The SIDO conducts training programmes on export marketing and organises meetings and seminars on export promotion.
13. **District Industries Centers (DICs):** The 1977 Industrial Policy Statement introduced the concept of DICs. Accordingly a DIC is set up in each district. The DIC provides and arranges a package of assistance and facilities for credit guidance, supply of raw materials, marketing etc.

#### **Question 4. Describe the scope of small business in India.**

**Answer:** In most of the developing countries like India, Small Scale Industries (SSI) constitute an important and crucial segment of the industrial sector. They play an important role in employment creation, resource utilisation and income generation and helping to promote changes in a gradual and phased manner. They have been given an important place in the framework of Indian planning since beginning both for economic and ideological reasons. The reasons are obvious.

The scarcity of capital in India severely limits the number of non-farm jobs that can be created because investment costs per job are high in large and medium industries. An effective development policy has to attempt to increase the use of labour, relative to capital to the extent that it is economically efficient.

Small Scale Enterprises are generally more labour intensive than larger organisations. As a matter of fact, small scale sector has now emerged as a dynamic and vibrant sector for the Indian economy in recent years. It has attracted so much attention not only from industrial planners and economists but

also from sociologists, administrators and politicians.

### **Scope of Small Scale Industry:**

Defining small scale industry is a difficult task because the definition of small scale industry varies from country to country and from one time to the another in the same country depending upon the pattern and stage of development, government policy and administrative set up of the particular country.

Every country has set its own parameters in defining small scale sector. Generally, small scale sector is defined in terms of investment ceilings on the original value of the installed plant and machinery. But in the earlier times the definition was based on employment. In the Indian context, the parameter are as follows.

The Fiscal Commission, Government of India, New Delhi, 1950, for the first time defined a small-scale industry as, one which is operated mainly with hired labour usually 10 to 50 hands.

Fixed capital investment in a unit has also been adopted as the other criteria to make a distinction between small scale and large-scale industries. This limit is being continuously raised upwards by Government.

The Small Scale Industries Board in 1955 defined, "Small-scale industry as a unit employing less than 50 employees if using power and less than 100 employees if not using power and with a capital asset not exceeding Rs 5 lakhs".

The initial capital investment of Rs 5 lakhs has been changed to Rs 10 lakhs for small industries and Rs 15 lakhs for ancillaries in 1975. Again this fixed capital investment limit was raised to Rs 15 lakhs for small units and Rs 20 lakhs for ancillary units in 1980. The Government of India in 1985, has further increased the investment limit to Rs 35 lakhs for small-scale units and 45 lakhs for ancillary units.

Again the new Industrial Policy in 1991, raised the investment ceilings in plant an machinery to ? 60 lakhs for small-scale units and Rs 75 lakhs for ancillary units.

As per the Abid Hussain Committee's recommendations on small scale industry, the Government of India has, in March 1997 further raised investment ceilings to Rs 3 crores for small-scale and ancillary industries and to Rs 50 lakhs for tiny industry. The new policy initiatives in 1999-2000 defined small-scale industry as a unit engaged in manufacturing, repairing, processing and preservation of goods having investment in plant and machinery at an original cost not exceeding Rs 100 lakhs.

In case of tiny units, the cost limitation is up to Rs 5 lakhs. Again, the Government of India in its budget for 2007-08 has raised the investment limit in plant and machinery of small-scale industries to Rs 1.5 crores. An ancillary unit is one which is engaged or proposed to be engaged in the manufacture of production of parts, components, sub-assemblies, tooling or intermediaries or rendering services and the undertaking supplies or renders or proposes to supply or render not less than 50% of its production or services, as the case may be, to one or more other industries undertakings and whose investment in fixed assets in plant and machinery whether held on ownership terms or lease or on hire purchase does not exceed Rs 75 lakhs.

For small-scale industries, the Planning Commission of India uses terms 'village and small scale industries'. These include modern small-scale industry and the traditional cottage and household industry.

### **Question 5. Highlight the role of the small business in promoting economic growth and solving other socio-economic problems.**

**Answer:** In a developing country like India, the role and importance of small-scale industries is very significant towards poverty eradication, employment generation, rural development and creating regional balance in promotion and growth of various development activities.

It is estimated that this sector has been contributing about 40% of the gross value of output produced in the manufacturing sector and the generation of employment by the small scale sector is more than five times to that of the large-scale sector.



This clearly shows the importance of small-scale industries in the economic development of the country. The small-scale industry has been playing an important role in the growth process of Indian economy since independence in spite of stiff competition from the large sector and not very encouraging support from the government.

The following are some of the important role played by small scale industries in India.

1. **Employment Generation:** The basic problem that is confronting the Indian economy is increasing pressure of population on the land and the need to create massive employment opportunities. This problem is solved to larger extent by small-scale industries because small scale industries are labour intensive in character. They generate huge number of employment opportunities. Employment generation by this sector has shown a phenomenal growth. It is a powerful tool of job creation.
2. **Mobilisation of resources and entrepreneurial skill:** Small-scale industries can mobilize a good amount of savings and entrepreneurial skill from rural and semi-urban areas remain untouched from the clutches of large industries and put them into productive use by investing in small-scale units. Small entrepreneurs also improve social welfare of a country by harnessing dormant, previously overlooked talent. Thus, a huge amount of latent resources are being mobilised by the small-scale sector for the development of the economy.
3. **Equitable distribution of income:** Small entrepreneurs stimulate a redistribution of wealth, income and political power within societies in ways that are economically positive and without being politically disruptive. Thus small-scale industries ensure equitable distribution of income and wealth in the Indian society which is largely characterised by more concentration of income and wealth in the organised section keeping unorganised sector undeveloped. This is mainly due to the fact that small industries are widespread as compared to large industries and are having large employment potential.
4. **Regional dispersal of industries:** There has been massive concentration of industries in a few large cities of different states of Indian union. People migrate from rural and semi-urban areas to these highly developed centres in search of employment and sometimes to earn a better living which ultimately leads to many evil consequences of over-crowding, pollution, creation of slums, etc. This problem of Indian economy is better solved by small scale industries which utilize local resources and brings about dispersion of industries in the various parts of the country thus promotes balanced regional development.
5. **Provides opportunities for development of technology:** Small scale industries have tremendous capacity to generate or absorb innovations. They provide ample opportunities for the development of technology and technology in return, creates an environment conducive to the development of small units. The entrepreneurs of small units play a strategic role in commercializing new inventions and products. It also facilitates the transfer of technology from one to the other. As a result, the economy reaps the benefit of improved technology.
6. **Indigenization:** Small scale industries make better use of indigenous organizational and management capabilities by drawing on a pool of entrepreneurial talent that is limited in the early stages of economic development. They provide productive outlets for the enterprising independent people. They also provide a seed bed for entrepreneurial talent and a testing round for new ventures.
7. **Promotes exports:** Small scale industries have registered a phenomenal growth in export over the years. The value of exports of products of small-scale industries has increased to Rs 393 crores in 1973-74 to Rs 71, 244 crores in 2002-03. This contributes about 35% India's total export. Thus they help in increasing the country's foreign exchange reserves thereby reducing the pressure on country's balance of payment.

8. **Supports the growth of large industries:** The small scale industries play an important role in assisting bigger industries and projects so that the planned activity of development work is timely attended. They support the growth of large industries by providing components, accessories and semi finished goods required by them. In fact, small industries can breathe vitality into the life of large industries.
9. **Better industrial relations:** Better industrial relations between the employer and employees helps in increasing the efficiency of employees and reducing the frequency of industrial disputes. The loss of production and man days are comparatively less in small- scale industries. There is hardly any strikes and lock out in these industries due to good employee-employer relationship.

**Question 6. Explain the importance of SSI in overall development of an economy. Also discuss hurdles in its route.**

**Answer: Role of small scale industries:**

1. Contribution in industrial production;
2. Employment creation;
3. Contribution to export;
4. The same distribution of income and prosperity.

**Hurdles it faces:**

Small scale industries in India can't progress satisfactorily due to various problems likely confronted with while operating enterprises. In spite of needing huge potentialities, the major problems, small industries face are given below.

1. **Problem associated with Skilled Manpower:** The success of your small enterprise revolves about the entrepreneur and its personnel, provided the employees tend to be skilled and efficient. Because inefficient human element and unskilled manpower create innumerable problems for your survival of small companies. Non-availability of adequate skilled manpower in the rural sector poses trouble to small scale industries.
2. **Inadequate Credit Assistance:** Adequate and timely supply of credit facilities is an important problem faced by small-scale companies. This is partly because of scarcity of capital and partly because of weak credit worthiness of the small units near you.
3. **Irregular Supply Associated with Raw Material:** Small units face severe problems in procuring the recyclables whether they use locally available recyclables or imported raw products. The problems arise because of faulty and irregular supply of raw materials. Non-availability of Sufficient variety of raw materials, sometimes poor quality of raw materials, increased cost of recyclables, foreign exchange crisis and most importantly lack of knowledge associated with entrepreneurs regarding Government insurance policy are other few hindrances regarding small-scale sector.
4. **Trouble of Marketing:** Another important problem confronted by small-scale units may be the absence of organized marketing system. Due to lack of organized marketing, their products compare unfavorably with the grade of the product of large- level units. They are also not able to get adequate information with regards to consumer's choice, taste and preferences of the kind of product. The above problems do not let them to stay out there.
5. **Lack of Equipment:** Small-scale units are striving hard to use modem machines and equipment in their process of production so that you can compete with large companies. Most of the little units employ outdated and also traditional technology and products. Lack of appropriate technology and equipment create a major stumbling block for your growth of small-scale companies.

6. **Absence of Ample Infrastructure:** Indian economy is seen as an inadequate infrastructure which is a major problem for small units growing. Most of the little units and industrial estates found in towns and cities are having a number of problems like lack of power supply, water and drainage trouble, poor roads, raw products and marketing problem.

Thus lack of adequate infrastructure adversely affects the product quality, quantity and production schedule in the enterprises which ultimately ends up with under-utilization of capacity.

7. **Rivalry from Large Scale Units and also Imported Articles:** Small-scale units still find it very difficult to contend with the product of large-scale units and imported articles that are comparatively very cheap and also of better quality compared to small units product.

**Question 7. Name the institutions and banks set up to promote small scale industries in rural, backward and hilly areas. Explain their objectives.**

**Answer:** Small Scale Industry (SSI) is an industrial undertaking in which the investment in fixed assets in plant and machinery, whether held on ownership term or on lease or hire purchase, does not exceed Rs 1 crore. However, this investment limit is varied by the Government from time to time. Entrepreneurs in small scale sector are normally not required to obtain a license either from the Central Government or the State Government for setting up units in any part of the country. Registration of a small scale unit is also not compulsory. But its registration with the State Directorate or Commissioner of Industries or DIC's makes the unit eligible for availing different types of Government assistance like financial assistance from the Department of Industries, medium and long term loans from State Financial Corporations and other Commercial Banks, machinery on hire-purchase basis from the National Small Industries Corporation, etc. Registration is also an essential requirement for getting benefits of special schemes for promotion of SSI viz. Credit Guarantee Scheme, Capital subsidy, Reduced custom duty on selected items, ISO-9000 Certification reimbursement and several other benefits provided by the state government.

1. The Ministry of Micro, Small and Medium Enterprises acts as the nodal agency for growth and development of SSIs in the country. The ministry formulates and implements policies and programmes in order to promote small scale industries and enhance their competitiveness. It is assisted by various public sector enterprises like:-
  - (a) Small Industry Development Organisation (SIDO) is the apex body for assisting the Government in formulating and overseeing the implementation of its policies and programmes/projects/schemes.
  - (b) National Small Industries Corporation Ltd (NSIC) was established by the Government with a view to promoting, aiding and fostering the growth of SSI in the country, with focus on commercial aspects of their operation.
  - (c) The Ministry has established three National Entrepreneurship Development Institutes which are engaged in development of training modules, undertaking research and training and providing consultancy services for entrepreneurship development in the SSI sector. These are
    - (i) National Institute of Small Industry Extension Training (NISIET) at Hyderabad, National Institute of Entrepreneurship and Small Business Development (NIESBUD) at NOIDA.
    - (ii) Indian Institute of Entrepreneurship (HE) at Guwahati.
2. The National Commission for Enterprises in the Unorganised Sector (NCEUS) has been constituted with the mandate to examine the problems of enterprises in the unorganised sector and suggest measures to overcome them.
3. Small Industries Development Bank of India (SIDBI) acts as apex institution for financing SSIs through various credit schemes.

#### IV. Higher Order Thinking Skills (HOTS)

**Question 1. “The path of small scale industries is full of hurdles”. Discuss.**

**Answer:** Yes, it is absolutely correct to say that path of SSI is full of hurdles. The following are the major problems faced by Small Scale Industries (SSIs) in India.

- **Inadequate Finance and Credit:** The SSIs have always faced the problem of inadequate finance and credit. This is partly because of the scarcity of capital available with the entrepreneurs in the sector and partly because of their lack of assets for offering as collateral/mortgage to secure bank loans. As a result, these businesses have to rely on local financial resources and moneylenders' for funds.
- **Problem of Procuring Raw Materials:** Due to inadequate finance and credit, SSIs face a shortage of funds for procuring raw materials and for carrying out their day- to-day business activities. In addition, the poor transportation system and the faulty supply mechanism often result in irregular supply of raw materials. For these reasons, SSIs face a severe shortage of raw materials, which hinders their smooth functioning.
- **Lack of Skilled Labour:** As SSIs cannot afford to pay high salaries to their employees, they usually employ semi-skilled or unskilled labourers. Hence, they face lack of skilled and talented manpower, which adversely affects their efficiency.
- **Marketing:** Efficient systems for marketing and promoting products have remained an unfulfilled dream of small scale industries. The main reason is the shortage of funds. Because of the lack of efficient marketing systems, small units are forced to sell their products in the markets through the middlemen, which further leads to the exploitation of the small scale entrepreneurs.
- **Obsolete/outdated technology:** Many small-scale industries use production techniques which are outdated and obsolete. This lowers their productivity and makes their operations unfeasible.

**Question.2. What are the marketing problems faced by Small Scale Industries?**

**Answer:** Small scale units are exposed to numerous problems. Major problems faced by these units are concerned with raw-material, labour, finance and marketing. Problem of marketing is more complicated in case of small scale industries. These units are in no position to face the onslaught of large scale limits i.e., quantity, quality and cost and at the same time are not in a position to assess the prevailing market scenario (or) changes which are taking place with respect to tastes, liking, disliking, competition, technology etc. Moreover these units do not possess the requisite expertise to adjust their operations according to the changed situation.

- **Problem of Standardization:** Small scale units face problems with respect to fixing the standards and sticking. This results in the poor quality of their products and it adversely affects their image (or) goodwill in the market.
- **Competition from Large Scale Units:** Small scale units are ill equipped to face competition from large scale units' with respect to quantity, quality and cost. In the modern competitive world there is survival of the fittest, even the existence of small scale units is endangered.
- **Poor Sale Promotion:** Small scale units have limited financial resources and hence, cannot afford to spend more on sales promotion. These units are not having any standard brand name under which they can sell their products. Various channel members try to exploit them because of the lack of goodwill of their products in the market.
- **Poor Bargaining Power:** Due to limited resources and lower scale of operations small scale units are in a weak position while negotiating with the suppliers of raw- material, finances (or)



marketing agencies. They are always at the receiving end and as such are not in a position to safeguard their interests.

**Question 3. Explain the future of small scale enterprises in the light of policy of LPG.**

**Answer:** Present time is the time of WTO. India is a founder member of WTO. Therefore, it is bound to open its economy for the global producers. As new giant scale MNCs enters the market, it becomes must for them to steadily re-orient themselves to face the challenges coming from increased competition. Certainly competition will increase for them. In these situations the mantra of success will be “Think global and act local”.

- They need to bring dynamism, flexibility, innovative entrepreneurial spirit, small businesses need to modify themselves as per the changing needs of market driven economy.
- Government also needs to change its role from a regulator to facilitator and promoter.
- New strategies have to be found to increase partnership between large and small industries.
- In order to maintain their market share and healthy growth, SSIs need to create a level playing field for themselves.
- They will be able to compete in this global scenario if they learn to manage, adopt and improve their competitive strength.

**V. Value Based Questions**

**Question 1. It is right on moral grounds to give some special incentives to small scale industries. Do you agree? Justify your answer.**

**Answer:** Yes, I agree. There are many problems with SSIs. Major problems faced by the small scale industries are : (1) Finance (2) Raw Material (3) Idle Capacity (4) Technology (5) Marketing (6) Infrastructure (7) Under Utilization of Capacity (8) Project Planning. Small scale industries play a vital role in the economic development of our country. This sector can stimulate economic activity and is entrusted with the responsibility of realizing various objectives, i.e., generation of more employment opportunities with less investment; reducing regional imbalances etc. Small scale industries are not in a position to play their role effectively due to various constraints. If government provides certain incentives in the form of incentives on land, power, tax holiday etc, it can grow well and can be able to compete with large scale enterprises.

**Question 2. We need to give special attention for the growth of rural, backward and hilly areas. Why?**

**Answer:** It is rightly said that we need to give special attention for the growth of rural, backward and hilly areas because:

- Large scale business houses are unwilling to invest in these areas. It leads to lack of employment opportunities in these areas.
- There is disguised and seasonal unemployment in rural areas. This type of unemployment can best be tackled by developing small scale and village industries.
- It is the duty of the government to ensure balanced development in all corners of the country.
- It can help to make these areas developed and bring them at par with other areas of the country.

# NCERT SOLUTIONS For Class 11 Business Studies

## <http://freehomedelivery.net/Solutions> Chapter 10

### Internal Trade

#### Class 11 Business Studies Solutions Chapter 10 Internal Trade

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#### I. Short Answer Type Questions

##### Question 1. What is meant by internal trade?

**Answer:** Internal trade refers to the buying and selling of goods and services within the domestic territory of a country. It is known as internal trade. In other words, the process of exchanging goods and services within the national boundaries of a country is called internal trade. Purchases of goods from a local shop, a mall or an exhibition are all examples of internal trade. The government does not levy customs or import duties on goods and services that are produced within the country for meeting the domestic demand.

