MODULE II

CHAPTER 2

Entrepreneurship Development and Leadership

University Prescribed Syllabus w.e.f Academic Year 2021-2022

Entrepreneurial Motivation : motivating factors, Types of start-ups ; Characteristics of entrepreneurial leadership, Components of Entrepreneurial Leadership; Factors influencing entrepreneurial development and motivation, Entrepreneurial Opportunities and challenges, Entrepreneurship process. Types of Enterprises and Ownership Structure: small scale, medium scale and large-scale enterprises: Meaning and definition (evolution), role of small enterprises in economic development; proprietorship, Policies governing SMEs, partnership, Ltd. companies and co-operatives: their formation, capital structure and source of finance.

Self-learning Topics : study the white paper https://www.ncert.nic.in/ncerts/l/lebs213.pdf

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2.1 ENTREPRENEURIAL MOTIVATION – MOTIVATING FACTORS

GQ. Briefly describe the factors that motivate entrepreneurs.

GQ. "Although the failure rate among startups is high, more and more entrepreneurs are wanting to start their own enterprise." Explain

What motivates an entrepreneur? This has always been a subject of great interest for everyone. Why would someone take all the risks, put everything to stake and launch a new venture when the odds of failure are high. A study has revealed that most of these new ventures fail to pick up and the failure rate is much higher than the success rate. Despite all this we find more and more people venturing out to start their own enterprise and brave the risk of failure and lose all that they have. So, what is that motivates them to do all that. Why would someone leave their cozy job and venture into the unknown? Following is a list of all the factors that motivate a person to undertake this arduous task.

(1) **Independence :** Top amongst the list of motivating factors is independence. An entrepreneur is independent from the shackles of a regular job. This does not mean that he has free time but it means that he can select the activities that he feels are important for the success of his venture. Independence means not wanting to work for someone else but to be your own boss. This is what drives male and female entrepreneurs around the world to accept all the social, financial and psychological risks and to put in the extra hour needed to establish a successful new venture.

(2) **Desire to prove oneself (achievement) :** The next motivating factor that drives an entrepreneur is the desire to prove one's ability. An entrepreneur could be previously working in another organization wherein he challenges the policies and decisions of the management. He then ventures out and starts his own enterprise to prove that he has the ability and that his choice of policy and decision could yield success. The sense of having achieved something ranks high amongst the motivating factors.

(3) **Money :** Money is another motivating factor that ranks high amongst the factors mainly for male entrepreneurs.

(4) **Opportunity :** An entrepreneur could spot an opportunity and feel that his chances of succeeding in the new venture are high and hence could undertake the journey.

(5) **Job satisfaction :** This motivating factor ranks high in developed country wherein the entrepreneur is dissatisfied with his current job or the jobs that are available and decides to venture on his own. The current job or the jobs on offer may not be challenging for the entrepreneur and they may fail to motivate the entrepreneur to stick to them. Dissatisfaction with current job may motivate a person to start his own venture.

2.2 TYPES OF STARTUPS

GQ. DESCRIBE THE DIFFERENT TYPES OF STARTUPS.

The division of startups can be based on the potential that they possess to grow which is in turn based on the quantum of capital that the entrepreneur has invested, the nature of business, and the research and development undertaken by the enterprise. Based on these three parameters startups can be divided into three types :

(1) **Lifestyle firms :** These are the lowest form of enterprises and are privately held by the owners. They have very little potential for growth and employ not more than 50 people and have a turnover of not more than a few crore rupees. These research and development undertaken in such firms is minimal or no research takes place. They are privately held and are run to support the family of the entrepreneur. Although, they are small in nature such enterprises form the backbone of the economy as they provide localized employment and add to the GDP.

(2) **Foundation Company :** These types of ventures are based on research and development that the entrepreneur has undertaken and possess the potential to grow in the short and long term. The provide employment to more than 100 people and have an annual turnover of more than a few hundred crores. As these ventures do not public they attract lots of private investors.

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(3) **High potential venture :** Although this company may start out like a foundation company it may live up to its potential. Such ventures receive great publicity and attract investors both public and private. If their growth is properly managed they surpass all expectations. Such ventures employ more than 500 people and have a turnover running into a few thousand crores. These ventures are integral to the economic development of the country.

Every new venture could be bracketed into one of the above mentioned three types of startups.

2.3 CHARACTERISTICS AND COMPONENTS OF ENTREPRENEURIAL LEADERSHIP

GQ. Enumerate the leadership qualities of an entrepreneur.

- Conventionally management is referred to as activities which execute five managerial functions like planning, organizing, staffing, leading and controlling. Managers execute and integrate these functions and thus manage the organization. There is confusion that management and leadership are similar, but that is not the fact.
- Leading is not just being first, biggest or most powerful. It is much beyond than that. Leading in the organization carries much importance and is having different and meaningful definition. The leadership is an art of motivating a group of people to act towards achieving a common goal. Emerging trends in management has brought a different meaning to leadership.
- According to traditional theories, leaders in business lead and manage the business. It states that there is no sharp distinction between leadership and management. Leaders occupy positions of authority and it is a formal role. It even predicts that leaders make strategic decisions. They are good at managing people. New discovered role of manager in contemporary era state that leader gives the direction to the organization.
- A study of leadership is diverse in nature and multiple definitions have been offered. Nevertheless, leadership style can be defined broadly as the manner and approach of providing direction, implementing plans, and motivating people.
- Leadership can be defined as a process by which one individual influences others toward the attainment of group or organizational goals. Three points about the definition of leadership should be emphasized.
- Leadership is a social influence process. Leadership cannot be there without a leader and the followers. Key aspect of leadership is it elicits voluntary action on the part of followers. Because of voluntary nature of compliance, leadership is different from other types of influence based on formal authority.
- Leadership results in followers' behavior that is focused and goal-oriented in some sort of organized setting. Most of the studies of leadership concentrate on the nature of leadership in the workplace.
- There is distinction between leader and leadership. Leader is an individual who exercises the leadership. Leadership is an activity of leading people towards organizational goal is executed by this individual.
- The word manager and leader are interchangeably used. The managers are called as leaders because of the formal authority, inspire of observing whether they really exercise leadership in their job or not.
- Harvard's John Kotter says that management is coping with the business complexities and leadership on other hand is coping with the change. According to him leadership is the part of management. Leadership produces the change. So for organization strong management as well as effective leadership is required.
- In short, in a business enterprise, several activities like setting of the objectives of organization, designing methods to achieve them, directing and coordinating the activities of various departments can be successfully managed if there is proficient leadership.
- Tata Iron and Steel Company and Reliance Industries are some of the best examples of leadership in India. These companies would have not achieved great success without leaders like J.N. Tata and Dhirubhai Ambani respectively.

2.3.1 Defining Leadership

The different leadership thinkers have different definitions from their own perspectives.

- **Encyclopedia of Social Sciences** states that "Leadership refers to the relation between an individual and a group around some common interest and behaving in a manner directed or determined by time (i.e. leader).

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- **Chester. L. Bernard** defined leadership as "It refers to the quality of the behavior of the individual whereby they guide people on their activities in organized efforts.
- **George R. Terry** stated that "Leadership is the activity of influencing people to strive willingly for mutual objectives".
- **Peter F. Drucker** "Leadership is the lifting of man's visions to higher rights, the raising of man's performance to higher standards, the building of man's personality beyond its normal limitations."
- **R.T. Livingston** holds "Leadership is the ability to awaken in other the desire to follow a common objective"
- **Allen** says "Leader is one who guides and directs other people. He must give effective direction and purpose."
- **Robert C. Appleby** opines "Leadership is a means of direction, is the ability of the management to induce subordinate to work toward group ideals with confidence and keenness.

2.3.2 Leadership characteristics of an Entrepreneur

- As discussed earlier, the leader is a person who motivates the employees to work to attain the goal of an organization. It is very important to get the right leader who works in the positive direction and enhances organizational standards and ensures organizational growth. According to many management thinkers leaders are not born they are made.
- Leaders earn the trust and respect from their group members. This is the reason why followers follow the leader. To be leader is not as easy as it is to become a manager. It is long process where person has to take lot many experiences and needs to learn many skills.
- These competencies of the leader are depend on a variety of factors
  (1) The number of people following the leader
  (2) The extent of the leader's leadership skills
  (3) The leader's basic nature and values
  (4) Organization's background, such as whether it's for profit or not-for- profit, new or long established, large or small etc.
  (5) The particular culture (or values and associated behaviors) of whomever is being led
  (6) The leadership is totally dependent on the situation. So it is really difficult to list exact and all leadership skills.
- Following are the major leadership attributes :
  (1) **Integrity :** One of the important attributes of the leadership is integrity. Leaders have high ethics and they are honest. Because of this they gain people's trust and respect. This creates a positive response in the group of followers. Leaders never play the blame game, they always take the responsibility of the action and its consequence.
  (2) **Passionate :** Passion is very important ingredient of success. Leaders are passionate. They are enthusiastic about their work and they even have the ability to emit this energy to the followers.
  (3) **Commitment :** Commitment in any work is important. Leaders are committed throughout the work. Once they take the responsibility of one task, they complete it in the given time and available resources. They follow the strong discipline while executing the tasks and same is applicable to their followers.
  (4) **Courageous :** Leaders handle many risky and uncertain situations. Their decision makings are very important as it directly impacts the organization's future. So they need to have courage to handle any type of situation. They should be able to speak up whenever appropriate time comes.
  (5) **Goal oriented :** Everyone who works for the organization contributes to the organizational goal. The leaders need to be very focused on the objectives of the organization as they lead the whole team. They need to be very much focused and develop the strategic plans to ensure the organization's benefit.
  (6) **Developing People :** An organization can grow if the employees grow and develop. The development of people can be done by giving the training, coaching or may be teaching. This is one of the key traits of a leader. Leader alone cannot achieve the organizational goal. So his responsibility is to develop the human resource available to him.

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(7) **Prioritize :** In case of multiple responsibilities on one person, a person has to prioritize the activities or actions. Leaders are the people who need to fight on many fronts and so need to decide the preliminary and secondary activates they need to find out the most urgent and important things first regardless of their interest in them.

(8) **No Public Glory :** Leaders know that they cannot achieve anything alone. So they always share the credit of success with the team. They do not expect public glory or any awards or accolades. Leaders understand that at best they will get private credit for their work.

(9) **Drive :** Leaders are ambitious and take initiative.

(10) **Motivation :** Leaders want to lead and are willing to take charge of the activity.

(11) **Self-confidence :** One of the most important factor which affects leadership is self confidence. Leaders are assertive and decisive. They enjoy taking risks. They admit mistakes and foster trust and commitment to a vision. Leaders are emotionally stable rather than irresponsibly adventurous.

(12) **Cognitive ability :** Leaders are conceptually skilled, intelligent and perceptive. They need not be necessarily geniuses. They have analytical ability, good judgment, and the capacity to think strategically.

(13) **Business knowledge :** Leaders tend to have technical expertise in their businesses.

2.4 FACTORS INFLUENCING ENTREPRENEURIAL DEVELOPMENT AND MOTIVATION

GQ. Briefly describe any five factors that influence entrepreneurial development.

- Apart from the obstacles, there are certain major factors that affect the growth of entrepreneurship. In many of the less developed countries, most of their inventions either lie in idle conditions or flow out to the prosperous nations.
- One can find a paradoxical situation in less developed countries. On the one hand, entrepreneurs do no not seem to come forward; on the other hand, those who are present tend to leave their countries in search of better opportunities.
- Several inimical factors are affecting the growth of entrepreneurship. They can be studied under the following heads :

(A) Economic Factors

The economic factors that affect the growth of entrepreneurship in the less developed countries are :

(i) Lack of adequate Basic facilities

- Certain basic or overhead facilities like modern transport and communication, adequate irrigation and power facilities, latest technology etc. are very essential for undertaking innovative activities. They provide external economies by increasing the output and reducing the cost of production.
- Unfortunately, these facilities are not adequately available in less developed countries. Hence, entrepreneurs have to provide these facilities themselves or obtain them at exorbitant costs.

(ii) Non-availability of Capital

- Innovations generally require huge capital investment or capital equipments. Capital equipments have to be imported which involves heavy shipping and insurance companies.
- Sometimes even the basic expertise has to be imported.
- Imports also involve considerable amount of foreign exchange which is also scarce in less developed countries.
- Hence innovations are scarce to developing countries and thus, non-availability of capital hampers entrepreneurial growth,

(iii) Non-availability of raw materials and Finished Goods

- Large stocks of inventories have to be kept to ensure adequate industrial supplies. Hence the amount of working capital required is increased considerably in less developed countries pushing up the cost of production.

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- Borrowed capital either for fixed or working capital requirements involves higher interest rates also.
- Hence, the entrepreneurial growth is affected very much in these countries.

(iv) Greater Risks involved in business

- Risks are greater in less developed countries than developed nations due to the following reasons :
- There is considerable instability in both domestic and foreign economic policies.
- There is instability in the market due to seasonal fluctuations of demand.
- Exports of these countries are subject to violent swings of prosperity and depression prevailing in import countries.
- The domestic market is also small that inhibits new investments.
- There is lack of information on cost, market demand, overhead facilities etc. Hence, an entrepreneur cannot make correct estimates of his proposed venture.
- Due to the aforesaid risks, entrepreneurs have a tendency to prefer short-term investments to long-term investments. Hence, entrepreneurship growth is very much affected.

(v) Non-availability of skilled labour

- In developing countries, labour is not trained and hence lacks industrial skills. The traditional skills of workers are highly insufficient for modern industrial jobs.
- Moreover, due to agrarian character, industrial labour is not available in plenty. Hence, an entrepreneur finds it very difficult to get skilled labour which retards his growth.