Internal trade can be classified into the following two categories:

- **Retail Trade:** It refers to the buying and selling of goods in small quantities for final consumption.
- **Wholesale Trade:** It refers to the buying and selling of goods in bulk, i.e., the exchange of large quantities of goods meant for resale in local markets.

##### Question 2. Specify the characteristics of fixed shop retailers.

**Answer:** As the name suggests, fixed-shop retailers are retailers who have permanent establishments. It means that they sell goods and services from fixed shops and do not move from place to place to serve customers. For example, retailers functioning from fixed establishments in the local grocery market.

The following are some of the characteristics of fixed-shop retailers:

1. Fixed-shop retailers operate on a large scale and have huge resources at their disposal compared with itinerant traders. However, among fixed-shop retailers, there are retailers who operate on a small scale or a large scale.
2. They generally deal in more than one product—that is, their range of goods varies from consumer durable goods to non-durable goods.
3. Fixed-shop retailers provide services such as free home delivery and supply of goods on credit to their customers.
4. They have a greater credibility in the eyes of consumer as they can be traced if the product is found to be defective or there is any other problem.

##### Question 3. What purpose is served by wholesalers providing warehousing facilities?

**Answer:** Wholesalers purchase goods in bulk from manufacturers, store them and distribute them to retailers in small quantities for further resale. This bulk purchase of goods enables manufacturers to undertake production on a large scale without worrying about storage facilities. By offering warehouses close to the centres of distribution, wholesalers provide what is known as 'place utility'.

Wholesalers not only provide warehousing facilities such as collection, storage and protection of goods but also facilitate marketing and distribution, creating 'time utility'.

**Question 4. How does market information provided by wholesalers benefit the manufacturers?**

**Answer:** Wholesalers provide a variety of information to both manufacturers and customers. To manufacturers, they provide information about:

1. The tastes and preferences of customers
2. Conditions prevailing in the market
3. Level of competition in the market and
4. Types of goods and features demanded by consumers.

This information helps manufacturers to cater to the changing needs of consumers.

**Question 5. How do the wholesalers help the manufacturer in availing the economies of scale?**

**Answer:** Wholesalers often purchase goods in bulk quantities from manufacturers. Once a purchase is made, the wholesalers distribute the goods in small quantities to retailers for further resale. However, during this process, they provide manufacturers with a variety of warehousing facilities such as collection, storage, marketing and distribution of goods. These services reduce the burden on manufacturers by creating time and place utility, thus enabling them to produce goods on a large scale and benefit from the economies of scale.

**Question 6. Distinguish between single line stores and specialty stores. Can you identify such stores in your locality?**

**Answer:** Single-line stores are small shops that deal in only one product. For example, garments or shoes. However, single-line stores offer a wide variety of the product. For instance, a single-line store that deals in garments will have a wide variety of clothes in all sizes for men, women and children. On the other hand, specialty stores deal only in a particular type of product from a selected product line. For example, men's clothing. Such stores generally sell all the brands of the product in which they specialise. For instance, if a store specialises in men's clothing, then it will have all the brands of men's garments.

On the basis of these features, we can identify the different types of stores in a locality—whether they are single-line stores or specialty stores.

Single line stores are more frequently found in local retail markets while specialty stores are found in wholesale markets.

**Question 7. How would you differentiate between street traders and street shops?**

**Answer:**

Basis of difference	Street traders	Street shops
Definition	Small retailers who generally sell low-priced consumer items on streets.	Shops situated on street sides or main roads.
Shops/establishments	Do not have permanent shops.	Have permanent establishments.
Products	Bathroom items, eatables, newspapers, etc.	Clothes, shoes, grocery items, bakery items, etc.
Reliability	These are taken as less reliable by customers.	These are taken relatively more reliable by customers.

**Question 8. Explain the services offered by the wholesalers to the manufacturers.**

**Answer:** Wholesalers offer a wide variety of services to manufacturers. The following are examples of such services:

1. **They facilitate large-scale production:** Wholesalers purchase goods in bulk from manufacturers and sell them to retailers in small quantities for further resale. This bulk purchase made by wholesalers enables manufacturers to undertake production on a large scale without worrying about storage facilities. Thus, wholesalers facilitate large-scale production.
2. **They provide storage facilities:** When wholesalers purchase goods in bulk quantities from manufacturers, they store these goods in their god owns or warehouses, reducing manufacturers burden of finding proper storage .
3. **They collect market information:** Wholesalers provide different kinds of information to manufacturers, such as information about the tastes and preferences of customers, prevailing market conditions, level of competition in the market and type of goods demanded by consumers. This in turn helps manufacturers to produce goods according to the market needs.

**Question 9. What are the services offered by retailers to wholesalers and consumers?**

**Answer:** Retailers offer a variety of services to wholesalers and customers. Some of these services are listed below.

1. **They provide information to customers:** Retailers provide information to customers about the new products available in the market, their features, prices, etc. This information helps customers decide which product to buy.
2. **They provide information to wholesalers:** Retailers provide information to wholesalers, such as the tastes and preferences of customers, prevailing market conditions and level of competition in the market. Wholesalers pass on this information to manufacturers.
3. **They store a wide variety of goods:** Retailers generally store a wide variety of goods based on consumer tastes and preferences and thus allow customers to choose from the available range of products.
4. **They facilitate distribution of goods:** Retailers facilitate the distribution of goods to consumers for final consumption.
5. **They help in promotion of goods:** Since retailers are in direct touch with customers, they can promote the sale of goods through personal interaction. Thus, retailers help wholesalers and manufactures in promoting the sale of goods.



## II. Long Answer Type Questions

**Question 1. Itinerant traders have been an integral part of internal trade in India.**

**Analyse the reasons for their survival in spite of competition from large scale retailers.**

**Answer:** Itinerant traders are retailers who do not have a fixed place of operation. That is, they do not have a shop from where they sell their products. They are also known as mobile traders as they keep moving from place to place in order to sell their products. They are generally found on street sides, and they shift their place of operation in search of more customers. They usually sell low-priced and non-standard goods.

The reasons that itinerant traders survive in spite of the tough competition from large-scale retailers can be attributed to the following factors:

1. It is very easy to set up a small scale retail shop. One person with limited funds himself can start business. He need not associate other persons and no formalities are necessary.
2. A small scale retail shop can be located anywhere. It can provide goods of daily use near the place of consumers. They are not required to travel to big markets.
3. The small scale retailer knows his customers. He can attend to them personally and cater to their individual tastes and needs. Such personalised service is not available in large scale retail stores.
4. Small scale retailers cater to the masses that have limited income and can afford to buy small quantity. In India majority of the population is poor.
5. It is easy to manage and control a small sale retail shop. The owner himself is the manager. He has direct motivation to work hard and increase the efficiency of business. He takes personal interest in his business organisations.
6. Small amount of capital is required to start a small retail shop. People with small amount of funds can start retail business on a small scale.

**Question 2. Discuss the features of a departmental store. How are they different from multiple shops or chain stores?**

**Answer:** Departmental stores are basically large, fixed establishments that deal in a wide variety of products. The following points highlight the features of a departmental store:

1. **Central locations:** Department stores are generally located in central areas so as to attract a large number of customers.
2. **Defined hierarchy:** The management in departmental stores follows the same hierarchy that is generally followed in any joint stock company. That is, the top management consists of a board of directors, with the managing director, the general manager and the department managers under it in that order.
3. **Absence of middlemen:** Departmental stores purchase goods directly from manufacturers and sell them to customers. Thus, they eliminate the role of middlemen.
4. **Centralised purchase with decentralised sales:** In a departmental store, the purchases from manufacturers are handled by a single division that follows a centralised purchase policy. On the other hand, the sales are handled by the respective sections of the departmental store, which follow a decentralised policy for sales.

### Differences between Departmental stores and Multiple shops

Basis of difference	Departmental Stores	Multiple Shops
Variety of products	They offer a wide variety of products to customers.	They deal in a single line of product and specialise in it.
Customer services	They offer a wide variety of customer services.	They offer limited customer services.
Location	They are located in central parts of cities so as to attract a large number of customers.	They have multiple locations—that is, they are spread across cities or towns.
Pricing policy	They do not follow a fixed pricing policy as the prices of products vary across departments.	They follow a fixed pricing policy across all the shops that are part of a particular chain.
Cost of failure	They have a very high cost of failure because of the huge initial and operating expenses.	They have a limited cost of failure because the initial investment is not very large and the losses of one shop can be covered by the profits of others.

**Question 3. Why are consumer cooperative stores considered to be less expensive? What are its relative advantages over other large scale retailers?**

**Answer:** Consumer cooperative stores are formed by groups of consumers to provide goods at reasonable prices to members of consumer societies. In such societies, the role of middlemen is eliminated as these societies purchase goods from manufacturers or wholesalers directly and sell them to society members at reasonable rates. As consumer cooperative stores do not aim at profit making, the prices of goods offered by them are much lower than the prices of goods at retail shops. Compared with large-scale retailers, the capital requirement for starting a consumer cooperative society is very low. Thus, consumer cooperative stores do not require much investment, and the goods sold by them are priced lower.

The following are some advantages that consumer cooperative stores have over large-scale retailers:

1. **Democratic management:** Consumer cooperative stores are democratic organisations as they are managed and controlled by elected managing committees of consumer societies. The members of managing committees are elected by the members of consumer societies on the principle of 'one member, one vote'.
2. **Limited liability:** The liability of the members of consumer cooperative societies is limited to the amount of shares held by them. Thus, in case a society's liabilities increase beyond the assets, the members will not be liable to repay the debts using their personal assets.
3. **Low price of goods:** As the goods offered by consumer cooperatives are directly purchased from manufacturers and wholesalers, the role of middlemen is eliminated. Therefore, consumer societies are able to sell goods at lower prices.

**MORE QUESTIONS SOLVED**

## **I. Very Short Answer Type Questions**

### **Question 1. What do you mean by internal trade?**

**Answer:** Internal trade refers to the buying and selling of goods and services within the domestic territory of a country. In other words, the process of exchanging goods and services within the national boundaries of a country is called internal trade.

### **Question 2. Who are Itinerants?**

**Answer:** Itinerant traders are retailers who do not have a fixed place of operation. That is, they do not have a shop from where they sell their products. They are also known as mobile traders as they keep moving from place to place in order to sell their products.

### **Question 3. Name any two Itinerants.**

**Answer:** Hawkers and Peddlers

### **Question 4. Large quantity buying is characteristic of which trade?**

**Answer:** Wholesale trade

### **Question: 5. Goods with little defects are sold in which type of shops?**

**Answer:** Cheap jacks

### **Question 6. Used goods are bought and sold in which type of shops.**

**Answer:** Second hand goods shop

### **Question 7. Give any two services of retailer to the customers.**

**Answer:**

1. They provide regular availability of goods.
2. They provide information on new products.

### **Question 8. Give one example of chain stores.**

**Answer:** Food chains of Mcdonald, showrooms of DCM

### **Question 9. In which business are goods bought and sold through postal services?**

**Answer:** Mail Order Business

### **Question 10. Name the machine in which goods are bought and sold by inserting coins.**

**Answer:** Automatic Vending Machines

### **Question 11. Give the full form of FICCI.**

**Answer:** The Federation of Indian Chambers of Commerce and Industry

### **Question 12. What type of goods are suitable for Automatic vending machines?**

**Answer:** Pre-packed brands of low priced products, hot beverages, milk, chocolates, newspaper, platform ticket

### **Question 13. What is meant by Automatic vending machines?**

**Answer:** Automatic vending machines are coin operated vending machines which work like an ATM. It is useful in selling hot beverages, milk, chocolates, newspaper, platform ticket etc.

**Question 14. Name the retail outlets that sell merchandise through mail.**

**Answer:** Telebrands

**Question.15. Name any two departmental stores.**

**Answer.** Akberally in Mumbai and Spencers in Chennai

**Question 16. Name the retail organization where same types of commodities are sold at uniform prices located all over the country.**

**Answer:** Chain Stores

## **II. Short Answer Type Questions**

**Question 1. Enumerate the features of retail trade.**

**Answer:** A retailer is a business enterprise that is engaged in the sale of goods and services directly to the ultimate consumers. It has following features:

1. A retailer is the intermediary between wholesaler and the ultimate consumer. He is the last link in the chain of distribution.
2. A retailer buys goods from wholesalers and sells them in small quantities to ultimate consumers.
3. He maintains personal contact with his customers.
4. Generally, a retailer deals in a wide variety of goods.
5. He performs various marketing functions and displays goods to attract customers.
6. A retailer usually buys goods on credit and sells on cash basis.
7. Retail shops are generally situated near to customers.





**Question 2. Differentiate between retail trade and wholesale trade.**

**Answer:** Major differences between wholesalers and retailers are as follows:

<b>Wholesalers</b>	<b>Retailers</b>
(1) They are connecting links between the manufacturers and the retailers.	(1) They are connecting links between the wholesalers and the customers.
(2) They purchase goods in large quantities from the manufacturers.	(2) They purchase goods in small quantities from the wholesalers.
(3) They deal in limited number of products.	(3) They deal in variety of products for meeting the varied needs of consumers.
(4) They need more capital to start their business.	(4) They can start business with limited capital.
(5) The display of goods and decoration of premises is not necessary for them.	(5) They lay more emphasis on window display and proper decoration of business premises in order to attract the customers.
(6) Their business operations extend to different cities and places.	(6) They usually localise at a particular place, area or city.
(7) They do not directly deal with the customers.	(7) They have a direct link with the customers.
(8) They do not extend free home delivery and after sales services.	(8) They provide free home delivery and after sales services to the consumers.

**Question 3. Describe the role and functions of the Chamber of Commerce.**

**Answer:** Role and functions of Chambers of Commerce are given below:

1. Businessmen get valuable information free of cost.
2. They can expand their business activities with the help of suggestions and advice from Chambers of Commerce.
3. Chambers of Commerce creates markets for the products of their members by organising fairs and exhibitions.
4. Businessmen get a common forum at which they can discuss problems and exchange views on matters of common interest.
5. Differences and disputes among businessmen can be solved amicably and economically with the help of Chambers of Commerce.
6. Members take advantage of educational and training facilities offered by Chambers of Commerce.
7. Chambers of Commerce undertakes research on behalf of their members.
8. Chambers of Commerce fosters a sense of cooperation among businessmen.

**Question 4. What is the difference between a hawker and a peddler?**

**Answer: Hawkers:** A hawker moves about in residential localities. He carries his goods in a hand cart or bicycle. He deals in low-priced goods of daily use. For example, combs, toys, soaps, mirrors, bangles, vegetables, fruits, ice-cream, etc.

**Peddlers:** A peddler also moves from house to house and sells articles of daily use.

But he carries his wares on his head or on the back of a mule.

Therefore, the basic difference between the two is that hawker has a cycle or cart to carry his goods while peddler carries his goods on heads. So we can say that financially, peddler is weaker than hawker.

**Question 5. Who are itinerants? Name different types of itinerants.**

**Answer:** These retailers do not have the fixed places to carry their trade and generally move from one place to another in order to sell goods. They can be usually seen along the road sides, streets, railway compartments, bus stands, and fairs etc. They usually possess that stock which can be conveniently sold during the day. They need limited funds to carry their business. These types of retailers deal in daily need articles like vegetables, fruits, milk, eggs and fishes etc.

A brief explanation of this type of retailers is given as under:

**1. Hawkers and peddlars:**

These are the petty retailers who carry their products on their heads or on wheeled vehicles from door to door. They usually sell seasonal goods like fruits, vegetables and eatables and also sell certain other goods like pens, toys and utensils, etc.

**2. Cheap Jacks:**

They hire shops in different residential localities wherein they display their products for sale. They do not stick to one place; rather keep moving from one locality to another. They usually deal in household articles.

**3. Market Traders:**

They sell their products at periodical markets on 'market days'. The markets may be weekly or fortnightly. They also sell their wares at different fairs and gatherings.

**4. Street Traders:**

These traders are found on the pavements of crowded streets or markets of the cities. They are also known as "pavement retailers". In big cities like Calcutta, Delhi, Mumbai and Chennai etc., these traders are usually found selling their goods in different markets.

**Question 6. Enumerate the services of the wholesaler to manufacturer and some general services.**

**Answer:** Buying goods in large quantities from the manufacturer and selling them in small quantities to the retailer to cater the needs of the consumer is termed as wholesale trade. The person who undertakes such a trade is known as wholesaler. The wholesaler acts as an intermediary between the producer and the retailer. He is known as the first intermediary in the channel of distribution. The wholesaler distributes business works amongst the members of the staff in such a way that the whole enterprise may work as a complete unit. The distribution of work should be done in such a manner as to yield maximum efficiency at minimum troubles.

**To Manufacturers**

1. The wholesaler provides valuable information to the producers regarding the needs and the requirements of the consumer.
2. As the wholesaler takes the responsibility of collecting order from retailers, he relieves the producers from this task and thereby encourage producers to concentrate on production.
3. The wholesaler provides finance to the producers at the time of need.
4. The wholesaler helps the producers in determining the quality and quantity of goods to be produced as he is in direct contact with the retailers.
5. The producers are helped to maintain steady prices for the product because wholesaler buys when prices are low and sell when prices are high.

## General Service

1. There are certain goods which are to be assembled or graded before they pass to the retailer or the consumer. For these goods the presence of wholesaler is a must.
2. Wholesaler helps in standardisation and grading of the products.
3. For marketing of food grains the services of the wholesalers cannot be dispensed with because they help in packing and re-packing of goods.

### **Question 7. Explain the meaning and advantages of carrying on mail order business.**

**Answer:** Mail order business is a type of retail trade where orders for the supply of goods are received from customers through mail and goods are dispatched through mail. The goods are supplied either by registered parcel or V.P.P. For this type of business, seller advertises in the leading dailies and magazines and desires the buyers to ask for quotation or price list from the seller. Mail order business has been described as shopping by post from the point of view of buyers and selling by post from the point of view of sellers. This form of retail trade has received wider application in USA and Canada. The leading mail order houses are Montgomery Ward Company, Sears Roebuck and Co. of USA. There are various types of mail order houses like general mail order houses, specialty mail order house, producer's mail order house, wholesaler's mail order house and middlemen type mail order. In this trade, there is no direct contact between the seller and the buyer.