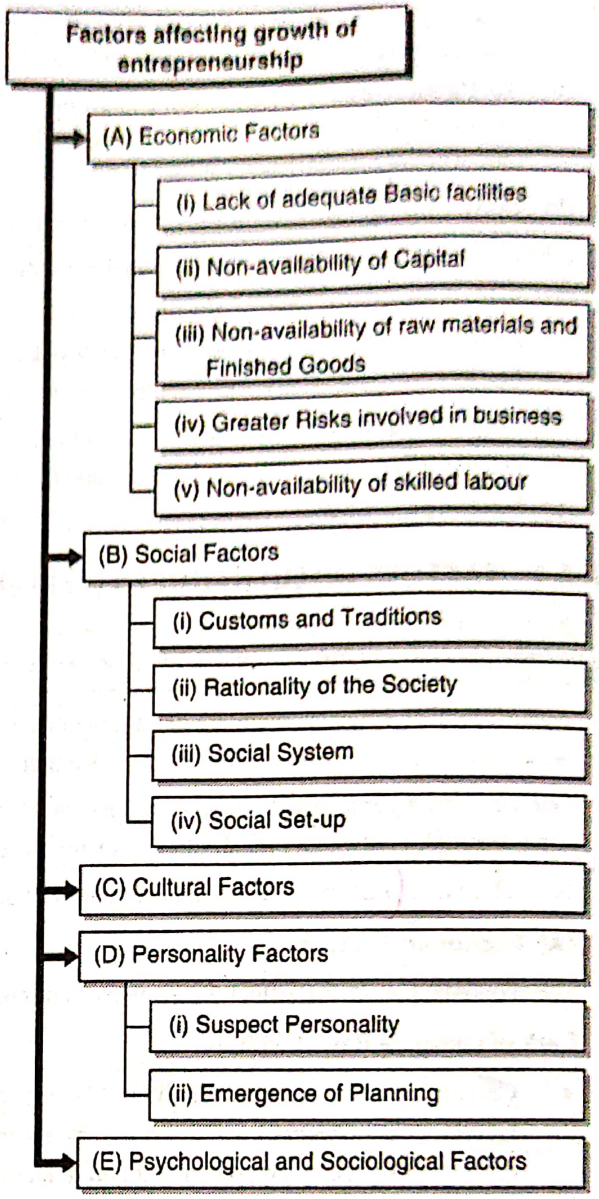

Fig. C1.3 : Factors affecting growth of entrepreneurship

(B) Social Factors

- Social factors also play a decisive role in encouraging entrepreneurship in a country.
- In fact, the favourable social factors that prevailed in Europe during 17th and 18th centuries led to the very emergence of the 'entrepreneur' as a factor of production. Some of these factors are :

(i) Customs and Traditions

- If customs and traditions play a dominant role in production decision-making rather than the critical assessment of facts, then entrepreneurship will not be encouraged.
- It is so because an entrepreneur will be guided more by customs than his individual initiative and drive.

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(ii) Rationality of the Society

- A society is said to be rational when decisions regarding resource utilisation are based on empirical facts and critical scientific standards.
- While rational behaviour is the order of the day in the developed nations, a majority of the less developed countries are characterised by a non-rational society which is unsuitable to entrepreneurship.

(iii) Social System

- The social system prevailing in a locality also affects entrepreneurship. For example, in a society where the joint family system is in vogue, entrepreneurship cannot be developed.
- It is so because those members of the joint family who gain wealth by their hard work are denied of the opportunity to enjoy the fruits of their labour, since they have to share their wealth with the other members of the family.

(iv) Social Set-up

- The social set-up in some countries is hostile to entrepreneurship and take up a negative approach to new ventures. For instance, in some societies, education, research and training are given very little importance.
- Such societies cannot expect entrepreneurs to emerge and take up new ventures. Again, if narrow parochial and caste considerations are given importance in a society, it cannot produce entrepreneurs with skills and aptitudes.

(C) Cultural Factors

- The cultural factors prevailing in a country decide the level of entrepreneurial activities in that country. If the culture does not attach great value to business talents, industrial leadership etc. then people may not prefer any business venture.
- Again, entrepreneurial growth requires proper motivation to the entrepreneurs to take action. The proper motives are profit maximization, social status attainment, prestige acquisition etc.
- If the culture in a society is economical or monetarily oriented, entrepreneurship will be encouraged and appreciated. In less developed countries, people are not economically motivated and they have greater scope for attaining social status by non-economic pursuits. Hence, entrepreneurship is not developed.

(D) Personality Factors

(i) **Suspect Personality :** In the lesser developed countries, the entrepreneur is looked upon with suspicion. People tend to see in the entrepreneur as a suspect personality. They view the entrepreneur only as profit maker and an exploiter. Thus the public opinion tends to become hostile to entrepreneurship.

(ii) **Emergence of Planning :**In developed countries, people favour direct state activity in the economy rather than private entrepreneurship due to suspect personality factors. Hence, many countries have resorted to planning as a means of achieving economic progress and the State has been given a pivotal role. Planning imposes controls and this goes against the very personality of the entrepreneurs.

(E) Psychological and Sociological Factors

There are many psychological and sociological factors that affect entrepreneurship. Many theories have been put forth by psychologists and sociologists to explain the root of entrepreneurship. They can be summarized as follows :

(i) According to McClelland "need achievement" motive induces entrepreneurship. This is confirmed by Paul Wilken who says that "entrepreneurship becomes the link between need achievement and economic growth."

(ii) This need achievement is influenced not only by social and cultural factors, but also by parental influence.

(iii) Psychological consequences of social change like a radical loss of status are the root cause of entrepreneurship.

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(iv) Some other theories of entrepreneurship stress the motives on goals of entrepreneurs. According to Cole, besides wealth, entrepreneurs seek power, prestige, security and service to society. Evens has distinguished three kinds of entrepreneurs on the basis of motives, viz :

- Managing entrepreneurs whose chief motive is security.
- Innovating entrepreneurs whose motive is excitement.
- Controlling entrepreneurs whose chief motives are power and authority.
- Rostow has examined inter-generational changes in the families of entrepreneurs. He believes that the first generation seeks wealth, the second prestige and the third art and beauty.

(v) According to leading psychologists, entrepreneurs are characterized by the presence of "Type A" behavior in all their ventures. 'Type A' behavior is nothing but a "chronic incessant struggle to achieve more and more in less and less."

2.5 ENTREPRENEURIAL OPPORTUNITIES AND CHALLENGES

GQ. What is an opportunity?

GQ. "The ability to recognize an opportunity is critical for an entrepreneur." Explain.

2.5.1 What is an Opportunity ?

- An opportunity is a situation that is attractive, durable but timely and is anchored in a product or service which adds value to the end-user. Successful entrepreneurs have the ability to recognise opportunities i.e. they start with what customers want and do not lose sight of it.
- In the business world, opportunities are created using ideas and entrepreneurial creativity. Ideas interact with the prevalent business environment and entrepreneurial creativity to create a business opportunity.
- Actions taken on opportunity recognition lead to the creation of a new venture.
- Anticipation of changing business environment is critical in entrepreneurship. Constant vigilance for changing business environment is a valuable habit for entrepreneurs.
- An entrepreneur with credibility, creativity and decisiveness can seize an opportunity while others merely observe.
- In the current business environment, opportunities are apparent to a limited number of individuals.