The main advantages of mail-order business are given below:

1. This type of business can be started with a small amount of capital and involve less risks in comparison to other types of business houses.
2. Consumers staying at a distant place are benefitted by this method of sale.
3. There is no fear of bad debt as this business does not facilitate credit sale.
4. This business facilitates a country wide market and thereby results in market and operational economies.

### **Question 8. What is a departmental store?**

**Answer:** Departmental Stores : "A departmental store is that type of retail institution which handles a wide variety of merchandise under one roof with the merchandise grouped into well defined departments which are centrally controlled."

"A departmental store is a large retail establishment having in the same building a number of departments each of which confines its activities to one particular branch of trade and forms a complete unit in itself."

"A departmental store carries several product lines, typically clothing, home furnishings, and household goods, where each line is operated as a separate department managed by specialist buyers or merchandisers."

**Features of a departmental store are given below:**

1. Central location
2. Provision of services
3. Corporate status
4. Elimination of middlemen
5. Centralised purchasing
6. Large variety of goods

### **Question 9. Explain different types of fixed shops under retail trade.**

**Answer:** Fixed shops are of two types: (A) Small scale and (B) Large scale.

### (A) Small Scale:

There are different types of small retailers which are explained as under:

1. **Street Stalls Holders:** These retailers carry their business on a very small scale basis in busy and crowded streets by erecting permanent shops. They purchase goods in large quantities from the wholesalers and local suppliers for reselling to the ultimate consumers. They usually deal in household articles and products of daily need. These stall holders are usually the sole proprietors of their shops i.e. carrying every activity right from buying till final disbursement of goods to the consumers.
2. **Second Hand Goods Sellers:** These dealers deal in second hand or used articles. They purchase these articles from public or private auctions and private households. These articles usually include used garments, furniture, books etc. These dealers meet the needs of the poor people who cannot afford new articles.
3. **General Shops:** They deal in different variety of goods and are known as general merchants. The goods are meant for daily use or household purposes. They carry their business in permanent shops. They manage the shops themselves and are most often assisted by sales assistants. Usually goods are sold on credit by these merchants to their permanent customers. They also provide free home delivery service and facility of exchange of rejected goods to the customers.
4. **Speciality Shops:** These retailers deal in one particular line of goods e.g. books, utensils, shoes and medicines etc. These shops can be operated on small scale basis and managed by the owners themselves assisted by salesmen. The most important advantage which can be derived from these shops is that the owners possess the specialised knowledge about the product which is very helpful in satisfying the customers.

### (B) Large Scale Retailers:

The second type of retailers under fixed shops is large scale retailers. The large scale production and rapid urbanisation are responsible for the establishment of large scale retailing organizations.

Most prevalent of these are:

1. Departmental Stores;
2. Multiple Shops or Chain Stores;
3. Mail Order Houses;
4. Super-Markets;
5. Co-operative Stores ; and
6. Vending Machines

### Question 10. Write a short note on Vending Machines.

**Answer:** They are coin operated machines which are used in selling several products such as milk, soft drinks, chocolates, platform tickets etc in many countries. The latest area in which this concept is getting popular is the case of Automated Teller Machines (ATM) in the banking service. They made it possible to withdraw money at any time without visiting any branch of a bank. They can be useful for selling pre-packed brands of low priced product which have high turnover and which are uniform in size and weight. However, the installation cost and expenditure on regular maintenance and repair of these machines are quite high. Moreover, the consumers can neither see the product before buying nor can return the unwanted goods.

## III. Long Answer Type Questions

**Question 1. Explain different types of small scale retail shops.**



**Answer:** Retail trade is carried on both at small scale and large scale. Small scale retailers are either mobile traders (itinerants) or fixed shops.

#### Mobile Traders or Itinerants

These retailers have no fixed place of business. They move from place to place and sell articles of daily use near to consumers. These include the following:

1. **Hawkers:** A hawker moves about in residential localities. He carries his goods in a hand cart or bicycle. He deals in low-priced goods of daily use. E.g. combs, toys, soaps, mirrors, bangles, vegetables, fruits, ice-cream, etc.
2. **Peddlers:** A peddler also moves from house to house and sells articles of daily use. But he carries his wares on his head or on the back of a mule.
3. **Cheap Jacks:** A cheap jack hires a small shop in a residential locality for a temporary period. He shifts his business from one locality to another depending on the availability of customers. He deals in low-priced household articles.
4. **Pavement dealers or Street Traders:** A pavement dealer displays his wares on footpath and outside public places such as railway station, bus stand, cinema, temple, etc. He sells low priced articles like newspapers, magazines, fruits, vegetables, footwear to the passersby. He is also called street trader.
5. **Market Traders:** A market trader sells goods at weekly markets when the shops are closed for weekly holiday. He displays goods outside the closed shops. He deals in low-priced articles of daily use. He may also set up stalls on fairs and exhibitions.

#### Fixed Shops (Small Scale Retail Shops)

Small scale retail shops are the most popular form of retail trade. These may be classified as follows:

1. **Street stalls holders:** These stalls are located in the main streets or street crossings. A stall is an improvised structure made of tin or wood. The street stall holder displays his goods on a temporary platform and sells toys, stationery, hosiery items, etc. at low prices.
2. **Second hand goods shops:** These shops sell used or second hand articles such as books, clothes, furniture, etc. They cater to the needs of poor people who cannot afford new articles. These shops collect goods at private and public auctions.
3. **General stores:** These stores sell a wide variety of products under one roof. For example, a provision store deals in grocery, bread, butter, toothpaste, razor blades, bathing soap, washing powder, soft drinks, confectionery, cosmetics, etc. Consumers can buy most of their daily requirements at one place. Their time and effort is saved. Some of these stores offer free home delivery and monthly credit facilities to regular customers.
4. **Single line stores:** These stores deal in one line of goods. They keep stock of different size, design and quality of goods in the same line. Book stores, chemist shops, electrical stores, shoe stores, cloth stores, jeweler shops, etc., are examples of single line stores.
5. **Specialty shops:** These shops generally specialise in one type of product rather than dealing in a line of products. Shops selling children's garments, educational books, etc., are examples of such shops.

#### Question 2. Discuss the meaning, features and advantages of Consumer Cooperative Store.

**Answer:** Meaning, Features and Advantages of Consumer Cooperative store.

The societies started to help lower and middle class people and protect these sections from the clutches of profit-hungry businessman are called Consumers Cooperative Stores. A consumer's co-operative society is a combination of persons whose aim is to economise by buying in common and retain their profits by selling in common. According to M.C. Sukla, "Consumer Cooperative Store is an

economic enterprise set by the consumers for the distribution of fundamental consumption goods, primarily among the shareholders to the subscriber consumers who are called members of such organization and who have an equal voice in the control of the organization. Features Following are some of the essential features of a consumer's cooperative store:

1. There is no restriction on membership of a consumer co-operative store as any adult person can become a member of a co-operative.
2. The members of the consumer co-operative store distribute capital in the form of share. A member can purchase shares of a value of? 1000 only. Beyond this, shares are not issued to members.
3. The surplus of a store is distributed among the members in the form of dividend. The dividend is paid in proportion to purchases made by the members.
4. It adopts the principles of 'one man, one vote'. A man is not allowed vote by proxy system.
5. The trading of co-operative stores is made on the basis of cash.
6. A sale can be made to non-members on the basis of market rate.
7. It makes bulk purchases directly from the producers and sell these goods to its members on retail basis.

### **Advantages**

Consumer's Cooperative Store has the following advantages:

1. It facilitates its members in getting pure and unadulterated goods at a competitive price.
2. It develops a state of moral booster to the poor people who develop greater confidence among themselves.
3. As the societies are purchasing goods in bulk quantities from the producers, these are in a better position to supply these goods at a competitive price to its members.
4. It improves the purchasing power of the members since dividend is paid on the basis of purchases made.
5. It encourages people to save.

### **Question 3. What difficulties can a consumer face if there is no retail shop?**

**Answer:** If there is no retailer then the consumer will not get the services provided by retailers to him. These services are as under:

1. The consumers are provided with a wide variety of products as the retailers stock a wide range of products produced by different firms.
2. The retailers provide expert advice on the merits and uses of different products and thereby educate consumers on the product.
3. As ready stock of different varieties are maintained with the retailers, the consumer is not required to maintain enough stock of the products.
4. The consumers are given the facilities of purchasing according to their purchasing power since a wide range of products are maintained with the retailers.
5. The retailer arranges home delivery of the product if necessary and renders after sale service.

### **Question 4. Mention different types of Chambers of Commerce in India. Explain any one.**

**Answer:** In India, Chambers of Commerce have been organised at both regional and national levels.

#### **1. Regional Chambers of Commerce**

- Indian Chamber of Commerce (Kolkata)

- Bengal Chamber of Commerce (Kolkata)
- Indian Merchants Chamber (Mumbai)
- Mewari Chamber of Commerce (Mumbai)
- Madras Chamber of Commerce (Chennai)
- Punjab, Haryana and Delhi Chambers of Commerce (New Delhi).

## 2. National Chambers of Commerce

- Federation of Indian Chambers of Commerce and Industry (FICCI)
- Confederation of Indian Industry (CII)
- Associated Chambers of Commerce and Industry (ASSOCHAM)
- All India Organizations of Employers (AIOE)

### **FICCI:**

The Federation of Indian Chambers of Commerce and Industry (FICCI) was established in 1926 in New Delhi. It acts as an apex central body of businessmen in India. It consists of both individual and corporate members.

Its membership consists of 50 chambers of commerce and trade associations, 200 overseas members, and 1500 associate members. Its management is vested in an executive committee. FICCI acts as a representative body of Indian business. It is a non-government, not-for-profit organization. FICCI draws its membership from the corporate sector, both private and public, including SMEs and MNCs. The chamber has an indirect membership of over 2, 50,000 companies from various regional Chambers of Commerce. It is involved in sector specific business policy consensus building, and business promotion and networking. It is headquartered in the national capital New Delhi and has presence in 11 states in India and 8 countries across the world.

### **Question 5. Explain the services of a wholesaler to a retailer, consumer and general services.**

#### **Answer:**

#### **To Retailers**

*WE ARE WITH YOU.....*

1. The retailers are relieved of maintaining huge stock of goods because the wholesaler fills up the stock regularly. The wholesaler buys in large quantities and sell them at convenient lots to the retailers.
2. The wholesaler provides finance and credit facilities to the retailer and thereby relieves the financial difficulties of the retailer.
3. The wholesaler saves retailers from many types of risks. The retailer is not required to carry huge stock as he can get them from the wholesaler at regular interval. By extending credit has saved the retailers a lot.
4. The wholesaler provides valuable advices to the retailer on all matters relating to new product and market condition and thereby relieves him from collection of market data.
5. The wholesaler gives trade discounts on bulk purchase and as such it enables the retailers to earn handful amount of profit.

#### **To Consumer**

1. He enables the consumer to purchase required quantities of goods at the desired time because he supplies goods regularly to the retailers.
2. He provides goods at a cheaper rate because he facilitates in large scale production.

3. The wholesaler is in a better position to stabilize prices of the products by adjusting demand and supply. The consumers are benefitted a lot on account of stabilization of prices.
4. There is no shortage of goods as the wholesaler goes on large purchasing.

**Question 6. Name and define different large scale retail shops.**

**Answer:** The retail trade is conducted now on a large scale. The mass production of goods and the concentration of population in urban centers has necessitated the establishment of large-scale retail trading houses. There are many advantages of retailing on a large scale.

However, in spite of the economies of large scale retailing, the small-scale units could not be eliminated because of the various special advantages possessed by them. Some of the more prominent large-scale retail organizations are as follows:

1. Departmental Stores
2. Multiple Shops or Chain Stores
3. Mail Order Houses
4. Super Markets
5. Consumer Cooperative Stores
6. Vending Machines

1. **Departmental Stores:** A departmental store is a large-scale retail organisation having a number of departments under one roof. Each department specialises in one particular kind of trade. All these departments are centrally organized and are under one united management and control. A departmental store is an organization of several retail stores carried on in one building and under united controlled management. The basic objective of a departmental store is to provide a large variety of merchandise from a pin to an aeroplane at one place.
2. **Multiple Shops or Chain Stores:** A multiple shop system is a network of branch shops, situated at different localities in the city or in different parts of the country, under a centralised management and dealing in similar lines of goods. Such multiple shops are very common and popular in the west and are known as Chain Stores. According to J.L. Fri, "Chain Stores is a group of stores handling similar lines of merchandise with single ownership and centralised location." The Federal Trade Commission defined a chain store as "an organization owing a controlling interest in two or more establishments which sell substantially similar merchandise at retail prices."
3. **Mail Order Sale Houses:** A Mail Order Sale is a retail business where orders are placed by post or mail and goods are received either by registered parcel or V.P.P. i.e., Value Payable Post. Under such a type of selling, the seller advertises his products in the leading dailies and magazines of the area and the intending buyers respond to such advertisements by requesting for catalogues and price lists from the seller. The buyers do not inspect the goods before purchasing but place orders on the basis of the advertisements which they see in the newspapers and magazines. After orders are received from customers, the goods are dispatched by V.P.P. or registered mail. The postman of the buyer's locality delivers the goods to him and takes the payment for the same. Thus the post office plays a vital role in such type of sale, and it is because of this type of sale is also sometimes referred to as "Shopping by Post".
4. **Super Markets:** The super market is a large-scale retail institution specialising in necessities and convenience goods. They have huge premises and generally deal in food and non-food articles. In the words of M. M. Zimmerman, "A super market is a departmentalised retail establishment having four basic departments viz, self-service grocery, meat produce, dairy products plus other household departments, doing a maximum business. It may be entirely owner operated or have some of the departments leased out on a concession basis." Super markets came into existence in the USA during the Great Depression of the thirties. However,



the original super markets were established by independent merchants who dealt mainly in food products.

5. **Consumer Co-Operative Stores:** A consumer co-operative is a retail business which is owned by the consumers themselves. Their basic objective is to eliminate middlemen. The consumers join together and manage the business and the profit thus earned is retained among themselves in the proportion of their contribution. The society purchases in bulk and avails the discounts and sells in small lots to the members. Some of the co-operative stores are run on a large-scale basis while others are small in size and nature.
6. **Vending Machines:** Such selling machines are extensively used in the west. The vending machine is operated by inserting a coin and the buyer can get the articles. Vending machines are usually acquired to sell articles like cigarettes, soft drinks, chocolates, candles etc. Railway platform and bus tickets are also sold by this method. The articles sold by a vending machine are pre-packed and labeled and are usually of reputed brands. The goods should be uniform in size and shape and less bulky in weight. The installation of such machines is an expensive affair and it needs regular maintenance also. Such machines are quite attractive in appearance and installed at busy shopping centers.

### **Question 7. Explain the meaning, features, advantages and disadvantages of super market.**

**Answer:** Super market is nothing but a retail organization providing food and household articles to consumer under one roof without any kind of sales pressure from salesmen and sale assistants. The United States of America (USA) is said to be the homeland .of super markets.

In India, Apna Bazaar, Sahakari Bhandar, etc., are some good examples of super markets or super bazaars.

According to Dictionary of Business and Finance, Supermarket is defined as, “Large store selling a wide variety of consumer goods, particularly food and small articles of household requirements.”

Features of Super market

The characteristics or features of the super market are as follows:

1. **Centrally located in big premises:** Super markets are normally opened in a central locality where ample space is available. It is housed in big premises. Without such premises proper display of different goods cannot be arranged.
2. **No sales pressure:** One important feature of a super market is self-service. There is a complete absence of salesmen and sales assistants. Thus, there is no sales pressure of any kind. Customers can make a selection according to their needs and desires.
3. **Maintains low prices:** The prices of goods in the super markets are reasonable or low. This is because they (companies running super markets) buy in bulk and enjoy all the advantages of bulk buying. Similarly, their salary bill is low due to the absence of salesmen and sales assistants.
4. **Sell goods on a cash basis:** Super markets sell goods on ‘Cash and carry basis In such a kind of a business, credit facilities are usually not offered. This reduces bad debts.
5. **Deals in necessities of life:** Super market deals in commodities, which are required regularly. Thus, they deal in tinned products of well-known brands, groceries and provision, ready made garments, fruits, etc. The turn over is quick as the demand for the necessities of life is a continuous one.
6. **Established by companies:** Super markets are retailing shops, which are large in size. They do business on a large scale and require huge financial resources. Hence, they are normally established by Joint-stock companies.

7. **Deals in pre-packed goods:** Super market normally deals in pre-packed goods or products. It uses latest and up-to-date packing material to protect quality and quantity. On all packages, prices, weights, particulars of goods, grade and quality are specified.
8. **Needs huge capital to operate:** Super market is a large retail trading organization. It requires a substantial amount of capital for big premises, huge warehousing, ample parking and stocking of a wide variety of commodities.
9. **Self-service store:** Customers are given attractive trolleys or hand baskets or bags for keeping goods which they want to buy. Goods are systematically arranged and beautifully displayed. Customers select these goods and keep them in the trolley. Finally, they have to come to the billing section for making payment and then delivery is given at the delivery counter.

### Advantages of Super Market

- Saving in labour cost due to self-service system.
- Super market has large turn over.
- Reasonable or low prices of goods.
- Low cost of operation.
- Freedom of selection.
- Shopping is very easy and quick.
- Due to adequate parking space, shopping becomes easy and pleasing activity rather than boredom.
- High degree of efficiency due to elimination of service.
- High margin of profit to organisers.
- Advantages of large scale operations.

### Disadvantages of Super Market

The disadvantages of a super market or Super Bazaar are as follows:

- Super market requires huge financial resources.
- It is normally situated at a long distance from the residential localities.
- There is lack of personal attention.
- Super market does not provide various services such as free home delivery, personal guidance, credit facility and after sale service.
- It faces the problem of co-ordinating activities of various sections of the market.
- It requires large and extensive premises.
- Goods which require explanation by salesmen cannot be sold in such markets.