2.5.2 Opportunity Recognition and Entrepreneurship

- Opportunity recognition and entrepreneurship are like two sides of the same coin.
- Entrepreneurship as we have seen is the creation and operation of viable new companies through vigorous application of ideas, skills, knowledge and talent. Thus, central to this definition of entrepreneurship is the ability of entrepreneurs to recognise opportunities, evaluate and act on those opportunities which they feel has potential.
- The true entrepreneur skill lies in the ability to recognise and select the right opportunities for new business ventures. Recognizing high potential opportunities can often lead to substantial gains in profit, growth and competitive positioning.
- Thus, the concept of opportunity recognition became central to entrepreneurship research.

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2.5.3 Opportunity Recognition

- There are two opposing views regarding opportunities. One view argues that opportunities are discovered while the other view argues that they are created. These two main perspectives differ on how opportunities are discovered or created.
- It is argued that entrepreneurial opportunity recognition is a cognitive process as it relies on the individual.
- Entrepreneurs use cognitive insights and spend more time compared to non-entrepreneurs in searching for information which will lead to new business opportunities.
- Researchers have suggested that prior knowledge adds significant insights to the recognition of opportunity. Prior knowledge in a particular industry provides entrepreneur the capacity to better recognize opportunities.
- Although, macro environmental forces such as technology, social-culture, economic and political changes are important source of opportunity, it is the ability of the entrepreneur to recognize particular opportunities amidst these contextual changes.
- In a given same set of circumstances and situation, not all people can recognize a given entrepreneurial opportunity.
- Some would be able to identify it while others have overlooked it. Why do some people see it while others don't? Past studies have lend support to the suggestion that possession and wider exposure to prior and new information and superior cognitive capabilities help formulate a conjecture towards opportunities.
- Also, some individuals are able to spot opportunities while others do not due to two major reasons.
- Firstly, the individuals have better access to information about the existence of the opportunities through prior knowledge, social network structure and information search. Secondly, they are able to more easily identify the opportunities given the same amount of information though their cognitive properties.
- Based upon these studies, we can safely say that entrepreneur must first be equipped with a level of education and experience.
- Together with other critical factors such as the entrepreneurial alertness and the entrepreneurial network, the combination will enable the entrepreneur who has the ability to recognize meaningful business opportunity and who are able to strategically position the business be able to successfully complete the development process and launch the new venture. As suggested, the opportunity recognition is a process with a number of steps and not simply rather a coming flash of sudden insights.

2.5.4 Opportunity Recognition Framework

As discussed in the previous section the three factors of opportunity recognition are :

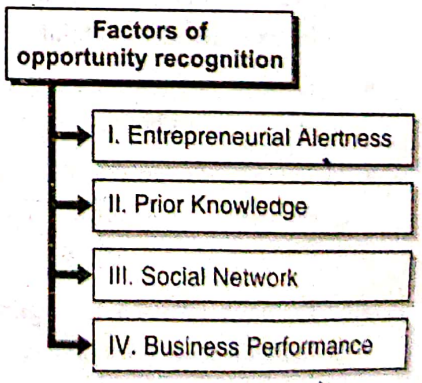

Fig. 2.5.1 : Factors of opportunity recognition

(I) Entrepreneurial Alertness

- Alertness is defined as a process and perspective that helps some individuals to be more aware of changes, shifts, opportunities and overlooked possibilities.
- Alertness involves a number of cognitive capacities and processes such as prior knowledge and experiences, pattern recognition, information processing skills and social interactions.
- Extending alertness as part of the cognitive process, the alert scanning and search dimension involves prior knowledge, preparedness and sensitivity to new opportunities.

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- Alert scanning and search will enable the entrepreneur to examine new ideas in an unconventional manner as in the process, they increase the entrepreneur's domain-relevant information.
- The second dimension of alert association and connection involves putting together disparate pieces of information and reassembling them into coherent alternatives. This dimension focuses on the availability of new information, creativity and making extensions in logic.
- Information are gathered and creatively applied. Such skills in association, allows the entrepreneur to consider various options and possibilities in making unique connections.
- The individual connects the multiple pieces of information to a big picture so that connections previously undiscovered can be made.
- The last dimension of evaluation and judgment refers to the evaluations and judgments made by the entrepreneur on new changes of information and to decide on its effect on the business opportunity and profit potential.
- Opportunity that arises with the existence of new information will be assessed and evaluated.
- Entrepreneurs are successful because of their alertness to information on the market condition and opportunity movements.
- Researchers argue that some people are better than others at seeing relationships and patterns in information. They integrate the information and create new causal links which all facilitates recognizing opportunities. It is hypothesized that individuals with such a schema will be more likely to notice industry/ market changes.

(II) Prior Knowledge

- Prior knowledge refers to an individual's distinctive information about a particular subject matter which may be a result of work experience, education or other means.
- With the stock of information and knowledge gained through life experiences, certain people are able to make the connection to recognize the opportunity as it is related to their available information.
- Past research have shown a strong suggestion that increased knowledge in a particular field awards individuals with an added advantage.
- The increase of likelihood of opportunity recognition is attributed to:
- Prior knowledge provides an absorptive ability which facilitates the gaining of additional information about markets, production processes and technologies which triggers an entrepreneurial conjecture and;
- People's existing stock of information influences their abilities to see solutions when encountering problems.
- With increased knowledge, they individuals become increasingly more efficient in their task and to also appear to be more intuitive in thinking during the decision process.
- Each person's prior knowledge creates a 'knowledge corridor' that allows the entrepreneur to recognize certain opportunities but not others.
- The knowledge corridor principle explains that once entrepreneurs found their companies, they set off on a journey down a corridor through which windows of opportunities opens around them.
- If they had not entered the corridor they would not be able to see the opportunity.
- Previous research in cognition suggests that increased prior knowledge in a particular field will provide an individual with certain advantages in decision making.
- Higher levels of prior knowledge are associated with higher opportunity recognition.
- Knowledge can be in the form of tacit knowledge and explicit knowledge.
- Tacit knowledge refers to the knowledge that is gained from experiences while explicit knowledge are those gained through formal education.

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- It could also be argued that opportunity is recognized by some individuals and not others due to the differences in their ability and access to resources. In addition, it is reasoned that individual's education can help improve the skills of opportunity recognition by tapping on the individual's knowledge.
- It is also reasoned that higher level of education increases an individual's knowledge base which leads to increase in skills to recognize opportunities and such knowledge is utilize to form a framework from which new information can be recognized and processed.

(III) Social Network

- Social networks have been included in the entrepreneurship studies as one of the key antecedents to opportunity recognition. The entrepreneurial activities do not exist in a state of vacuum but rather it is embedded in cultural and social context.
- Hence, it can be said that entrepreneurship is embedded in social networks which facilitates the entrepreneurial process by linkages among entrepreneurs, resources and opportunities.
- Social network is a resource and a potential capital while social capital is a network which is used to engage in productive economic activities.
- Social network theory suggests that individuals are interconnected thought their social networks. Through social network, the entrepreneur gains access to support, information and assistance while revealing how individuals are connected to each other.
- Social network theory studies the connections between people and provides insights with regards to information flow and social mobility and how individuals interact and disseminate information.
- The combination of social capital and networks creates a favorable condition for information exchange and creation of new knowledge.
- It is argued that an entrepreneur's social network is their most important source of knowledge and new ideas. The differences in network characteristics help explain the extent to which knowledge transfers and provide the opportunity for new knowledge generation.
- Studies have shown that networks are associated with the number of new opportunities an entrepreneur perceives and depending on the network which they are embedded in, different individuals may be more likely to spot and recognize opportunities than others.
- According to past studies, the quantity and the nature of the social ties are the major source of information and ideas. Based on the strength and closeness of relations involved, social network can be classified as strong and weak ties.
- Strong ties are the ties that require substantial interaction between people such as family members, relatives and close friends.
- Weak ties on the other hand are ties with casual acquaintance within the social network such as customers, supplier and strangers. The two different set of ties offers an entrepreneur with information of different nature.
- Strong ties are more likely to offer information which are trustworthy in respect to opportunity recognition while weak ties act as a source of non-redundant information. Non-redundancy of ties within the network increases the possibilities of entrepreneur gaining the right complement of information necessary for opportunity recognition.
- In the opportunity recognition process, social capital plays a role in assisting the entrepreneur in exposing them to new and different ideas about the business venture. Frequently, we would find entrepreneurs making decisions as a results of association based on advice or friendship, and this is often originate from social capital of weak-tie relationships. Strong-tie relationship on the other hand would play a more prominent role in assisting during the discovery process.

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- Weak ties existence is temporary in nature. It refers to relationships between parties that do not invest time and effort in maintaining these ties.
- However, weak ties are able to offer entrepreneurs links to various actors who move in different circles other than the main circle which an entrepreneur belongs to. As a result, the entrepreneur will be able to gather novel information from different levels of society. As proposed, weak ties can be seen as a bridge linking to new and different information which give entrepreneurs a better chance of recognizing opportunities.
- The stronger the weak-ties the entrepreneur possess are associated with higher opportunity recognition. In a strong tie network where it is rich with structural holes, entrepreneurs receive not only information but also control more rewarding opportunities. The entrepreneur is able to span and bridge these structural holes gaining valuable resources in doing so. From these strong ties, the entrepreneur is able to gain benefits such as trust and fine-tuned information.

(IV) Business Performance

- Entrepreneurial opportunity recognition scholars have examined and investigated the relationship between opportunity recognition and firm performance.
- The field of entrepreneurship is about the importance of recognizing and acting upon opportunities and hence is a key step in the entrepreneurial process. At the end of the entrepreneurial process lies the end result of superior business performance.
- Researchers have proposed that prior knowledge of market and customers lead to successful opportunity recognition and eventually leading to successful ventures.
- Stronger the opportunity recognition skills are positively associated with better business performance.
- There are three antecedents of opportunity recognition skills proposed that are alertness, prior knowledge and social network.
- Entrepreneurial alertness is dependent on the cognitive skills and intelligence of the individuals. Coupled with prior knowledge, enterprising entrepreneurs are able to produce innovative solutions in addressing customer's problems. Through offerings of innovative solutions to customers, there is an increase of customer satisfaction leading to high sales and finally better business performance.
- The opportunity recognition skills act as a mediator between alertness, prior knowledge, social network and business performance. Putting all these factors together we get the Opportunity Recognition Framework:
- An opportunity is a situation that is attractive durable but timely and is anchored in a product or service which adds value to the end-user. Successful entrepreneurs have the ability to recognize opportunities i.e. they start with what customer want.

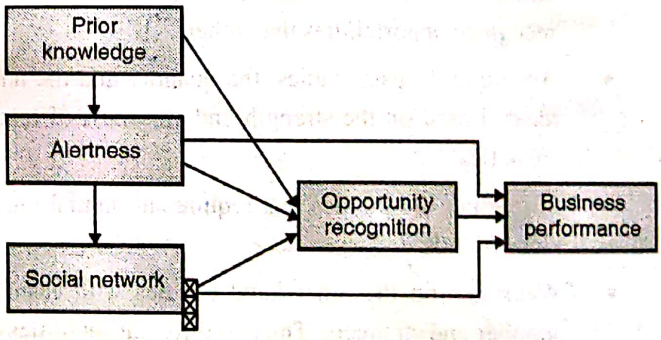

Fig. 2.5.2

- In the business world, opportunities are created using ideas and entrepreneurial creativity. Ideas interact with the prevalent business environment and entrepreneurial creativity to create an opportunity action taken an opportunities recognition leads to the reaction of a new venture.
- Anticipation of changing business environment is critical in entrepreneurship. constant vigilance for changing business environment is a valuable habit for entrepreneurs. An entrepreneur with credibility, creativity and decisiveness can seize an opportunity while others merely observe.

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- In the current business environment opportunities are apparent to a limited number of individuals.
- According to the framework, opportunities that emerge from the market are picked up by alert entrepreneurs.
- These alert entrepreneurs recognize the opportunities through a cognitive process based on their stock of information from prior experiences and knowledge gained which are tacit and explicit.
- An entrepreneur who possesses an extended network of personal and professional relationships increases their ability to recognize opportunities. From casual acquaintances that are more likely to provide unique information to close friends and family who provided the support needed, entrepreneurs identify significantly more opportunities than those without network support. With stronger opportunity recognition skills, entrepreneurs are able to provide innovative and value added solutions to need the market needs. This in turn, is translated to higher customer satisfaction, higher sales, venture profit and growth.
- Thus, an individual's cognitive capabilities in alertness, prior knowledge and social network act as antecedents to opportunity recognition.

2.6 ENTREPRENEURSHIP PROCESS

GQ. Briefly describe the entrepreneurship process.

- The entrepreneurial process is a methodical way of starting a new venture which involves four steps. The entrepreneur realizes, evaluates, and develops an opportunity by defeating forces of resistance.
- The four phases include identifying and evaluating and opportunity, developing a business plan, ascertaining resource needs, and managing the resulting enterprise.
- Each of these steps is in an order one to four in ranking as to the importance of each method. The elements in the steps in this discussion will be from an individual entrepreneurial and corporate entrepreneurial perspective.

Stage I

- Stage one of the entrepreneurial process deals with opportunity identification. An opportunity by definition is a favorable set of circumstances which creates a need for a new product, business, or service.
- Opportunity identification is the process by which the entrepreneur comes up with a prospective idea for a new venture.
- Identifying the opportunity is not simple. Identification takes research, exploration, and evaluation of current needs, demands, and trends from consumers and others.
- With researching and surveying, the product or service can develop. The organization or individual can now innovate what is lacking as long as the market exists for the opportunity to present itself.
- If the market is mature the window of opportunity is closed. Qualities through innovation add value to a product, service, or business.
- The qualities are attractiveness, durability, timeliness, and fixation to the product. These four conditions are what the consumer and end user want. Evaluating the opportunity through observing environmental forces, social forces, technology advances, and political or regulatory changes are attributes to thriving in any industry.
- From an individual perspective, opportunity identification and evaluation is the most important element because it identifies general trends, needs, and risks that involve the original idea which the entrepreneurial process can improve.