### Question 8. What are the differences between departmental stores and multiple shops?

**Answer:** The differences between departmental stores and multiple shops are summarized below:

1. **Location:** A departmental store is centrally located and attracts customers towards it. On the other hand, multiple shops are situated in different localities and attempt to reach near the customers.
2. **Variety of goods:** A departmental store deals in a wide variety of products and serves as a universal supplier. On the other hand, a multiple shop specialises in one line of goods.
3. **Type of customers:** A departmental store caters mainly to rich people, whereas multiple shops cater to the general public.
4. **Nature of dealings:** A departmental store sells goods both on cash and credit basis. But multiple shops sell goods on cash and carry basis.

5. **Services:** A departmental store offers banking, post office, restaurant and other facilities to customers. Multiple shops do not offer such services.
6. **Pricing:** Different departments of a departmental store may sell goods at different prices. But all the multiple shops sell goods at the same prices.
7. **Decoration and display:** Every department of a departmental store may have different decoration and display. But all the multiple shops of an owner have uniform shop decoration and window display. A departmental store advertises at local level, whereas multiple shops advertise at national level.
8. **Object:** A departmental store aims at providing everything at one place. Multiple shop system, on the other hand, is an attempt to eliminate middlemen and establish direct contact between the manufacturer and consumers.
9. **Flexibility:** In a departmental store quick adjustment can be made according to local changes. One line of goods can be substituted by others. Multiple shop system lacks such flexibility.
10. **Control:** In a departmental store, heads of departments have considerable discretion in the management of operations. Branch managers in a multiple shop system have to follow the policies and procedures laid down by the head office.
11. **Ownership:** A departmental store is generally owned and established by a retail trader. On the other hand, multiple shop system usually operates under the ownership and management of a manufacturer or a wholesaler.
12. **Risk:** Risk involved in a departmental store is relatively greater because success depends on the prosperity of a single location. In multiple shops system risks are spread over different shops located in different areas .

**Question 9. Mention and define the documents which are used in internal trade.**

**Answer:** The following are the main documents used in the internal trade.

1. **Invoice:** In case of credit purchases, a statement is supplied by the seller of goods in which he gives particulars of goods purchased by buyer such as quantity, quality, rate, total value, sales tax, trade discount, etc. It is also called a Bill or Memo. Buyer gets information about the amount he has to pay to the seller from Invoice only.
2. **Performa Invoice:** The “statement (or forwarding letter) containing the details of goods consigned from consigner to consignee is known as a Performa Invoice. It gives the particulars regarding quantity, quality, price and expenses incurred on the goods consigned. In case of consignment, consignee is an agent of consigner who is supposed to sell goods on behalf of consigners and this statement Performa Invoice is only for his information. It is also known as Interim Invoice.
3. **Debit Note:** It refers to a letter or note which is sent by the buyer to the seller stating that his (seller’s) amount has been debited by the amount mentioned in note on account of goods returned herewith. It states the quantity, rate, value and the reasons for the return of goods.
4. **Credit Note:** It refers to a letter or note which is sent by the seller to the buyer stating that his account has been credited by the mentioned amount on account of acceptance of his claim about the goods returned by him.
5. **Lorry Receipt:** It refers to a receipt issued by the transport company for goods accepted by it for sending from one place to another. It is also known as Transport Receipt (TR) and Bilty.
6. **Railway Receipt:** It refers to a receipt issued by the railways for goods accepted for sending from one station to another.

**Question 10. Discuss advantages and disadvantages of Mail Order House.**

**Answer:** The retail outlets that sell their goods through mail are referred to as mail order houses. There is no personal contact between the buyers and the sellers in this type of trading. The trader

contacts the customer through advertisement in newspaper or magazines, circulars, catalogues and price list is sent to them by post. All the information about product such as price, features, delivery terms, terms of payment etc are described in the advertisement. The customers may be asked to make full payment in advance or goods may be sent by VPP (Value Payable Post), under which goods are delivered to the customer only when he makes full payment for the same. The goods may be sent through a bank which delivers them to the customer only when he makes full payment.

#### **Advantages of Mail Order Houses:**

1. They can be started with low amount of capital as no expenditure on building or other infrastructural facilities are required.
2. They do not require the services of middlemen so they are eliminated. .
3. They do not extend credit facilities to the customers and thus there are no chances of bad debts.
4. They can serve people wherever postal services are available.
5. They deliver goods at the doorstep of the customer which result in great convenience to the customers in buying the goods.

#### **Limitations of Mail Order Houses:**

1. There is no personal contact between the buyers and the sellers. The buyers are not in a position to examine the products before buying.
2. They rely heavily on advertisement and other promotional activities which increases their cost of product.
3. In mail order selling after sales services are absent.

#### **IV. Higher Order Thinking Skills (HOTS)**

##### **Question 1. What difficulties will be faced by the manufacturers if wholesalers are eliminated from the chain?**

**Answer:** Manufacturer gets following services from retailer which he will not be able to get if wholesaler is eliminated from the chain.

1. By selling under his own brand name the wholesaler often relieves the manufacturer of the need to advertise his product.
2. The wholesaler removes goods in larger quantities as they are produced, thus clearing the production lines.
3. By warehousing the goods the wholesaler bridges the time gap between production and consumption, leaving the manufacturer free to concentrate on his specialised activities.
4. He eliminates the need for a marketing system with all that involves in terms of warehousing space, distribution network, sales staff, accounting records, and debt collection.
5. By paying promptly the wholesaler reduces the working capital required by the manufacturers.

##### **Question 2. “The chambers interact with the government at different levels to reorient or put in place policies which reduce trade hindrances.” Comment.**

**Answer:** The chambers interact with the government at different levels to reorient or put in place policies which reduce hindrances, increase interstate movement of goods, introduce transparency and remove multiple layers of inspection and bureaucratic hurdles. It also aims at establishing right kind of infrastructure and simplifying and harmonizing the tax structure.



- **Transportation:** The Chambers of Commerce and Industry help in many activities concerning interstate movement of goods which includes registration of vehicles, surface transport policies, construction of highways and roads.
- **Octroi and other Local Levies:** The Chambers of Commerce and Industry ensures that its imposition is not at the cost of smooth transportation and local trade.
- **Harmonization between Sales Tax and VAT:** The Chambers of Commerce and Industry plays an important role in interacting with the government to harmonize the sales tax structure in different states. A uniform sales tax is important for balanced growth as it is a source of state revenue.
- **Marketing of Agro products and related issues:** The Chambers of Commerce and Industry can intervene and interact with concerned agencies in formulating policies regarding marketing of agro-products and related issues.
- **Weights and Measures to prevention of duplication in brands:** It is necessary to protect the interests of the consumers as well as traders. They need to be enforced strictly. The Chambers of Commerce and Industry interact with the government and makes such laws which takes action against wrong doers.
- **Excise Duty:** The Chambers of Commerce and Industry play a vital role in streamlining of excise duties.
- **Promoting sound Infrastructure:** The Chambers of Commerce and Industry in collaboration with the government takes initiative to develop a sound infrastructure.
- **Labour Legislations:** The Chambers of Commerce and Industry interacts with the government constantly on issues related to labour laws and retrenchment.

**Question 3. What difficulties will be faced by the consumers if retailers are eliminated from the chain?**

**Answer:** If retailers are removed, it will lead to direct marketing. In general, you cannot save money by “eliminating the middleman” because intermediaries specialize in performing certain tasks that they can perform more cheaply than the manufacturer. Most grocery products are most efficiently sold to the consumer through retail stores that take a modest mark-up—it would not make sense for manufacturers to ship their grocery products in small quantities directly to consumers. Intermediaries perform tasks such as

1. Moving the goods efficiently (e.g., large quantities are moved from factories or warehouses to retail stores);
2. Breaking bulk (manufacturers sell to a modest number of wholesalers in large quantities—quantities are then gradually broken down as they make their way toward the consumer);
3. Consolidating goods (retail stores carry a wide assortment of goods from different manufacturers—e.g., super markets span from toilet paper to catsup); and Aiding services (e.g., demonstrations and repairs).
4. If these middlemen are eliminated, they will face absence of these functions which will be troublesome for them.

**Question 4. Explain important terms used in context of internal trade.**

**Answer:** The following are the main terms used in the internal trade.

1. **Cash on delivery (COD):** It refers to a type of transaction in which payment for goods or services is made at the time of delivery. If the buyer is unable to make payment when the goods or services are delivered, then it will be returned to the seller.

2. **Free on Board or Free on Rail (FOB or FOR):** It refers to a contract between the seller and the buyer in which all the expenses up to the point of delivery to a carrier (it may be a ship, rail, lorry, etc.) are to be borne by seller.
3. **Cost, Insurance and Freight (CIF):** It is the price of goods which includes not only the cost of goods but also the insurance and freight charges payable on goods.
4. **E and OE (Errors and Omissions Expected):** It refers to that term which is used in trade documents to say that mistakes and things that have been forgotten should be taken into account. This term is used in an attempt to reduce legal liability for incorrect or incomplete information supplied in a document such as price list, invoice, cash memo, quotation etc.

## V. Value Based Questions

**Question 1. Peddlers and hawkers create traffic indiscipline and therefore it must be declared as illegal. Do you agree? Justify your answer.**

**Answer:** I do not agree. In India it is the most visible segment of the urban informal economy. It is indisputable that there are thousands—and in some cases, tens or hundreds of thousands—of street vendors in most big cities of the developing world. Yet it is exceedingly difficult to produce accurate estimates of the number of street traders in any given city. In some countries, official statistics on street vendors are available, though they underestimate the total number of people engaged in street vending. Without providing them an alternative employment, we cannot think of making it illegal. Yes, for security reasons, they may be asked to get an ID with them or they may be issued a pass by local authorities.

**Question 2. Which retail shops are run by the weaker sections? Do you think they are capable to face competition from large scale retail shops? How do they exist then?**

**Answer:** Weaker sections of society run retail shops in following ways:

1. **Hawkers and Peddlers:** The hawkers carry their goods in a wheeled vehicle while the peddlers carry the goods on their heads or backs.
2. **Market Traders:** These retailers open their shops at different places on fixed days.
3. **Street Traders or Pavement Vendors:** These retailers display their goods at busy street corners or pavements.
4. **Cheap Jacks:** These retailers generally hire a small shop in a residential colony for a temporary period.

No, they are not capable to face competition from large scale retailers. In fact there I do not have to face competition from large scale retailers because their clientele is different from them. Poor and lower middle class people buy from small retail shops while upper middle class and rich people buy from large scale retail shops. Therefore, they can manage to exist due to following advantages over large scale retail shops.

- A small scale retailer himself looks after his business. He is not required to employ managers or to spend on advertising, etc. Therefore, he can sell goods at lower prices.
- A small scale retailer can take quick decisions. He is not required to consult others.
- A small scale retailer can easily adjust his stocks according to the changing needs and fashions of his customers.
- A small scale retailer can more easily maintain secrecy of his business affairs.

# **NCERT SOLUTIONS For Class 11 Business Studies**

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### **International Business 1**

#### **Class 11 Business Studies Solutions Chapter 11 International Business 1**

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International Business 1

#### **I. Multiple Choice Questions**

**Question 1. In which of the following modes of entry, does the domestic manufacturer give the right to use intellectual property such as patent and trademark to a manufacturer in a foreign country for a fee**

- (a) Licensing (b) Contract manufacturing**
- (c) Joint venture (d) None of these**

**Question 2. Outsourcing a part of or entire production and concentrating on marketing operations in international business is known as**

- (a) Licensing (b) Franchising**
- (c) Contract manufacturing (d) Joint venture**

**Question 3. When two or more firms come together to create a new business entity that is legally separate and distinct from its parents it is known as**

- (a) Contract manufacturing (b) Franchising**
- (c) Joint ventures (d) Licensing**

**Question 4. Which of the following is not an advantage of exporting?**

- (a) Easier way to enter into international markets**
- (b) Comparatively lower risks**
- (c) Limited presence in foreign markets**
- (d) Less investment requirements**

**Question 5. Which one of the following modes of entry requires higher level of risks?**

- (a) Licensing (b) Franchising**
- (c) Contract manufacturing (d) Joint venture**

**Question 6. Which one of the following modes of entry permits greater degree of control over overseas operations?**

- (a) Licensing/franchising (b) Wholly owned subsidiary**
- (c) Contract manufacturing (d) Joint venture**

**Question 7. Which one of the following modes of entry brings the firm closer to international markets?**

- (a) Licensing (b) Franchising**
- (c) Contract manufacturing (d) Joint venture**

**Question 8. Which one of the following is not amongst India's major export items?**

- (a) Textiles and garments (b) Gems and jewellery**
- (c) Oil and petroleum products (d) Basmati rice**

**Question 9. Which one of the following is not amongst India's major import items?**

- (a) Ayurvedic medicines (b) Oil and petroleum products**
- (c) Pearls and precious stones (d) Machinery**

**Question 10. Which one of the following is not amongst India's major trading partners?**

- (a) USA (b) UK**
- (c) Germany (d) New Zealand**

**Answer:**

1. (a) 2. (c) 3. (c) 4. (a) 5. (c)
6. (b) 7. (c) 8. (d) 9. (b) 10. (d)

## II. Short Answer Type Questions

### Question 1. Differentiate between international trade and international business.

**Answer:** Difference between international trade and international business is similar to difference between trade and business.

1. The scope of international business is much wider than international trade. International trade means exports and imports of goods which is an important component of international business but international business includes much more than this.
2. International trade in services like travel and tourism, transportation, communication, banking, warehousing, distribution and advertising is a part of international business.
3. International business also includes foreign direct investments, contract manufacturing, and setting up wholly owned subsidiaries etc. which are not included in international trade.

### Question 2. Discuss any three advantages of international business.

**Answer:** The following are some of the advantages of foreign trade:

1. **Optimum use of resources:** Foreign trade helps in the optimum use of natural resources and avoids wastage's of resources. It ensures the presence of stable price by avoiding wide fluctuations in prices. It tries to equalise the world price.
2. **Increased standard of living:** It ensures more production to meet the demand of the people of different countries. By increased production, it becomes possible to increase income and the standard of living of its people. It also increases the standard of living by increasing more employment opportunities. It enables a country to import those goods which it cannot produce.
3. **Large scale production:** It ensures large production because the production is carried on to meet the demand of its people as well as world market. Large scale production also ensures a great deal of internal economies which reduces the cost of production.

### Question.3. What is the major reason under lying trade between nations?

**Answer.** The major reason behind international business is that the countries cannot produce equally well or cheaply all the commodities. This is called theory of comparative cost advantage. It is so because resources are unequally distributed in natural resources. Some countries are abundant in one commodity and scarce in others while opposite is true for some other country. It makes a case for international trade and exchanging abundant commodity with scarce commodity by nations. Different nations are endowed with different factors of production which includes land, labour, capital and entrepreneurship. For example, India is a labour abundant country. Therefore, it is advisable for India to produce such commodities which use labour intensive methods and exchange it for those which use capital intensive methods. USA is a capital abundant country. Therefore, nations need to trade. Due to these reasons one country has a comparative advantage in production of particular goods as compared to other countries. Consequently, each country finds it advantageous to produce those selected goods and services that it can produce more effectively at home and importing those goods in which other nations have a comparative cost advantage.

### Question 4. Discuss as to why nations trade.

**Answer:** Nations trade because of following reasons:



1. **Unequal distribution of natural resources:** Resources are unequally distributed in natural resources. Some countries are abundant in one commodity and scarce in other while opposite is true for some other country. It makes a case for international trade and exchanging abundant commodity with scarce commodity by nations.
2. **Unequal availability of factors of production:** Different nations are endowed with different factors of production which includes land, labour, capital and entrepreneurship. For example, India is a labour abundant country. Therefore, it is advisable for India to produce such commodities which use labour intensive methods and exchange it for those which use capital intensive methods. USA is a capital abundant country. Therefore, nations need to trade.
3. **Theory of Comparative Cost Advantage:** Due to these factors, some countries are in an advantageous position in producing selected goods and services which other countries cannot produce that effectively and efficiently and vice-versa. Consequently, each country finds it advantageous to produce those selected goods and services that it can produce more effectively at home and importing those goods in which other nations have a comparative cost advantage.
4. **Geographical Specialisation:** The international business as it exists today is the result of geographical specialisation. Even within a country each state specialises in those goods for which it is geographically more suitable. Similarly, each nation specialises in those goods in which it is specialised as per availability of resources and exchanges it for other goods and services in foreign market.
5. **Cost minimization principle of firms:** Firms get involved in international business to minimise their costs and maximise their profits.

**Question 5. Enumerate limitations of contract manufacturing.**

**Answer:** Major limitations of contract manufacturing are discussed below:

1. **Non adherence to quality standards:** Local firms may not adhere to quality standards or product design. It may cause serious quality problems for international firm. .
2. **No control on production by local producer:** Local producer has no control on manufacturing as goods are manufactured strictly as per the terms and specifications by international firm.
3. **Zero control over sales:** Local producer can't sell the output to customers directly. He needs to sell to the international firm at a pre-determined price. It reduces profits of local firm.

**Question 6. Why is it said that licensing is an easier way to expand globally?**

**Answer:** It is said that licensing is an easier way to expand globally because of its advantages over other modes of international business.

1. **Less Expensive:** Under the licensing, it is the licensee who sets up the business unit. Therefore, licensor has to invest no money. Therefore, it is considered as a cheaper way of entering\*into international business.
2. **Zero Risk of Loss:** Licensor need not take pain of risk of profits and loss. He is paid a pre-determined fees called royalty by the licensee. As long as licensor continues to produce under the license, licensor keeps on getting his fees irrespective of whether licensee is making profits or incurring losses.
3. **Less risk of government intervention or takeovers:** A local person handles the business in foreign country. Therefore, there are lesser chances of government intervention or takeovers.
4. **Better knowledge of local needs:** Since licensee is the local person, he has better understanding of local needs, marketing strategies and business environment.

5. **Safety of Intellectual Property Rights:** As per the terms of the licensing, only licensee can make use of licensor's copyrights, patents and brand names in foreign countries. Therefore, there is lesser risk of these intellectual property rights being missed by other local firms.