Stage II

- The second stage is developing a business plan. Business plan development is an integral piece for submitting a proposal for an entrepreneurial or intrapreneurial business.
- The organization or entrepreneur develops a description of the future direction of the business.

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- A good business plan must be in place that displays a distinct opportunity. The process in business plan formulation can be the most time-consuming stage for the individual entrepreneur or organization.
- An example of this is researching and doing a feasibility analysis for business plan formulation. Testing the viability of the idea gives the ability to change the thought process from idea to a business plan. Business plan development is part of strategic thinking and planning and works well with organizational activities.
- On an individual basis, the sole entrepreneur must rely on brainstorming in smaller focus groups.
- From a corporate perspective, business planning is the essential element to the entrepreneurial process.

☞ **Stage III**

- The third stage is determining and allocating resources. Ascertaining resource needs is a requirement to opportunity and business plan implementation.
- Assessing the risks in association with insufficient or inappropriate resources must be set apart from useful ones.
- The question that needs an answer here is: Can the organization or individual propositioning the venture be capable of obtaining sufficient resources to move forward?
- The entrepreneurial process calls for securing financial and non-financial resources as well as intellectual proprietary protection where it applies.
- Financial resources include start-up costs, the financial performance of like business, and economic attractiveness.
- Non-financial resources include skill sets and labor pools for potential employees. In the health care setting, for example, the skill set for nurses is different from radiology technicians.
- Organizations and individuals performing a resource assessment must be aware of the community the business exists in and whether or not this is a major factor. Resource allocation and availability are important to corporations because sustainability and profit depend on proper planning and understanding the physical internal and external environments.
- For the individual gaining funding from investors and loans and knowing where to cut cost in execution and implementation is the most important issue with resource determination and allocation.
- An example from an individual perspective is making a product via a manufacturer that already exists as opposed to manufacturing the product themselves.

☞ **Stage IV**

- The fourth stage is managing the enterprise. Once resources are secure with the entrepreneurial process business plan implementation can take place. Managing the company means examining operational issues that will occur when implementation begins and throughout the entire business plan cycle.
- The management process involves implementing structure and business style while determining variables for success.
- Establishing a control system to identify and resolve any problem areas will help the management process. Lack of experience can give the individual entrepreneur issues with business growth and administration.
- Organizations understand the business development, growth, and sustainability better than individuals in many cases because resources are easier to be had and utilize as well as methods with strategic management and system development cycles.
- Individuals fare better in the entrepreneurial process improving on existing ideas that have a strong consumer focus and demand.
- Present day brings the ever-increasing demand for quality health care, a continuous stream of technological innovation and health care reform strain the relationship between health care providers, organization, and the community.

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- The relationships between these providers and organizations embody a critical determinant for successful health care delivery. Health care delivery improves with entrepreneurship through the partnership with existing health agencies and providers.
- The entrepreneurship process influences the delivery of health care services and products by sharing ownership in the health care issues and finding solutions to these problems for the community, medical practice and technology, as well as health organizations.
- A wide range of factors influences people and organization in the entrepreneurial process. These factors include environmental, social, personal, and economic influences. There are foursteps or stages in the entrepreneurial process:

(1) Spot and assess the opportunity
(2) Draw up a business plan
(3) Establish resources
(4) Run the company

2.7 TYPES OF ENTERPRISES

GQ. State the basis for the formation of a business enterprise.
GQ. Briefly describe any two forms of business organization

Business Organisation

1. Ownership :

Ownership refers to the right of an individual or a group of individuals to acquire legal title to assets or properties for the purpose of running the business. A business firm may be owned by one individual or a group of individuals jointly. We will be studying the various forms of ownership along with the liability that it brings along.

2. Lawful Business :

The business activity that is undertaken by the business enterprise must be lawful. This implies that illegal activities should not be undertaken and the enterprise should comply with the law of the land.

3. Separate Entity and Management :

Every enterprise is an independent entity and has its own assets and liabilities and a separate way of functioning. Another important feature of being a separate entity is that the profit or losses of one entity cannot be passed to another entity.

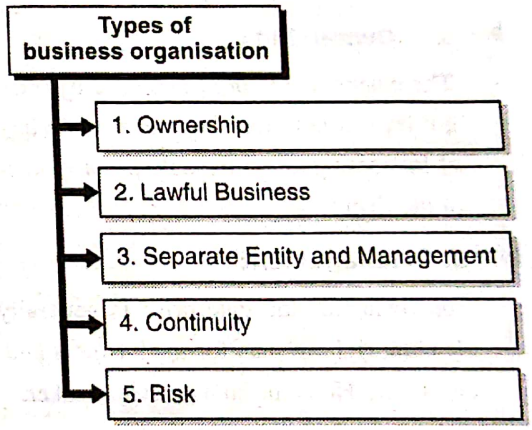

Fig. C2.1 : Types of business organisation

4. Continuity :

The business operations undertaken by the entity should be on a continuous basis and cannot have one single operation or transaction.

5. Risk :

As we are aware that business is directly associated with risk and uncertainty and business enterprises are always exposed to risk and uncertainty. The greater the risk the greater has to be the profits. It is the profit behind the venture that induces the person to take the risk and face the uncertainty.

Forms of Business Organization

- While forming a new business enterprise it is important to select a proper form of organization as the form of organization have;

(1) Legal implications
(2) Decide on the conduct of business

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(3) Assist the Capital formation (4) Profit and Loss sharing

- The important forms of business organization are as follows :

(1) Sole Proprietorship (2) Partnership

(3) Joint Stock Company (4) Cooperative Society (5) Government Company

2.8 SOLE PROPRIETORSHIP

Meaning

- When the ownership and management of business are in control of one individual, it is known as sole proprietorship or sole trader.
- It is seen everywhere, in every country, every state, every locality.
- The shops or stores which you see in your locality - the grocery store, the vegetable store, the sweets shop, the chemist shop, the paanwala, the stationery store, the STD/ISD telephone booths etc. come under-sole proprietorship. It is not that a sole trader business must be a small one.
- The volume of activities of such a business unit may be quite large. However, since it is owned and managed by one single individual, often the size of business remains small.

2.8.1 Characteristics of Sole Proprietorship

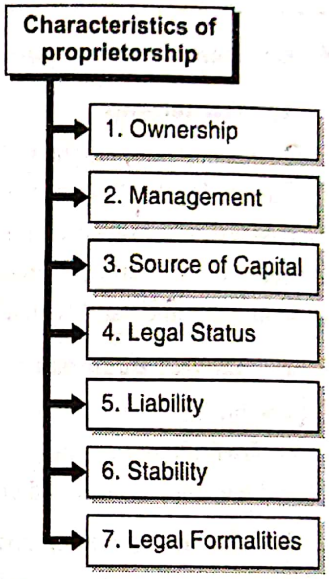

Fig. C2.2 : Characteristics of proprietorship

1. Ownership :

The business enterprise is owned by one single individual, which is the individual, has got legal title to the assets and properties of the business. The entire profit arising out of business goes to the sole proprietor. Similarly, he also bears the entire risk or loss of the firm.

2. Management :

The owner of the enterprise is generally the manager of the business. He has got absolute right to plan for the business and execute them without any interference from anywhere. He is the sole decision maker.