**Question 7. Differentiate between contract manufacturing and setting up wholly owned production subsidiary abroad.**

**Answer:** The difference between contract manufacturing and wholly owned subsidiary is discussed below:

Basis	Contract Manufacturing	Wholly Owned Subsidiary
Meaning	It refers to the type of international business where a firm enters into contract with some local manufactures in foreign countries to get certain components of goods produced as per their specifications.	In this the parent company acquires the full control over the foreign company by purchasing its 100% equity capital.
Forms	It can take three forms: (a) Getting produced certain parts of final products which will be used for the production of final products later. (b) Assembly of components into final products. (c) Complete manufacture of the products like garments.	It can be established in two ways: (a) As a green field venture, in which an altogether a new firm is set up to start operations in a foreign country. (b) Acquiring an existing firm in foreign country and using it for manufacturing and promoting its products in home country.

**Question 8. Distinguish between licensing and franchising.**

**Answer:**

Basis	Licensing	Franchising
Meaning	Licensing is a contractual agreement in which one firm grants access to its patents, trade secrets, technology to another firm in a foreign country for a fee. This fee is called royalty.	Franchising is basically a specialized form of licensing in which franchisor sells intangible property to the franchisee but also imposes strict rules on franchisee as to how business is to be done.

Connected with	Licensing is used in connection with production and marketing of goods.	The term franchising is used in connection with production of services.
Stringency	Licensing is relatively less stringent than franchising. Strict rules and regulations are not set by licensors as to how licensees should operate while running their business.	Franchising is relatively more stringent than licensing. Strict rules and regulations are set by franchisers as to how franchisees should operate while running their business.

**Question 9. List major items of India's import.**

**Answer:** India's major items of imports include crude oil and petroleum products, capital goods, electronic goods, pearls, precious and semi precious stones, gold, silver and chemicals.

**Question 10. What are the major items that are exported from India?**

**Answer:** India's major items of exports include textiles, garments, gems and jewellery, engineering products and chemicals, agriculture and allied products.

**Question 11. List the major countries with whom India trades.**

**Answer:** India's major trading partners are USA, UK, Germany, Japan, Belgium, Hong Kong, UAE, China, Switzerland, Singapore and Malaysia.

**III. Long Answer Type Questions**

**Question 1. What is international business? How is it different from domestic business?**

**Answer:** International business refers to business which is carried on in two or more nations. It means carrying on business activities beyond national boundaries. These activities normally include the transaction of economic resources such as goods, capital, services (comprising technology, skilled labour, and transportation, etc.), and international production. It refers to that business activity that takes place beyond the geographical limits of a country. Production may either involve production of physical goods or provision of services like banking, finance, insurance, construction, trading, and so on. Thus, international business includes not only international trade of goods and services but also foreign investment, especially foreign direct investment.

Differences between International Business and Domestic Business are summarised below:

Basis	International Business	Domestic Business
Nationality of buyers and Sellers	People of different nationality participate in international business.	People of one nationality participate in domestic business. Exceptions are possible.
Nationality of other stakeholders	Employees, suppliers, customers, shareholders, partners, middlemen etc. belong to different nationality in international business.	Employees, suppliers, customers, shareholders, partners, middlemen etc. belong to same nationality in domestic business. Exceptions are possible.
Political Systems	International business is subject to political system of many nations.	Domestic business is subject to political system of one country.



Risk	Degree of risk is higher in international business.	Degree of risk is lower as compared to international business.
Mobility of factors of production	Mobility of factors of production is less across countries.	Mobility of factors of production is more within geographical boundaries of the country.
Consumer's taste and preferences	International markets are heterogeneous in terms of taste and preferences of the customer.	Domestic markets are more homogeneous in terms of taste and preferences of the consumer.
Currency	International business involves usage of foreign currency.	Domestic business makes use of domestic currency.
Business regulations and policy	International business is subject to rules laws, policies, and taxation system etc of multiple countries.	Domestic business is subject to rules, laws, policies, and taxation system etc of single country.
Differences in business systems and practices.	Business systems and policies are heterogeneous in two countries.	Business system and policies are more homogeneous within a country.

**Question 2. "International business is more than international trade". Comment.**

**Answer:** It is rightly said that international business is more than international trade. The scope of international business is much wider than international trade. International trade means exports and imports of goods which is an important component of international business but international business includes much more than this. International trade in services like travel and tourism, transportation, communication, banking, warehousing, distribution and advertising is a part of international business. International business also includes foreign direct investments, contract manufacturing, and setting up wholly owned subsidiaries etc. which are not included in international trade. It is clear from the diagram given below:



**Question 3. What benefits do firms derive by entering into international business?**

**Answer:** The trade between two or more nations is termed as foreign trade or international trade. It involves exchange of goods and services between the trades of two countries. Foreign trade consists of import trade, export trade and entrepot trade. In the early stages of human civilization, production was confined as per consumption. Human wants were limited. Nowadays, human wants are increasing and as such no man was considered to be self-dependent. Like this no country can live in isolation and claimed the status to be self-sufficient. Because of this reason countries have trade



relationships with each other. The primary objective of foreign trade is to increase foreign trade and increase the standard of living of its people. There is an increasing demand for foreign trade because of the following reasons:

1. The natural resources are unevenly distributed.
2. The presence of specialisation and division of labour.
3. Different countries have difference in economic growth rate.
4. The presence of the theory of comparative cost.

The following are some of the advantages of foreign trade:

1. **Optimum use of Resources:** Foreign trade helps in the optimum use of natural resources and avoids wastages of resources.
2. **Stable Price:** It ensures the presence of stable price by avoiding wide fluctuations in prices. It tries to equalise the world price.
3. **Availability of all types of goods:** It enables a country to import those goods which it cannot produce.
4. **Increased Standard of living:** It ensures more production to meet the demand of the people of different countries. By increased production, it becomes possible to increase income and the standard of living of its people. It also increases the standard of living by increasing more employment opportunities.
5. **Large Scale production:** It ensures large production because the production is carried on to meet the demand of its people as well as world market. Large scale production also ensures a great deal of internal economies which reduces the cost of production.

**Question 4. In what ways is exporting a better way of entering into international markets than setting up wholly owned subsidiaries abroad.**

**Answer:** Exporting is a better way of entering into international markets than setting up wholly owned subsidiaries abroad in following ways:

1. **Easiest Way:** It is easy to enter international markets through exports as compared to wholly owned subsidiaries.
2. **Less Involving:** It is less involving as compared to establishing a wholly owned subsidiary because firms need not invest that much time and money.
3. **Zero risk of Foreign Investment:** Exporting does not require much of investment in foreign countries. Therefore, foreign investments risks are low as compared to when a firm starts its wholly owned subsidiary in foreign country.
4. **Less Costly:** In a wholly owned subsidiary, 100% equity investment is to be made by foreign company. Therefore, small and medium size producers can't think of this mode of entering into international business.
5. **Risk of Profit and Loss:** In wholly owned subsidiary, 100% equity capital is contributed by foreign company alone. Therefore, it alone has to bear the risk of losses.
6. **Government Intervention:** Some countries are averse to setting up of 100% wholly owned subsidiaries by foreign companies. This form of business operations is subject to high degree of political risks.

**Question 5. Discuss briefly the factors that govern the choice of mode of entry into international business.**

**Answer:** Following factors govern the choice of mode of entry into international business,

1. **Ease of entry:** First and foremost factor that determines the choice of mode of entry into international business is ease of entry. A businessman wants to adopt such mode of entry into international business which is easy and less formalities requiring. Exporting, importing, licensing and franchising are better ways from this perspective.
2. **Cost:** Second determining factor is cost involved. For example, very less cost is involved in exporting, importing, licensing, franchising and contract manufacturing as compared to joint ventures and setting wholly owned subsidiaries.
3. **Control over production:** If the foreign company or producer wants full control over production activities in local country, he will prefer franchising, wholly owned subsidiary or joint venture with majority share holding. If it is not so important, he will prefer exporting, importing, contract manufacturing licensing etc.
4. **Sharing of Technology:** If the company has no problem in sharing of technology then it may choose joint venture or franchising. But if it does not want to share its technology and trade secrets, it will prefer wholly owned subsidiary or exporting,
5. **Risk Involved:** If a firm is ready to take risk, it may choose wholly owned subsidiary or joint ventures but if it is willing to minimize its loss then it should choose exporting, licensing, franchising or contract manufacturing.

**Question 6. Discuss the major trends in India's foreign trade. Also list the major products that India trades with other countries.**

**Answer:** India is 10th largest economy in the world. It is the second fastest growing economy, next only to China. But India's performance in international business is not very good. India's share in world trade in 2003 was just 0.8%. In absolute terms, there has been significant increase in imports as well as exports. Total exports have increased from 606 crores in 1950-51 to Rs. 2, 93,367 crores in 2003-04 while imports have increased from 608 crores in 1950-51 to 3, 59,108 crores in 2003-04. Exports increased 480 times while imports increased 590 times indicating that there is adverse balance of trade. India's major trading partners are USA, UK, Germany, Japan, Belgium, Hong Kong, UAE, China, Switzerland, Singapore and Malaysia.

India's major items of exports include: Textiles, garments, gems and jewellery, engineering products and chemicals, agriculture and allied products.

India's major items of imports include: Crude oil and petroleum products, capital goods, electronic goods, pearls, precious and semi precious stones, gold, silver and chemicals.

Before 1991, promotion of import substitution and discouraging of exports was government strategy. Imports consisted of machinery, equipment and intermediates in production, petroleum and petroleum-products. After green revolution, imports of fertilizer too increased.

Before 1991, India's exports consisted of agricultural products like tea, raw cotton with the diversifying industrial structure, promoted by import substitution, exports of manufactures were growing. During 1986-91, external trade formed only 13.40 % of the GDP. During the 1990-2000, this share is rising continuously.

India's foreign trade has grown to exports of \$250 billion and imports of \$380 billion in 2010-11. The ratio of exports plus imports to GDP has grown from 13.40 % during 1985-90 to almost three times that, being 37.7 % in 2010-11. On adding services it becomes from 22.9 % in the 1990s to 49.0 % in 2010-11.

Leading role has been played by 'invisibles' which includes both services, mainly software services, export of which has grown to \$59 billion in 2010-11. It has decreased the current account deficit from \$130 billion to \$44. This deficit was compensated by capital account surplus of \$59 billion in that year.

But it is only because of IT services and we are still lacking in manufacturing exports which can generate a large volume of employment. We have not done as well as China and Malaysia have done.

**Question 7. What is invisible trade? Discuss salient aspects of India's trade in services.**

**Answer:** Trade in services is called invisible trade. Since services are invisible, export and import of services has been named as invisible trade. In absolute terms, there has been significant increase in India's foreign trade in services. Export and import of foreign travel, transportation and insurance has largely increased during last four decades. There has been a change in composition of services exports. Software and other miscellaneous services have emerged as the main categories of India's export of services. Share of travel and transportation has declined to 29.6% in 2003-04 from 64.3% in 1995-96 while the share of software exports has increased from 10.2% in 1995-96 to 49% in 2003-04.

**Table showing Percentage share of major services to total services exports**

Sector/Year	1995-96	2000-01	2001-02	2002-03	2003-04
Travel	36.9	21.5	18.3	16.0	16.5
Transportation	27.4	12.6	12.6	12.2	13.1
Software	10.2	39.0	44.1	46.2	48.9
Miscellaneous	22.9	21.3	20.3	22.4	18.7

The composition of India's external trade has been changing. During 1950s and 60s exports were mainly of primary goods. Over time, the role of engineering goods has been increasing. Overall manufactured goods constitute 66 % of total exports, of which engineering goods are 27%. Textiles and textile products, garments and leather products make around 10 % of India's exports.

In nutshell, we can say that the role of the external or internationally traded goods sector has been growing steadily in Indian economy. At present imports and exports together account for upto 49 % of India's GDP which was 18% in 1990s. In India there is greater share of exports of services which are IT software services, called IT- enabled services (ITES). It contributed more than 20% of India's export earnings. India accounts for about 45% of the world's BPO services. The major Indian IT companies, TCS, Infosys and Wipro, initiated and perfected the Global Services Delivery (GSD) model. It is because India has a vast pool of software engineers and an even bigger pool of English-knowing staff. With growing competition in the market for such services, Indian companies have moved from BPO to Knowledge Process Outsourcing (KPO), which involves providing services for R and D and to high-end consulting.

## **MORE QUESTIONS SOLVED**

### **I. Very Short Answer Type Questions**

**Question 1. Out of international trade and international business which one is wider in scope?**

**Answer:** International business

**Question 2. What is the basic reason behind international trade?**

**Answer:** Comparative cost advantage in production of some goods.

**Question 3. Give one point of difference between licensing and franchising.**

**Answer:** Licensing is used for goods and franchising is used for services.

**Question 4. When a middleman is involved in handling export procedure, then it is called by what name?**

**Answer:** Indirect exporting

**Question 5. Licensee or franchisee pays a fee to licensor or franchisor. What is it called?**

**Answer:** Royalty.

**Question.6. Reebok orders for footballs to local manufacturers of Ludhiana and then sells it all over the world. It is an example of what?**

**Answer:** Contract manufacturing.

**Question 7. Name the country whose share is largest in India's exports and imports.**

**Answer:** USA

**Question 8. What is the share of India's exports in world exports?**

**Answer:** 0.8%

**Question 9. Which service has got dominating share in foreign trade in services?**

**Answer:** Software and Miscellaneous

**Question 10. India is\_ largest economy in the world.**

**Answer:** 10th

## **II. Short Answer Type Questions**

**Question 1. Define international business.**

**Answer:** According to Roger Beneett, "International business involves commercial activities that cross national frontiers."

In the words of John D Daniels and Lee H Radebough, "International business is all about business transactions—private and governmental that involve two or more countries. Private companies undertake such transactions for profits; government may or may not do the same in their transactions."

According to Michael R Czinkota, "International business consists of transactions that are devised and carried out across national borders to satisfy the objectives of the individuals, companies and organizations. These transactions take on various forms which are often correlated."

**Question 2. Explain different forms of Joint Ventures.**

**Answer:** A joint venture refers to establishing a firm which is jointly owned by two or more independent firms. It can be entered into three ways:

1. A foreign investor may buy interest in a local company
2. Local firm may acquire an interest in an existing foreign firm.
3. Both local and foreign firms jointly establish a new enterprise.

**Question 3. Explain different forms of contract manufacturing.**

**Answer:** Contract manufacturing can take three forms:

1. **Getting produced certain parts of final products:** In case of automobiles or purses or shoes some parts are got manufactured from foreign countries which are used for the production of final products later.



2. **Assembly of components into final products:** In case of electronic items, different parts are assembled at that country where they are to be sold.
3. **Complete manufacture of the products:** In some cases, commodities like garments a contract is given for complete manufacturing and products are sold in brand name of foreign companies.

#### Question 4. India embarks on the path of globalisation. Comment

**Answer:** Since 1991, with the announcement of New Economic Policy, 1991 India also embarks on the path of globalisation. India was facing a severe financial crisis. It approached International Monetary Fund and World Bank for help. IMF agreed to lend money to India on the condition that India will introduce structural changes in its economy. As a result, India announced the policy of LPG i.e. Liberalisation, Privatisation and Globalisation. Then on 1 January, 1995 WTO was formed. India became founder member of WTO and thereby was under a compulsion to follow rules and regulations of WTO. Therefore, it had to open up its economy for rest of the world and they also allowed India to enter their markets. Though the process of reforms has somewhat slowed down, India is very much on the path of globalisation.

#### Question 5. What are the benefits of international trade to firms?

**Answer:** Given below are benefits of international business for firms:

1. **Prospects for higher profits:** It creates better prospects for higher profits.
2. **Increased capacity utilisation:** It leads to better utilisation of capacity.
3. **Prospects for growth:** It creates better prospects for growth.
4. **Way out to intense competition in domestic market:** International business acts as an alternate when there is intense competition in domestic market.
5. **Improved business vision:** When a business firm acts globally, it gives it an improved business vision.

#### Question 6. Write a short note on India's foreign investments.

**Answer:** There has been a phenomenal increase in foreign capital inflow and outflow. Inward foreign investments have increased from 201 crores in 1990-91 to 151406 crores in 2003-04. India's investment in foreign countries has increased from 19 crores in 1990-91 to 83616 crores in 2003-04. Inward foreign investments have grown more than 750 times while India's investment abroad have increased 4927 times.

Table showing inflow and outflow of foreign capital in and from India:

Year	Inflow	Outflow	Net
1990-91	201	19	182
2000-01	80824	54080	26744
2001-02	73907	41987	31920
2002-03	67756	47658	22098
2003-04	151406	83616	67592

#### Question 7. Discuss the merits and demerits of entering into joint ventures.

**Answer:** Merits of Joint Venture

1. **Less Expensive:** It is financially less expensive as local producer also makes some contribution in equity capital. Half of the capital is contributed by local producer. It reduces the burden for foreign investor.
2. **Beneficial for projects requiring Large Scale Investment:** It is beneficial for projects requiring large capital investments like construction of metro. In such projects it is generally difficult for a single investor to invest.
3. **Knowledge about host country:** Local producers provide knowledge about host country. It helps the foreign investor to establish its foot in host country.
4. **Less risky:** Risk gets reduced by involving local manufacturer. First, he makes 50% equity and thereby shares losses and other risks. Secondly, he has an understanding of taste and preferences of customers in host country, laws and culture of host country.

### Disadvantages of Joint Venture

1. **Sharing of Technology:** In joint venture, foreign firm shares technology with the local producer. It is risky. He may start a business of his own once he gets acquainted with the technology.
2. **Conflicts:** There may be conflicts in managerial decisions as there is dual ownership arrangement.

### III. Long Answer Type Questions

#### Question 1. Discuss the benefits of international business.

**Answer:** The benefits of international business to nations are as follows:

1. **Earning of Foreign exchange:** International business helps a country to earn foreign exchange. It can use it for meeting its payments abroad.
2. **Better utilization of resources:** It is based on the principle of comparative cost advantage. It implies that produces what your country can produce more efficiently, and trade the surplus production so generated with other countries to procure what they can produce more efficiently. When countries produce on these principles, it increases their resource utilization.
3. **Improving Growth Prospects and Employment Potentials:** Producing solely for the purpose of domestic consumption severely restricts a country's prospects for growth and employment.
4. **Increased Standard of Living:** In the absence of international trade of goods and services, it would not have been possible to enjoy the standard of living it is enjoying now.