3. Source of Capital :

The entire capital of the business is provided by the owner. In addition to his own capital he may raise more funds from outside through borrowings from close relatives or friends, and through loans from banks or other financial institutions.

4. Legal Status :

The proprietor and the business enterprise are one and the same in the eyes of law. There is no difference between the business assets and the private assets of the sole proprietor. The business ceases to exist in the absence of the owner.

5. Liability :

The liability of the sole proprietor is unlimited. This means that, in case the sole proprietor fails to pay for the business obligations and debts arising out of business activities, his personal property can be used to meet those liabilities.

6. Stability :

The stability and continuity of the firm depend upon the capacity, competence and the life span of the proprietor.

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7. Legal Formalities :

In the setting up, functioning and dissolution of a sole proprietorship business no legal formalities are necessary. However, a few legal restrictions may be there in setting up a particular type of business. For example, to open a restaurant, the sole proprietor needs a license from the local municipality; to open a chemist shop, the individual must have a license from the government.

2.6.2 Advantages of Sole Proprietorship

1. Easy Formation :

The biggest advantage of a sole trader business is its easy formation. Anybody wishing to start such a business can do so in many cases without any legal formalities.

2. Better Control :

The owner has full control over his business. He plans, organizes, co-ordinates the various activities. Since he has all authority, there is always effective control.

3. Prompt Decision Making :

As the sole trader takes all the decisions himself the decision making becomes quick, which enables the owner to take care of available opportunities immediately and provide immediate solutions to problems.

4. Flexibility in Operations :

One-man ownership and control makes it possible for change in operations to be brought about as and when necessary.

5. Retention of Business Secrets :

Another important advantage of a sole proprietorship business is that the owner is in a position to maintain absolute secrecy regarding his business activities.

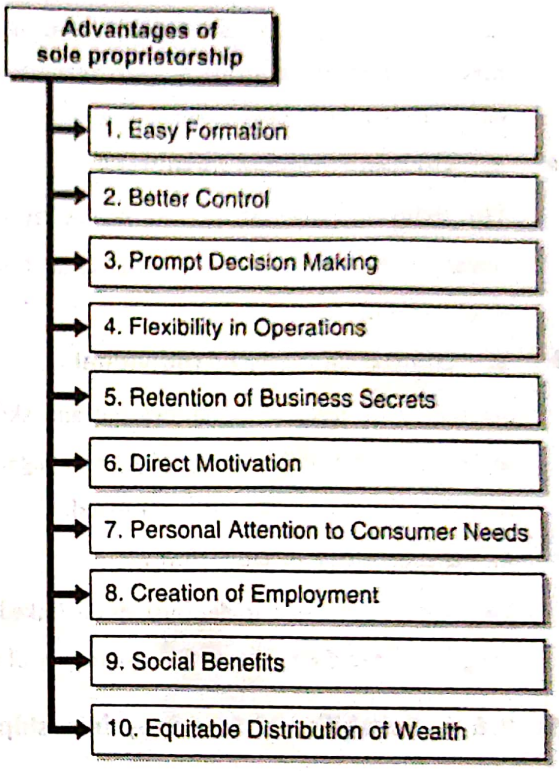

Fig. C2.3 : Advantages of sole proprietorship

6. Direct Motivation :

The owner is directly motivated to put his best efforts as he alone is the beneficiary of the profits earned.

7. Personal Attention to Consumer Needs :

In a sole trader business, one generally finds the proprietor taking personal care of consumer needs as he normally functions within a small geographical area.

8. Creation of Employment :

A sole trader business facilitates self-employment and also employment for many others. It promotes entrepreneurial skill among the individuals.

9. Social Benefits :

A sole proprietor is the master of his own business. He has absolute freedom in taking decisions, using his skill and capability. This gives him high self-esteem and dignity in the society and gradually he acquires several social virtues like self- reliance, self-determination, independent thought and action, initiative, hard work etc,. Thus, he sets an example for others to follow.

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10. Equitable Distribution of Wealth :

A sole proprietorship business is generally a small scale business. Hence there is opportunity for many individuals to own and manage small business units. This enables widespread dispersion of economic wealth and diffuses concentration of business in the hands of a few.

2.8.3 Disadvantages of Sole Proprietorship

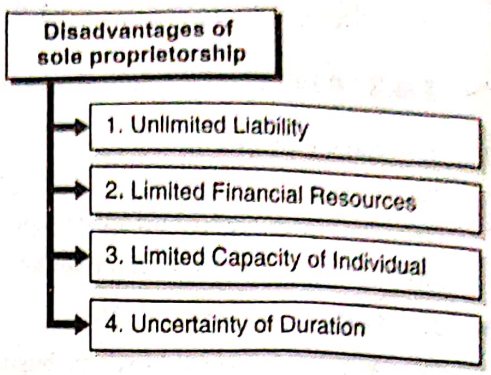

Fig. C2.4 : Disadvantages of sole proprietorship

1. Unlimited Liability :

In sole proprietorship, the liability of business is recovered from the personal assets of the owner. It restricts the sole trader to take more risk and increases the volume of his business.

2. Limited Financial Resources :

The ability to raise and borrow money by one individual is always limited. The inadequacy of finance is a major handicap for the growth of sole proprietorship.

3. Limited Capacity of Individual :

An individual has limited knowledge and skill. Thus his, capacity to undertake responsibilities, capacity to manage, to take decisions and to bear the risks of business are also limited.

4. Uncertainty of Duration :

The existence of a sole trader business is linked with the life of the proprietor. Illness, death or insolvency of the owner brings an end to the business. The continuity of business operation is, therefore, uncertain.

2.8.4 Suitability of Sole Proprietorship

- Sole proprietorship business is suitable where the market is limited, localized and where customers give importance to personal attention. This form of organization is suitable where the nature of business is simple and requires quick decision.
- For business where capital required is small and risk involvement is not heavy, this type of firm is suitable.
- It is also considered suitable for the production of goods which involve manual skill e.g. handicrafts, filigree works, jewellery, tailoring, hair-cutting, etc.

2.9 PARTNERSHIP

Definition

- A partnership form of organization is one where two or more persons are associated to run a business with a view to earn profit. Persons from similar background or persons of different ability and skills, may join together to carry on a business.
- Each member of such a group is individually known as 'partner' and collectively the members are known as a 'partnership firm'. These firms are governed by the Indian Partnership Act, 1932.

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2.9.1 Characteristics of partnership

1. Number of Partners :

A minimum of two persons are required to start a partnership business. The maximum membership limit is 10 in case of banking business and 20 in case of all other types of business.

2. Contractual Relationship :

The relation between the partners of a partnership firm is created by contract. The partners enter into partnership through an agreement which may be verbal, written or implied. If the agreement is in writing it is known as a 'Partnership Deed'.

3. Competence of Partners :

Since individuals have to enter into a contract to become partners, they must be competent enough to do so. Thus, minors, lunatics and insolvent persons are not eligible to become partners. However, a minor can be admitted to the benefits of partnership i.e. he can have a share in the profits.