**The benefits of international business to firms are as follows:**

1. **Prospects for higher profits:** International business proves more profitable as compared to domestic business. When prices in domestic market are lower, business firms can earn higher profits by selling their products in foreign countries.
2. **Increased Capacity Utilization:** Many firms set up production capacities for their products which are in excess of demand in the domestic market by planning overseas expansion and procuring orders from foreign customers. It allows them to make better use of their surplus capacity.
3. **Prospects for growth:** Business firms find it very irritating when there is fall in demand or saturation point comes in domestic market. Such firms can grow considerable prospects of their growth by entering into international business.

4. **Way out to intense competition in domestic market:** When competition in domestic market is very intense, internationalization seems to be the only way for significant growth. Highly competitive domestic market motivates many firms to enter into international business.
5. **Improved Business Vision:** The growth of international business of many companies is important for their survival and goodwill. Vision to become international is expression of urge to grow and the need to diversify and to take benefit of strategic advantages of internationalisation.

**Question.2. Discuss the scope of international business.**

**Answer.** There are many ways in which the firm's operate international major forms of business operations which constitute international business are given below:

1. **Merchandise exports and imports:** Merchandise means which are tangible. That can be seen and touched. It is also known as trading goods. It excludes trading services.
2. **Exports and Imports of Services:** Service exports and imports involve trade in intangibles. It is because of the intangible aspect of services that trade in services is termed as intangible trade.
3. **Licensing and Franchising:** Permitting another party in a foreign country to produce and sell goods under a firm's trademarks, patents or copyright for which a payment is made which is called royalty is another way of entering into international business. For example, McDonalds'.
4. **Foreign Investments:** Foreign investment is another way to operate internationally. It involves investment of funds abroad in exchange for financial return. It may take two forms:
  - **Direct Investment:** It takes place when a company directly invests in property like plant and machinery in foreign countries with a view to undertaking production and marketing of goods and services in these companies.
  - **Portfolio Investment:** It is an investment that a company makes into another company by way of acquiring shares or providing loans to the latter.

**Question 3. Licensing and franchising are suitable in different situations. Explain how?**

**Answer:** Yes, it is right to say that licensing and franchising are suitable in different situations. For a company looking to expand, franchising and licensing are often appealing business models. In a franchising model, the franchisee uses another firm's successful business model and brand name to operate what is effectively an independent branch of the company. The franchiser maintains a considerable degree of control over the operations and processes used by the franchisee, but also helps with things like branding and marketing support that aid the franchise. The franchiser also typically ensures that branches do not cannibalize each other's revenues.

Under a licensing model, a company sells licenses to other (typically smaller) companies to use intellectual property (IP), brand, design or business programs. These licenses are usually non-exclusive, which means they can be sold to multiple competing companies serving the same market. In this arrangement, the licensing company may exercise control over how its IP is used but does not control the business operations of the licensee.

Both models require that the franchisee/licensee make payments to the original business that owns the brand or intellectual property. There are laws that govern the franchising model and define what constitutes franchising; some agreements end up being legally viewed as franchising even if they were

originally drawn up as licensing agreements. It can be clarified from the differences given below:

Basis	Franchising	Licensing
Governed by	Securities Law	Contract Law
Registration	Required	Not required
Territorial rights	Offered to franchisee	Not offered; licensee can sell similar licenses and products in same area
Support and training	Provided by franchiser	Not provided
Royalty payments	Yes	Yes
Use of trademark/Logo	Logo and trademark retained by franchiser and used by franchisee	Can be licensed
Examples	McDonalds, Subway, 7-11, Dunkin Donuts	Microsoft Office
Control	Franchiser exercises control over franchisee.	Licensor does not have control over licensee.

#### Question 4. Discuss meaning, merits and demerits of contract manufacturing.

**Answer:** Contract manufacturing refers to type of international business where a firm enters into contract with some local manufactures in foreign countries to get certain components of goods produced as per their specifications. It is also called outsourcing. It can take three forms: Getting produced certain parts of final products which will be used for the production of final products later; assembly of components into final products; and complete manufacture of the products like garments.

#### Merits of Contract manufacturing

1. **Less investment:** It helps international firms in production of goods at massive scale without making any investment in setting up production facilities. Therefore, it is more suitable for small and medium size manufacturers who can't undertake 100% or even 50% investment.
2. **Less risky:** It is less risky as there is little investment involved. Moreover, local manufacturers who have been given specific product design and quality standards do not deviate from them.
3. **Low cost:** If goods are contracted in low labour and material cost country, then it also gives benefit of low cost. For example, in India labour is very cheap and therefore it has become a favorite destination for contract manufacturing.
4. **Better capacity utilization:** Local producers benefit get from contract manufacturing because it allows them to make better use of their idle production capacity.
5. **An opportunity for local producers to become international:** Local producer also gets an opportunity to get involved in international business.

#### Disadvantages of Contract Manufacturing

1. **Deviations from Product design and quality Specifications:** Local firms might not follow product design and quality standards causing serious product quality problems for international firm.



2. **Loses control over Manufacturing Process:** Local manufacturer in the foreign country loses control over manufacturing process.
3. **No authority to sell output:** The local firm cannot sell the output according to his will. It has to sell the goods to international firm at pre-determined prices.

**Question 5. State the important changes being observed in composition of India's external trade since 2007-08.**

**Answer:** Till 1980's exports were mainly of primary goods, viz. agricultural commodities and raw materials, such as minerals. Over time, the role of manufactures including engineering goods has been increasing. Share of manufactured goods is 66 % of total exports, of which engineering goods contribute 27 % of the value of goods exported. Composition of India's external trade since 2007-08 is shown below:

**India's Exports and Imports (US\$ billion).**

	2007-08	% share	2010-11	% share
<b>Exports</b>				
(1) Primary Products	27.55	16.91	35.35	13.89
(a) Agricultural and allied	18.43	11.31	24.69	9.70
(b) Ores and minerals	9.11	5.59	10.66	4.19
(2) Manufactured Goods	102.97	63.21	168.09	66.07
(a) Leather and Manufactures	3.50	21.48	3.78	1.48
(b) Chemicals and related items	21.19	13.00	28.79	11.31
(c) Engineering goods	19.42	11.92	23.31	9.16
(d) Textiles and products	19.42	11.92	23.31	9.16
(e) Gems and jewellery	19.67	12.07	40.79	16.03
(f) Handicrafts	0.50	0.30	0.23	0.09
(3) Petroleum products	28.36	17.40	41.91	16.47
Total exports	162.90		254.40	
(1) Bulk imports	112.74	44.83	150.48	42.60
(a) Petroleum	79.64	31.67	106.06	30.08
(2) Non-bulk Imports	138.69	55.16	202.08	57.31
(a) Capital goods	70.11	27.88	71.62	20.31
(b) Mainly export related	20.76	8.25	49.63	14.07
Total Imports	251.43		352.57	

**Source:** RBI, Annual Report, 2010-11, Appendix Table 17, p. 186.

**Question 6. "Wholly owned subsidiary is a more investing, more risky and less return giving venture." Do you agree? Substantiate your answer.**

**Answer:** I agree to the statement partially. Wholly owned subsidiary is a more investing, more risky and more return giving venture. In this the parent company acquires the full control over the foreign company by purchasing its 100% equity capital. It can be established in two ways: first as a green field venture, in which an altogether a new firm is set up to start operations in a foreign existing firm in foreign country and using it for manufacturing and promoting its products in home country.

**Merits of Wholly Owned Subsidiaries**

1. **Complete control over operations:** The parent firm is able to exercise full control over its operations in foreign countries because it has 100% equity holding in the company.
2. **No need to disclose technology:** It is less risky as 100% investment is made by parent company and hence there is no need to disclose technology to local producers.

### Demerits of Wholly Owned Subsidiaries

1. **100% Investment and hence require more funds:** The parent company needs to make 100% equity investment and therefore requires huge funds.
2. **More risky:** It is more risky as parent company has 100% equity investment; it has to bear all the losses, if any.
3. **Government rules and regulations:** Some countries do not allow establishing 100% wholly owned subsidiaries in their countries.

### Question 7. How is home trade different from external trade?

**Answer:** Internal trade takes place between the geographical boundaries of a nation, whereas international trade takes place between different nations.

1. In the trade of any nation, the volume of its internal trade will be more than that of external trade. Internal trade accounts for about 95% of the total volume of the trade of a country, whereas foreign trade accounts for only about 5% of the total volume of the trade of a country.
2. Though both internal trade and international trade are based on the principle of specialization or division of labour, regional specialization within a country leads to internal trade or inter-regional trade, whereas country wise specialization leads to international trade.
3. In the case of home trade, there is much scope for the operation of forces of demand and supply. But, in the case of foreign trade, there is not much scope for the full operation of the forces of demand and supply.
4. The number of documents of trade required for home trade is less than the required for foreign trade.
5. Home trade is subject to regulations and laws of only one country, whereas foreign trade is subject to regulations and laws of two or more countries.
6. Home trade is, generally, free from restrictions, whereas foreign trade is subject to a number of restrictions.
7. The cost of transport in home trade is much less than that in foreign trade.
8. The interval between the dispatch of goods by the seller and the receipt of the same by the buyer in home trade is not much.
9. Goods are subject to greater risk in foreign trade than in home trade.
10. As goods are subject to more risks in foreign trade, in the case of international trader, goods are, generally, insured against the risks.
11. Home trade involves the currency of only one country whereas foreign trade involves the currencies of two or more countries.

### IV. Higher Order Thinking Skills (HOTS)

#### Question 1. "Foreign trade is not free from difficulties." Comment.

**Answer:** Foreign trade is not free from difficulties. The following are some of the important difficulties of foreign trade:

1. It is a long distance trade and as such it becomes difficult to maintain close relationship between the buyer and the seller.

2. Each country has its own language. As foreign trade involves trade between two or more countries, there is diversity of languages. This difference in language creates problem in foreign trade,
3. Foreign trade involves preparation of a number of documents which also creates difficulties in the way of foreign trade.
4. Some restrictions are imposed on export and import of commodities. These restrictions stand on the progress of foreign trade.
5. Foreign trade involves a great deal of risks because trade takes place over a long distance. Though the risks are covered through insurance, it involves extra cost of production because insurance cost is added to cost.

**Question 2. “International trade benefits both the parties involve.” Do you agree?**

**Justify your answer:**

**Answer.** No doubt, trade benefits both the parties involved. These gains can be categorised as static and dynamic.

**Static gains from trade:**

1. If a country has an absolute or relative advantage in the production of some goods, it can specialize in those goods and can trade it for others. It will increase total productivity.
2. Increase in imports will increase country's ability to satisfy consumer needs. Imports of capital goods may also increase the economic growth rate in the initial stages. It may also shift economy closer to its production possibility curve indicating relatively fuller utilization of resources.
3. Specialization based on comparative advantage will result more efficient utilization of resources. Hence, a labour abundant country will expand those industries which use more of labour. It will stimulate employment and wage rates will go up.
4. According to Myint, international trade can provide a larger market for developing countries that will help these countries to increase their output and employment and hence, they will shift closer to PPC and real output will increase.
5. Trade brings various nations closer and interlinks the economies of the world. It helps to learn from each other's experience and sharing of capital, technology and knowhow also increases.

**Negative static effects of trade:**

1. An economy which specialises in labour intensive industries at the cost of modern sector may face problems. It is so because the products of these industries have low price elasticities of demand and supply of agriculture and primary goods is quite instable.
  2. Large chunks of stock will lead to unfavorable terms of trade for the country. It may reduce the benefits expected from trade.
  3. Specializing in labour intensive industries and relying on developed nations for modern machinery and commodities is not advisable on the principle of prudence.
  4. Since there is huge unemployment in developing countries, increased demand for labour will not increase wage rate so much.
  5. Since there are inflexibilities in traditional economies, the expected gains from trade do not get realized. Rather trade benefits developed countries more and thereby increases the inequalities of income amongst nations.
- Dynamic gains from trade:

**Dynamic positive effects:**

1. When economy operates at a larger scale with access to the markets of other countries, it can avail of economies of scale which otherwise will not be available.  
Economies of large scale will make these countries more competitive in international market.
2. International trade gives\*an exposure to world market and international technology of production which a closed economy can not have. It helps an under developed country to grow at a fast pace and become more competitive.
3. There are many other dynamic changes that occur in the economy via trade like increased investment due to better economic environment, approach to world class technology, institutional changes, exposure to new and different products.

### Dynamic negative effects:

1. Market imperfections may increase social costs. Hence, trade that considers only private costs may not be consistent with the long term development goals.
2. The overall effect of exports will vary from industry to industry; sector to sector. Some industries may get benefit more than others.
3. If increasing returns to scale are available for some commodity, it may lead to higher profits through exports rather than one in which decreasing returns to scale are expected. Hence, returns to scale may complicate the judgment whether exports are benefiting or not.
4. Existence of imperfection in markets and government policies may adversely affect the expected dynamic gains.
5. Many a time, trade benefits developed countries more than developing ones. In such a situation, it may worsen the relative economic strength of developing nations.

### V. Value Based Questions

**Question 1. Which mode of international business should be chosen by a small business man and why?**

**Answer:** A small business should consider following factors in selecting mode of entering into international business.

1. **Ease of entry:** First and foremost factor that determines the choice of mode of entry into international business is ease of entry. A businessman wants to adopt such mode of entry into international business which is easy and less formalities requiring. Exporting, importing, licensing and franchising are better ways from this perspective.
2. **Cost:** Second determining factor is cost involved. For example, very less cost is involved in exporting, importing, licensing, franchising and contract manufacturing as compared to joint ventures and setting wholly owned subsidiaries.
3. **Control over production:** If the foreign company or producer wants full control over production activities in local country, he will prefer franchising, wholly owned subsidiary or joint venture with majority share holding. If it is not so important, he will prefer exporting, importing, contract manufacturing licensing etc.
4. **Sharing of Technology:** If the company has no problem in sharing of technology then it may choose joint venture or franchising. But if it does not want to share its technology and trade secrets, it will prefer wholly owned subsidiary or exporting.
5. **Risk Involved:** If a firm is ready to take risk, it may choose wholly owned subsidiary or joint ventures but if it is willing to minimise its loss then it should choose exporting, licensing, franchising or contract manufacturing.

In my opinion, being a small businessman he will prefer exporting or licensing, franchising to other modes of business as it is easy, less costly, gives greater control over production and involves lesser risk.



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### **International Business 2**

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International Business 2

#### **I. Multiple Choice Questions**

**Question 1.** In which of the following modes of entry, does the domestic manufacturer give the right to use intellectual property such as patent and trademark to a manufacturer in a foreign country for a fee

- (a) Licensing (b) Contract manufacturing  
(c) Joint venture (d) None of these

**Question 2.** Outsourcing a part of or entire production and concentrating on marketing operations in international business is known as

- (a) Licensing (b) Franchising  
(c) Contract manufacturing (d) Joint venture

**Question 3.** When two or more firms come together to create a new business entity that is legally separate and distinct from its parents it is known as

- (a) Contract manufacturing (b) Franchising  
(c) Joint ventures (d) Licensing

**Question 4.** Which of the following is not an advantage of exporting?

- (a) Easier way to enter into international markets  
(b) Comparatively lower risks  
(c) Limited presence in foreign markets  
(d) Less investment requirements

**Question 5.** Which one of the following modes of entry requires higher level of risks?

- (a) Licensing (b) Franchising  
(c) Contract manufacturing (d) Joint venture

**Question 6.** Which one of the following modes of entry permits greater degree of control over overseas operations?

- (a) Licensing/franchising (b) Wholly owned subsidiary  
(c) Contract manufacturing (d) Joint venture

**Question 7.** Which one of the following modes of entry brings the firm closer to international markets?

- (a) Licensing (b) Franchising  
(c) Contract manufacturing (d) Joint venture

**Question 8.** Which one of the following is not amongst India's major export items?

- (a) Textiles and garments (b) Gems and jewellery  
(c) Oil and petroleum products (d) Basmati rice

**Question 9.** Which one of the following is not amongst India's major import items?

- (a) Ayurvedic medicines (b) Oil and petroleum products  
(c) Pearls and precious stones (d) Machinery

**Question 10.** Which one of the following is not amongst India's major trading partners?

- (a) USA (b) UK  
(c) Germany (d) New Zealand

**Answer:**

1. (a) 2. (c) 3. (c) 4. (a) 5. (c)
6. (b) 7. (c) 8. (d) 9. (b) 10. (d)

## II. Short Answer Type Questions

### Question 1. Differentiate between international trade and international business.

**Answer:** Difference between international trade and international business is similar to difference between trade and business.

1. The scope of international business is much wider than international trade. International trade means exports and imports of goods which is an important component of international business but international business includes much more than this.
2. International trade in services like travel and tourism, transportation, communication, banking, warehousing, distribution and advertising is a part of international business.
3. International business also includes foreign direct investments, contract manufacturing, and setting up wholly owned subsidiaries etc. which are not included in international trade.

### Question 2. Discuss any three advantages of international business.

**Answer:** The following are some of the advantages of foreign trade:

1. **Optimum use of resources:** Foreign trade helps in the optimum use of natural resources and avoids wastage's of resources. It ensures the presence of stable price by avoiding wide fluctuations in prices. It tries to equalise the world price.
2. **Increased standard of living:** It ensures more production to meet the demand of the people of different countries. By increased production, it becomes possible to increase income and the standard of living of its people. It also increases the standard of living by increasing more employment opportunities. It enables a country to import those goods which it cannot produce.
3. **Large scale production:** It ensures large production because the production is carried on to meet the demand of its people as well as world market. Large scale production also ensures a great deal of internal economies which reduces the cost of production.

### Question.3. What is the major reason under lying trade between nations?

**Answer.** The major reason behind international business is that the countries cannot produce equally well or cheaply all the commodities. This is called theory of comparative cost advantage. It is so because resources are unequally distributed in natural resources. Some countries are abundant in one commodity and scarce in others while opposite is true for some other country. It makes a case for international trade and exchanging abundant commodity with scarce commodity by nations. Different nations are endowed with different factors of production which includes land, labour, capital and entrepreneurship. For example, India is a labour abundant country. Therefore, it is advisable for India to produce such commodities which use labour intensive methods and exchange it for those which use capital intensive methods. USA is a capital abundant country. Therefore, nations need to trade. Due to these reasons one country has a comparative advantage in production of particular goods as compared to other countries. Consequently, each country finds it advantageous to produce those selected goods and services that it can produce more effectively at home and importing those goods in which other nations have a comparative cost advantage.

### Question 4. Discuss as to why nations trade.

**Answer:** Nations trade because of following reasons:

1. **Unequal distribution of natural resources:** Resources are unequally distributed in natural resources. Some countries are abundant in one commodity and scarce in other while opposite is true for some other country. It makes a case for international trade and exchanging abundant commodity with scarce commodity by nations.
2. **Unequal availability of factors of production:** Different nations are endowed with different factors of production which includes land, labour, capital and entrepreneurship. For example, India is a labour abundant country. Therefore, it is advisable for India to produce such commodities which use labour intensive methods and exchange it for those which use capital intensive methods. USA is a capital abundant country. Therefore, nations need to trade.
3. **Theory of Comparative Cost Advantage:** Due to these factors, some countries are in an advantageous position in producing selected goods and services which other countries cannot produce that effectively and efficiently and vice-versa. Consequently, each country finds it advantageous to produce those selected goods and services that it can produce more effectively at home and importing those goods in which other nations have a comparative cost advantage.
4. **Geographical Specialisation:** The international business as it exists today is the result of geographical specialisation. Even within a country each state specialises in those goods for which it is geographically more suitable. Similarly, each nation specialises in those goods in which it is specialised as per availability of resources and exchanges it for other goods and services in foreign market.
5. **Cost minimization principle of firms:** Firms get involved in international business to minimise their costs and maximise their profits.

**Question 5. Enumerate limitations of contract manufacturing.**

**Answer:** Major limitations of contract manufacturing are discussed below:

1. **Non adherence to quality standards:** Local firms may not adhere to quality standards or product design. It may cause serious quality problems for international firm. .
2. **No control on production by local producer:** Local producer has no control on manufacturing as goods are manufactured strictly as per the terms and specifications by international firm.
3. **Zero control over sales:** Local producer can't sell the output to customers directly. He needs to sell to the international firm at a pre-determined price. It reduces profits of local firm.

**Question 6. Why is it said that licensing is an easier way to expand globally?**

**Answer:** It is said that licensing is an easier way to expand globally because of its advantages over other modes of international business.

1. **Less Expensive:** Under the licensing, it is the licensee who sets up the business unit. Therefore, licensor has to invest no money. Therefore, it is considered as a cheaper way of entering\*into international business.
2. **Zero Risk of Loss:** Licensor need not take pain of risk of profits and loss. He is paid a pre-determined fees called royalty by the licensee. As long as licensor continues to produce under the license, licensor keeps on getting his fees irrespective of whether licensee is making profits or incurring losses.
3. **Less risk of government intervention or takeovers:** A local person handles the business in foreign country. Therefore, there are lesser chances of government intervention or takeovers.
4. **Better knowledge of local needs:** Since licensee is the local person, he has better understanding of local needs, marketing strategies and business environment.

5. **Safety of Intellectual Property Rights:** As per the terms of the licensing, only licensee can make use of licensor's copyrights, patents and brand names in foreign countries. Therefore, there is lesser risk of these intellectual property rights being missed by other local firms.

**Question 7. Differentiate between contract manufacturing and setting up wholly owned production subsidiary abroad.**

**Answer:** The difference between contract manufacturing and wholly owned subsidiary is discussed below:

Basis	Contract Manufacturing	Wholly Owned Subsidiary
Meaning	It refers to the type of international business where a firm enters into contract with some local manufactures in foreign countries to get certain components of goods produced as per their specifications.	In this the parent company acquires the full control over the foreign company by purchasing its 100% equity capital.
Forms	It can take three forms: (a) Getting produced certain parts of final products which will be used for the production of final products later. (b) Assembly of components into final products. (c) Complete manufacture of the products like garments.	It can be established in two ways: (a) As a green field venture, in which an altogether a new firm is set up to start operations in a foreign country. (b) Acquiring an existing firm in foreign country and using it for manufacturing and promoting its products in home country.

**Question 8. Distinguish between licensing and franchising.**

**Answer:**

Basis	Licensing	Franchising
Meaning	Licensing is a contractual agreement in which one firm grants access to its patents, trade secrets, technology to another firm in a foreign country for a fee. This fee is called royalty.	Franchising is basically a specialized form of licensing in which franchisor sells intangible property to the franchisee but also imposes strict rules on franchisee as to how business is to be done.



Connected with	Licensing is used in connection with production and marketing of goods.	The term franchising is used in connection with production of services.
Stringency	Licensing is relatively less stringent than franchising. Strict rules and regulations are not set by licensors as to how licensees should operate while running their business.	Franchising is relatively more stringent than licensing. Strict rules and regulations are set by franchisers as to how franchisees should operate while running their business.

**Question 9. List major items of India's import.**

**Answer:** India's major items of imports include crude oil and petroleum products, capital goods, electronic goods, pearls, precious and semi precious stones, gold, silver and chemicals.

**Question 10. What are the major items that are exported from India?**

**Answer:** India's major items of exports include textiles, garments, gems and jewellery, engineering products and chemicals, agriculture and allied products.

**Question 11. List the major countries with whom India trades.**

**Answer:** India's major trading partners are USA, UK, Germany, Japan, Belgium, Hong Kong, UAE, China, Switzerland, Singapore and Malaysia.

**III. Long Answer Type Questions**

**Question 1. What is international business? How is it different from domestic business?**

**Answer:** International business refers to business which is carried on in two or more nations. It means carrying on business activities beyond national boundaries. These activities normally include the transaction of economic resources such as goods, capital, services (comprising technology, skilled labour, and transportation, etc.), and international production. It refers to that business activity that takes place beyond the geographical limits of a country. Production may either involve production of physical goods or provision of services like banking, finance, insurance, construction, trading, and so on. Thus, international business includes not only international trade of goods and services but also foreign investment, especially foreign direct investment.

Differences between International Business and Domestic Business are summarised below:

Basis	International Business	Domestic Business
Nationality of buyers and Sellers	People of different nationality participate in international business.	People of one nationality participate in domestic business. Exceptions are possible.
Nationality of other stakeholders	Employees, suppliers, customers, shareholders, partners, middlemen etc. belong to different nationality in international business.	Employees, suppliers, customers, shareholders, partners, middlemen etc. belong to same nationality in domestic business. Exceptions are possible.
Political Systems	International business is subject to political system of many nations.	Domestic business is subject to political system of one country.

Risk	Degree of risk is higher in international business.	Degree of risk is lower as compared to international business.
Mobility of factors of production	Mobility of factors of production is less across countries.	Mobility of factors of production is more within geographical boundaries of the country.
Consumer's taste and preferences	International markets are heterogeneous in terms of taste and preferences of the customer.	Domestic markets are more homogeneous in terms of taste and preferences of the consumer.
Currency	International business involves usage of foreign currency.	Domestic business makes use of domestic currency.
Business regulations and policy	International business is subject to rules laws, policies, and taxation system etc of multiple countries.	Domestic business is subject to rules, laws, policies, and taxation system etc of single country.
Differences in business systems and practices.	Business systems and policies are heterogeneous in two countries.	Business system and policies are more homogeneous within a country.

**Question 2. “International business is more than international trade”. Comment.**

**Answer:** It is rightly said that international business is more than international trade. The scope of international business is much wider than international trade. International trade means exports and imports of goods which is an important component of international business but international business includes much more than this. International trade in services like travel and tourism, transportation, communication, banking, warehousing, distribution and advertising is a part of international business. International business also includes foreign direct investments, contract manufacturing, and setting up wholly owned subsidiaries etc. which are not included in international trade. It is clear from the diagram given below:



**Question 3. What benefits do firms derive by entering into international business?**

**Answer:** The trade between two or more nations is termed as foreign trade or international trade. It involves exchange of goods and services between the trades of two countries. Foreign trade consists of import trade, export trade and entrepot trade. In the early stages of human civilization, production was confined as per consumption. Human wants were limited. Nowadays, human wants are increasing and as such no man was considered to be self-dependent. Like this no country can live in isolation and claimed the status to be self-sufficient. Because of this reason countries have trade

relationships with each other. The primary objective of foreign trade is to increase foreign trade and increase the standard of living of its people. There is an increasing demand for foreign trade because of the following reasons:

1. The natural resources are unevenly distributed.
2. The presence of specialisation and division of labour.
3. Different countries have difference in economic growth rate.
4. The presence of the theory of comparative cost.

The following are some of the advantages of foreign trade:

1. **Optimum use of Resources:** Foreign trade helps in the optimum use of natural resources and avoids wastages of resources.
2. **Stable Price:** It ensures the presence of stable price by avoiding wide fluctuations in prices. It tries to equalise the world price.
3. **Availability of all types of goods:** It enables a country to import those goods which it cannot produce.
4. **Increased Standard of living:** It ensures more production to meet the demand of the people of different countries. By increased production, it becomes possible to increase income and the standard of living of its people. It also increases the standard of living by increasing more employment opportunities.
5. **Large Scale production:** It ensures large production because the production is carried on to meet the demand of its people as well as world market. Large scale production also ensures a great deal of internal economies which reduces the cost of production.

**Question 4. In what ways is exporting a better way of entering into international markets than setting up wholly owned subsidiaries abroad.**

**Answer:** Exporting is a better way of entering into international markets than setting up wholly owned subsidiaries abroad in following ways:

1. **Easiest Way:** It is easy to enter international markets through exports as compared to wholly owned subsidiaries.
2. **Less Involving:** It is less involving as compared to establishing a wholly owned subsidiary because firms need not invest that much time and money.
3. **Zero risk of Foreign Investment:** Exporting does not require much of investment in foreign countries. Therefore, foreign investments risks are low as compared to when a firm starts its wholly owned subsidiary in foreign country.
4. **Less Costly:** In a wholly owned subsidiary, 100% equity investment is to be made by foreign company. Therefore, small and medium size producers can't think of this mode of entering into international business.
5. **Risk of Profit and Loss:** In wholly owned subsidiary, 100% equity capital is contributed by foreign company alone. Therefore, it alone has to bear the risk of losses.
6. **Government Intervention:** Some countries are averse to setting up of 100% wholly owned subsidiaries by foreign companies. This form of business operations is subject to high degree of political risks.

**Question 5. Discuss briefly the factors that govern the choice of mode of entry into international business.**

**Answer:** Following factors govern the choice of mode of entry into international business,



1. **Ease of entry:** First and foremost factor that determines the choice of mode of entry into international business is ease of entry. A businessman wants to adopt such mode of entry into international business which is easy and less formalities requiring. Exporting, importing, licensing and franchising are better ways from this perspective.
2. **Cost:** Second determining factor is cost involved. For example, very less cost is involved in exporting, importing, licensing, franchising and contract manufacturing as compared to joint ventures and setting wholly owned subsidiaries.
3. **Control over production:** If the foreign company or producer wants full control over production activities in local country, he will prefer franchising, wholly owned subsidiary or joint venture with majority share holding. If it is not so important, he will prefer exporting, importing, contract manufacturing licensing etc.
4. **Sharing of Technology:** If the company has no problem in sharing of technology then it may choose joint venture or franchising. But if it does not want to share its technology and trade secrets, it will prefer wholly owned subsidiary or exporting,
5. **Risk Involved:** If a firm is ready to take risk, it may choose wholly owned subsidiary or joint ventures but if it is willing to minimize its loss then it should choose exporting, licensing, franchising or contract manufacturing.

**Question 6. Discuss the major trends in India's foreign trade. Also list the major products that India trades with other countries.**

**Answer:** India is 10th largest economy in the world. It is the second fastest growing economy, next only to China. But India's performance in international business is not very good. India's share in world trade in 2003 was just 0.8%. In absolute terms, there has been significant increase in imports as well as exports. Total exports have increased from 606 crores in 1950-51 to Rs. 2, 93,367 crores in 2003-04 while imports have increased from 608 crores in 1950-51 to 3, 59,108 crores in 2003-04. Exports increased 480 times while imports increased 590 times indicating that there is adverse balance of trade. India's major trading partners are USA, UK, Germany, Japan, Belgium, Hong Kong, UAE, China, Switzerland, Singapore and Malaysia.

India's major items of exports include: Textiles, garments, gems and jewellery, engineering products and chemicals, agriculture and allied products.

India's major items of imports include: Crude oil and petroleum products, capital goods, electronic goods, pearls, precious and semi precious stones, gold, silver and chemicals.

Before 1991, promotion of import substitution and discouraging of exports was government strategy. Imports consisted of machinery, equipment and intermediates in production, petroleum and petroleum-products. After green revolution, imports of fertilizer too increased.

Before 1991, India's exports consisted of agricultural products like tea, raw cotton with the diversifying industrial structure, promoted by import substitution, exports of manufactures were growing. During 1986-91, external trade formed only 13.40 % of the GDP. During the 1990-2000, this share is rising continuously.

India's foreign trade has grown to exports of \$250 billion and imports of \$380 billion in 2010-11. The ratio of exports plus imports to GDP has grown from 13.40 % during 1985-90 to almost three times that, being 37.7 % in 2010-11. On adding services it becomes from 22.9 % in the 1990s to 49.0 % in 2010-11.

Leading role has been played by 'invisibles' which includes both services, mainly software services, export of which has grown to \$59 billion in 2010-11. It has decreased the current account deficit from \$130 billion to \$44. This deficit was compensated by capital account surplus of \$59 billion in that year.

But it is only because of IT services and we are still lacking in manufacturing exports which can generate a large volume of employment. We have not done as well as China and Malaysia have done.



**Question 7. What is invisible trade? Discuss salient aspects of India's trade in services.**

**Answer:** Trade in services is called invisible trade. Since services are invisible, export and import of services has been named as invisible trade. In absolute terms, there has been significant increase in India's foreign trade in services. Export and import of foreign travel, transportation and insurance has largely increased during last four decades. There has been a change in composition of services exports. Software and other miscellaneous services have emerged as the main categories of India's export of services. Share of travel and transportation has declined to 29.6% in 2003-04 from 64.3% in 1995-96 while the share of software exports has increased from 10.2% in 1995-96 to 49% in 2003-04.

**Table showing Percentage share of major services to total services exports**

Sector/Year	1995-96	2000-01	2001-02	2002-03	2003-04
Travel	36.9	21.5	18.3	16.0	16.5
Transportation	27.4	12.6	12.6	12.2	13.1
Software	10.2	39.0	44.1	46.2	48.9
Miscellaneous	22.9	21.3	20.3	22.4	18.7

The composition of India's external trade has been changing. During 1950s and 60s exports were mainly of primary goods. Over time, the role of engineering goods has been increasing. Overall manufactured goods constitute 66 % of total exports, of which engineering goods are 27%. Textiles and textile products, garments and leather products make around 10 % of India's exports.

In nutshell, we can say that the role of the external or internationally traded goods sector has been growing steadily in Indian economy. At present imports and exports together account for upto 49 % of India's GDP which was 18% in 1990s. In India there is greater share of exports of services which are IT software services, called IT- enabled services (ITES). It contributed more than 20% of India's export earnings. India accounts for about 45% of the world's BPO services. The major Indian IT companies, TCS, Infosys and Wipro, initiated and perfected the Global Services Delivery (GSD) model. It is because India has a vast pool of software engineers and an even bigger pool of English-knowing staff. With growing competition in the market for such services, Indian companies have moved from BPO to Knowledge Process Outsourcing (KPO), which involves providing services for R and D and to high-end consulting.

## **MORE QUESTIONS SOLVED**

### **I. Very Short Answer Type Questions**

**Question 1. Out of international trade and international business which one is wider in scope?**

**Answer:** International business

**Question 2. What is the basic reason behind international trade?**

**Answer:** Comparative cost advantage in production of some goods.

**Question 3. Give one point of difference between licensing and franchising.**

**Answer:** Licensing is used for goods and franchising is used for services.

**Question 4. When a middleman is involved in handling export procedure, then it is called by what name?**

**Answer:** Indirect exporting

**Question 5. Licensee or franchisee pays a fee to licensor or franchisor. What is it called?**

**Answer:** Royalty.

**Question.6. Reebok orders for footballs to local manufacturers of Ludhiana and then sells it all over the world. It is an example of what?**

**Answer:** Contract manufacturing.

**Question 7. Name the country whose share is largest in India's exports and imports.**

**Answer:** USA

**Question 8. What is the share of India's exports in world exports?**

**Answer:** 0.8%

**Question 9. Which service has got dominating share in foreign trade in services?**

**Answer:** Software and Miscellaneous

**Question 10. India is\_ largest economy in the world.**

**Answer:** 10th

## **II. Short Answer Type Questions**

**Question 1. Define international business.**

**Answer:** According to Roger Beneett, "International business involves commercial activities that cross national frontiers."

In the words of John D Daniels and Lee H Radebough, "International business is all about business transactions—private and governmental that involve two or more countries. Private companies undertake such transactions for profits; government may or may not do the same in their transactions."

According to Michael R Czinkota, "International business consists of transactions that are devised and carried out across national borders to satisfy the objectives of the individuals, companies and organizations. These transactions take on various forms which are often correlated."

**Question 2. Explain different forms of Joint Ventures.**

**Answer:** A joint venture refers to establishing a firm which is jointly owned by two or more independent firms. It can be entered into three ways:

1. A foreign investor may buy interest in a local company
2. Local firm may acquire an interest in an existing foreign firm.
3. Both local and foreign firms jointly establish a new enterprise.

**Question 3. Explain different forms of contract manufacturing.**

**Answer:** Contract manufacturing can take three forms:

1. **Getting produced certain parts of final products:** In case of automobiles or purses or shoes some parts are got manufactured from foreign countries which are used for the production of final products later.

2. **Assembly of components into final products:** In case of electronic items, different parts are assembled at that country where they are to be sold.
3. **Complete manufacture of the products:** In some cases, commodities like garments a contract is given for complete manufacturing and products are sold in brand name of foreign companies.

#### Question 4. India embarks on the path of globalisation. Comment

**Answer:** Since 1991, with the announcement of New Economic Policy, 1991 India also embarks on the path of globalisation. India was facing a severe financial crisis. It approached International Monetary Fund and World Bank for help. IMF agreed to lend money to India on the condition that India will introduce structural changes in its economy. As a result, India announced the policy of LPG i.e. Liberalisation, Privatisation and Globalisation. Then on 1 January, 1995 WTO was formed. India became founder member of WTO and thereby was under a compulsion to follow rules and regulations of WTO. Therefore, it had to open up its economy for rest of the world and they also allowed India to enter their markets. Though the process of reforms has somewhat slowed down, India is very much on the path of globalisation.

#### Question 5. What are the benefits of international trade to firms?

**Answer:** Given below are benefits of international business for firms:

1. **Prospects for higher profits:** It creates better prospects for higher profits.
2. **Increased capacity utilisation:** It leads to better utilisation of capacity.
3. **Prospects for growth:** It creates better prospects for growth.
4. **Way out to intense competition in domestic market:** International business acts as an alternate when there is intense competition in domestic market.
5. **Improved business vision:** When a business firm acts globally, it gives it an improved business vision.

#### Question 6. Write a short note on India's foreign investments.

**Answer:** There has been a phenomenal increase in foreign capital inflow and outflow. Inward foreign investments have increased from 201 crores in 1990-91 to 151406 crores in 2003-04. India's investment in foreign countries has increased from 19 crores in 1990-91 to 83616 crores in 2003-04. Inward foreign investments have grown more than 750 times while India's investment abroad have increased 4927 times.

Table showing inflow and outflow of foreign capital in and from India:

Year	Inflow	Outflow	Net
1990-91	201	19	182
2000-01	80824	54080	26744
2001-02	73907	41987	31920
2002-03	67756	47658	22098
2003-04	151406	83616	67592

#### Question 7. Discuss the merits and demerits of entering into joint ventures.

**Answer:** Merits of Joint Venture

1. **Less Expensive:** It is financially less expensive as local producer also makes some contribution in equity capital. Half of the capital is contributed by local producer. It reduces the burden for foreign investor.
2. **Beneficial for projects requiring Large Scale Investment:** It is beneficial for projects requiring large capital investments like construction of metro. In such projects it is generally difficult for a single investor to invest.
3. **Knowledge about host country:** Local producers provide knowledge about host country. It helps the foreign investor to establish its foot in host country.
4. **Less risky:** Risk gets reduced by involving local manufacturer. First, he makes 50% equity and thereby shares losses and other risks. Secondly, he has an understanding of taste and preferences of customers in host country, laws and culture of host country.

### Disadvantages of Joint Venture

1. **Sharing of Technology:** In joint venture, foreign firm shares technology with the local producer. It is risky. He may start a business of his own once he gets acquainted with the technology.
2. **Conflicts:** There may be conflicts in managerial decisions as there is dual ownership arrangement.

### III. Long Answer Type Questions

#### Question 1. Discuss the benefits of international business.

**Answer:** The benefits of international business to nations are as follows:

1. **Earning of Foreign exchange:** International business helps a country to earn foreign exchange. It can use it for meeting its payments abroad.
2. **Better utilization of resources:** It is based on the principle of comparative cost advantage. It implies that produces what your country can produce more efficiently, and trade the surplus production so generated with other countries to procure what they can produce more efficiently. When countries produce on these principles, it increases their resource utilization.
3. **Improving Growth Prospects and Employment Potentials:** Producing solely for the purpose of domestic consumption severely restricts a country's prospects for growth and employment.
4. **Increased Standard of Living:** In the absence of international trade of goods and services, it would not have been possible to enjoy the standard of living it is enjoying now.

**The benefits of international business to firms are as follows:**

1. **Prospects for higher profits:** International business proves more profitable as compared to domestic business. When prices in domestic market are lower, business firms can earn higher profits by selling their products in foreign countries.
2. **Increased Capacity Utilization:** Many firms set up production capacities for their products which are in excess of demand in the domestic market by planning overseas expansion and procuring orders from foreign customers. It allows them to make better use of their surplus capacity.
3. **Prospects for growth:** Business firms find it very irritating when there is fall in demand or saturation point comes in domestic market. Such firms can grow considerable prospects of their growth by entering into international business.



4. **Way out to intense competition in domestic market:** When competition in domestic market is very intense, internationalization seems to be the only way for significant growth. Highly competitive domestic market motivates many firms to enter into international business.
5. **Improved Business Vision:** The growth of international business of many companies is important for their survival and goodwill. Vision to become international is expression of urge to grow and the need to diversify and to take benefit of strategic advantages of internationalisation.

**Question.2. Discuss the scope of international business.**

**Answer.** There are many ways in which the firm's operate international major forms of business operations which constitute international business are given below:

1. **Merchandise exports and imports:** Merchandise means which are tangible. That can be seen and touched. It is also known as trading goods. It excludes trading services.
2. **Exports and Imports of Services:** Service exports and imports involve trade in intangibles. It is because of the intangible aspect of services that trade in services is termed as intangible trade.
3. **Licensing and Franchising:** Permitting another party in a foreign country to produce and sell goods under a firm's trademarks, patents or copyright for which a payment is made which is called royalty is another way of entering into international business. For example, McDonalds'.
4. **Foreign Investments:** Foreign investment is another way to operate internationally. It involves investment of funds abroad in exchange for financial return. It may take two forms:
  - **Direct Investment:** It takes place when a company directly invests in property like plant and machinery in foreign countries with a view to undertaking production and marketing of goods and services in these companies.
  - **Portfolio Investment:** It is an investment that a company makes into another company by way of acquiring shares or providing loans to the latter.

**Question 3. Licensing and franchising are suitable in different situations. Explain how?**

**Answer:** Yes, it is right to say that licensing and franchising are suitable in different situations. For a company looking to expand, franchising and licensing are often appealing business models. In a franchising model, the franchisee uses another firm's successful business model and brand name to operate what is effectively an independent branch of the company. The franchiser maintains a considerable degree of control over the operations and processes used by the franchisee, but also helps with things like branding and marketing support that aid the franchise. The franchiser also typically ensures that branches do not cannibalize each other's revenues.

Under a licensing model, a company sells licenses to other (typically smaller) companies to use intellectual property (IP), brand, design or business programs. These licenses are usually non-exclusive, which means they can be sold to multiple competing companies serving the same market. In this arrangement, the licensing company may exercise control over how its IP is used but does not control the business operations of the licensee.

Both models require that the franchisee/licensee make payments to the original business that owns the brand or intellectual property. There are laws that govern the franchising model and define what constitutes franchising; some agreements end up being legally viewed as franchising even if they were

originally drawn up as licensing agreements. It can be clarified from the differences given below:

Basis	Franchising	Licensing
Governed by	Securities Law	Contract Law
Registration	Required	Not required
Territorial rights	Offered to franchisee	Not offered; licensee can sell similar licenses and products in same area
Support and training	Provided by franchiser	Not provided
Royalty payments	Yes	Yes
Use of trademark/Logo	Logo and trademark retained by franchiser and used by franchisee	Can be licensed
Examples	McDonalds, Subway, 7-11, Dunkin Donuts	Microsoft Office
Control	Franchiser exercises control over franchisee.	Licensor does not have control over licensee.

#### Question 4. Discuss meaning, merits and demerits of contract manufacturing.

**Answer:** Contract manufacturing refers to type of international business where a firm enters into contract with some local manufactures in foreign countries to get certain components of goods produced as per their specifications. It is also called outsourcing. It can take three forms: Getting produced certain parts of final products which will be used for the production of final products later; assembly of components into final products; and complete manufacture of the products like garments.

#### Merits of Contract manufacturing

1. **Less investment:** It helps international firms in production of goods at massive scale without making any investment in setting up production facilities. Therefore, it is more suitable for small and medium size manufacturers who can't undertake 100% or even 50% investment.
2. **Less risky:** It is less risky as there is little investment involved. Moreover, local manufacturers who have been given specific product design and quality standards do not deviate from them.
3. **Low cost:** If goods are contracted in low labour and material cost country, then it also gives benefit of low cost. For example, in India labour is very cheap and therefore it has become a favorite destination for contract manufacturing.
4. **Better capacity utilization:** Local producers benefit get from contract manufacturing because it allows them to make better use of their idle production capacity.
5. **An opportunity for local producers to become international:** Local producer also gets an opportunity to get involved in international business.

#### Disadvantages of Contract Manufacturing

1. **Deviations from Product design and quality Specifications:** Local firms might not follow product design and quality standards causing serious product quality problems for international firm.

2. **Loses control over Manufacturing Process:** Local manufacturer in the foreign country loses control over manufacturing process.
3. **No authority to sell output:** The local firm cannot sell the output according to his will. It has to sell the goods to international firm at pre-determined prices.

**Question 5. State the important changes being observed in composition of India's external trade since 2007-08.**

**Answer:** Till 1980's exports were mainly of primary goods, viz. agricultural commodities and raw materials, such as minerals. Over time, the role of manufactures including engineering goods has been increasing. Share of manufactured goods is 66 % of total exports, of which engineering goods contribute 27 % of the value of goods exported. Composition of India's external trade since 2007-08 is shown below:

**India's Exports and Imports (US\$ billion).**

	2007-08	% share	2010-11	% share
<b>Exports</b>				
(1) Primary Products	27.55	16.91	35.35	13.89
(a) Agricultural and allied	18.43	11.31	24.69	9.70
(b) Ores and minerals	9.11	5.59	10.66	4.19
(2) Manufactured Goods	102.97	63.21	168.09	66.07
(a) Leather and Manufactures	3.50	21.48	3.78	1.48
(b) Chemicals and related items	21.19	13.00	28.79	11.31
(c) Engineering goods	19.42	11.92	23.31	9.16
(d) Textiles and products	19.42	11.92	23.31	9.16
(e) Gems and jewellery	19.67	12.07	40.79	16.03
(f) Handicrafts	0.50	0.30	0.23	0.09
(3) Petroleum products	28.36	17.40	41.91	16.47
Total exports	162.90		254.40	
(1) Bulk imports	112.74	44.83	150.48	42.60
(a) Petroleum	79.64	31.67	106.06	30.08
(2) Non-bulk Imports	138.69	55.16	202.08	57.31
(a) Capital goods	70.11	27.88	71.62	20.31
(b) Mainly export related	20.76	8.25	49.63	14.07
Total Imports	251.43		352.57	

**Source:** RBI, Annual Report, 2010-11, Appendix Table 17, p. 186.

**Question 6. "Wholly owned subsidiary is a more investing, more risky and less return giving venture." Do you agree? Substantiate your answer.**

**Answer:** I agree to the statement partially. Wholly owned subsidiary is a more investing, more risky and more return giving venture. In this the parent company acquires the full control over the foreign company by purchasing its 100% equity capital. It can be established in two ways: first as a green field venture, in which an altogether a new firm is set up to start operations in a foreign existing firm in foreign country and using it for manufacturing and promoting its products in home country.

**Merits of Wholly Owned Subsidiaries**

1. **Complete control over operations:** The parent firm is able to exercise full control over its operations in foreign countries because it has 100% equity holding in the company.
2. **No need to disclose technology:** It is less risky as 100% investment is made by parent company and hence there is no need to disclose technology to local producers.

### Demerits of Wholly Owned Subsidiaries

1. **100% Investment and hence require more funds:** The parent company needs to make 100% equity investment and therefore requires huge funds.
2. **More risky:** It is more risky as parent company has 100% equity investment; it has to bear all the losses, if any.
3. **Government rules and regulations:** Some countries do not allow establishing 100% wholly owned subsidiaries in their countries.

### Question 7. How is home trade different from external trade?

**Answer:** Internal trade takes place between the geographical boundaries of a nation, whereas international trade takes place between different nations.

1. In the trade of any nation, the volume of its internal trade will be more than that of external trade. Internal trade accounts for about 95% of the total volume of the trade of a country, whereas foreign trade accounts for only about 5% of the total volume of the trade of a country.
2. Though both internal trade and international trade are based on the principle of specialization or division of labour, regional specialization within a country leads to internal trade or inter-regional trade, whereas country wise specialization leads to international trade.
3. In the case of home trade, there is much scope for the operation of forces of demand and supply. But, in the case of foreign trade, there is not much scope for the full operation of the forces of demand and supply.
4. The number of documents of trade required for home trade is less than the required for foreign trade.
5. Home trade is subject to regulations and laws of only one country, whereas foreign trade is subject to regulations and laws of two or more countries.
6. Home trade is, generally, free from restrictions, whereas foreign trade is subject to a number of restrictions.
7. The cost of transport in home trade is much less than that in foreign trade.
8. The interval between the dispatch of goods by the seller and the receipt of the same by the buyer in home trade is not much.
9. Goods are subject to greater risk in foreign trade than in home trade.
10. As goods are subject to more risks in foreign trade, in the case of international trader, goods are, generally, insured against the risks.
11. Home trade involves the currency of only one country whereas foreign trade involves the currencies of two or more countries.

### IV. Higher Order Thinking Skills (HOTS)

#### Question 1. "Foreign trade is not free from difficulties." Comment.

**Answer:** Foreign trade is not free from difficulties. The following are some of the important difficulties of foreign trade:

1. It is a long distance trade and as such it becomes difficult to maintain close relationship between the buyer and the seller.



2. Each country has its own language. As foreign trade involves trade between two or more countries, there is diversity of languages. This difference in language creates problem in foreign trade,
3. Foreign trade involves preparation of a number of documents which also creates difficulties in the way of foreign trade.
4. Some restrictions are imposed on export and import of commodities. These restrictions stand on the progress of foreign trade.
5. Foreign trade involves a great deal of risks because trade takes place over a long distance. Though the risks are covered through insurance, it involves extra cost of production because insurance cost is added to cost.

**Question 2. “International trade benefits both the parties involve.” Do you agree?**

**Justify your answer:**

**Answer.** No doubt, trade benefits both the parties involved. These gains can be categorised as static and dynamic.

**Static gains from trade:**

1. If a country has an absolute or relative advantage in the production of some goods, it can specialize in those goods and can trade it for others. It will increase total productivity.
2. Increase in imports will increase country's ability to satisfy consumer needs. Imports of capital goods may also increase the economic growth rate in the initial stages. It may also shift economy closer to its production possibility curve indicating relatively fuller utilization of resources.
3. Specialization based on comparative advantage will result more efficient utilization of resources. Hence, a labour abundant country will expand those industries which use more of labour. It will stimulate employment and wage rates will go up.
4. According to Myint, international trade can provide a larger market for developing countries that will help these countries to increase their output and employment and hence, they will shift closer to PPC and real output will increase.
5. Trade brings various nations closer and interlinks the economies of the world. It helps to learn from each other's experience and sharing of capital, technology and knowhow also increases.

**Negative static effects of trade:**

1. An economy which specialises in labour intensive industries at the cost of modern sector may face problems. It is so because the products of these industries have low price elasticities of demand and supply of agriculture and primary goods is quite instable.
  2. Large chunks of stock will lead to unfavorable terms of trade for the country. It may reduce the benefits expected from trade.
  3. Specializing in labour intensive industries and relying on developed nations for modern machinery and commodities is not advisable on the principle of prudence.
  4. Since there is huge unemployment in developing countries, increased demand for labour will not increase wage rate so much.
  5. Since there are inflexibilities in traditional economies, the expected gains from trade do not get realized. Rather trade benefits developed countries more and thereby increases the inequalities of income amongst nations.
- Dynamic gains from trade:

**Dynamic positive effects:**

1. When economy operates at a larger scale with access to the markets of other countries, it can avail of economies of scale which otherwise will not be available.  
Economies of large scale will make these countries more competitive in international market.
2. International trade gives\*an exposure to world market and international technology of production which a closed economy can not have. It helps an under developed country to grow at a fast pace and become more competitive.
3. There are many other dynamic changes that occur in the economy via trade like increased investment due to better economic environment, approach to world class technology, institutional changes, exposure to new and different products.

### Dynamic negative effects:

1. Market imperfections may increase social costs. Hence, trade that considers only private costs may not be consistent with the long term development goals.
2. The overall effect of exports will vary from industry to industry; sector to sector. Some industries may get benefit more than others.
3. If increasing returns to scale are available for some commodity, it may lead to higher profits through exports rather than one in which decreasing returns to scale are expected. Hence, returns to scale may complicate the judgment whether exports are benefiting or not.
4. Existence of imperfection in markets and government policies may adversely affect the expected dynamic gains.
5. Many a time, trade benefits developed countries more than developing ones. In such a situation, it may worsen the relative economic strength of developing nations.

### V. Value Based Questions

**Question 1. Which mode of international business should be chosen by a small business man and why?**

**Answer:** A small business should consider following factors in selecting mode of entering into international business.

1. **Ease of entry:** First and foremost factor that determines the choice of mode of entry into international business is ease of entry. A businessman wants to adopt such mode of entry into international business which is easy and less formalities requiring. Exporting, importing, licensing and franchising are better ways from this perspective.
2. **Cost:** Second determining factor is cost involved. For example, very less cost is involved in exporting, importing, licensing, franchising and contract manufacturing as compared to joint ventures and setting wholly owned subsidiaries.
3. **Control over production:** If the foreign company or producer wants full control over production activities in local country, he will prefer franchising, wholly owned subsidiary or joint venture with majority share holding. If it is not so important, he will prefer exporting, importing, contract manufacturing licensing etc.
4. **Sharing of Technology:** If the company has no problem in sharing of technology then it may choose joint venture or franchising. But if it does not want to share its technology and trade secrets, it will prefer wholly owned subsidiary or exporting.
5. **Risk Involved:** If a firm is ready to take risk, it may choose wholly owned subsidiary or joint ventures but if it is willing to minimise its loss then it should choose exporting, licensing, franchising or contract manufacturing.

In my opinion, being a small businessman he will prefer exporting or licensing, franchising to other modes of business as it is easy, less costly, gives greater control over production and involves lesser risk.