4. Sharing of Profit and Loss :

The partners can share profit in any ratio as agreed. In the absence of an agreement, they share it equally.

5. Unlimited Liability :

The partners have unlimited liability. They are liable jointly and severally for the debts and obligations of the firm. Creditors can lay claim on the personal properties of any individual partner or all the partners jointly. Even a single partner may be called upon to pay the debts of the firm. Of course, he can get back the money due from other partners. The liability of a minor is, however, limited to the extent of his share in the profits, in case of dissolution of a firm.

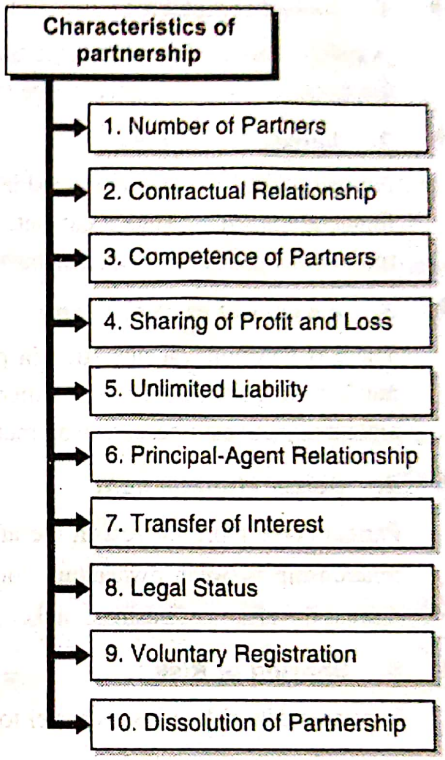

Fig. C2.5 : Characteristics of partnership

6. Principal-Agent Relationship :

The business in a partnership firm may be carried on by all the partners or any one of them acting for all. This means that every partner is an agent when he is acting on behalf of others and he is a principal when others act on his behalf. It is, therefore, essential that there should be mutual trust and faith among the partners in the interest of the firm.

7. Transfer of Interest :

No partner can sell or transfer his interest in the firm to anyone without the consent of other partners.

8. Legal Status :

A partnership firm is just a name for the business as a whole. The firm means partners and the partners mean the firm. Law does not recognize the firm as a separate entity distinct from the partners.

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9. Voluntary Registration :

Registration of partnership is not compulsory. But since registration entitles the firm to several benefits, it is considered desirable. For example, if it is registered, any partner can file a case against other partners, or a firm can file a suit against outsiders in case of disputes, claims, disagreements, etc.

10. Dissolution of Partnership :

Dissolution of partnership implies not only a complete closure or termination of partnership business, but it also includes any change in the existing agreement among the partners due to a change in the number of partners.

2.9.2 Advantages of Partnership Firm

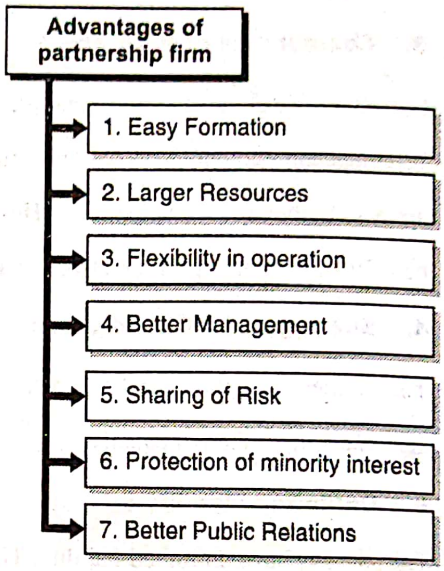

Fig. C2.6 : Advantages of partnership firm

1. Easy Formation :

A partnership can be formed without many legal formality and expenses. Every partnership firm need not be registered.

2. Larger Resources :

As compared to sole proprietorship, a partnership firm can pool larger financial resources. Thus it can enter into bigger operations and can have more credit facilities. It can also have better managerial talent.

3. Flexibility in operation :

There is flexibility of operation in partnership business due to a limited number of partners. These partners can change their operations and amend objectives if necessary by mutual consent.

4. Better Management :

Partners take more interest in the affairs of business as there is a direct relationship between ownership, control and profit. They often meet to discuss the affairs of business and can take prompt decision.

5. Sharing of Risk :

In partnership, risk of loss is easier to bear by individual partners as it is shared by all the partners.

6. Protection of minority interest :

Every partner has an equal say in decision making. A partner can prevent a decision being taken if it adversely affects his interests. In extreme cases a dissenting partner may withdraw from partnership and can dissolve it.

7. Better Public Relations :

In a partnership firm the group managing the affairs of the firm is generally small. It facilitates cordial relationship with the public.

2.9.3 Disadvantages of Partnership Firm

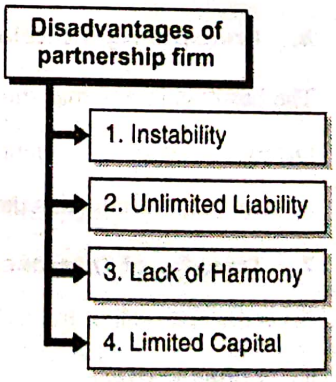

Fig. C2.7 : Disadvantages of partnership

1. Instability :

A partnership firm does not continue to exist indefinitely. The death, insolvency or lunacy of a partner may bring about an unexpected end to partnership.

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2. Unlimited Liability :

As the liability of partners is joint and several to an unlimited extent, any one of the partners can be called upon to pay all the debts even from his personal properties. Further, as every partner has a right to take part in the management of the firm, any wrong decision by a single partner may lead to heavy liabilities for others.

3. Lack of Harmony :

Since every partner has equal right, there are greater possibilities of friction and quarrel among the partners. Differences of opinion may lead to mistrust and disharmony which may ultimately result in disruption and closure of the firm.

4. Limited Capital :

As there is a restriction on the maximum number of partners, the capital which can be raised is limited.

2.9.4 Suitability of Partnership Firm

- In a partnership firm, persons from different walk of life having ability, managerial talent and skill join together to carry on a business. This increases the administrative strength of the organization, the financial resources, the skill and expertise, and reduces risk.
- Such firms are most suitable for comparatively small business such as retail and wholesale trade, professional services, medium sized mercantile houses and small manufacturing units.
- Generally it is seen that many organizations are initially started as partnership firms and later, when it is economically viable and financially attractive for the investors, it is converted into a company.

2.10 PRIVATE LIMITED COMPANY

A private limited company is a voluntary association of not less than two and not more than fifty members, whose liability is limited, the transfer of whose shares is limited to its members and who is not allowed to invite the general public to subscribe to its shares or debentures.

Its main features are :

(1) It has an independent legal existence. The Indian Companies Act, 1956 contains the provisions regarding the legal formalities for setting up of a private limited company. Registrars of Companies (ROC) appointed under the Companies Act covering the various States and Union Territories are vested with the primary duty of registering companies floated in the respective states and the Union Territories.

(2) It is relatively less cumbersome to organize and operate it as it has been exempted from many regulations and restrictions to which a public limited company is subjected to. Some of them are :

- It need not file a prospectus with the Registrar.
- It need not obtain the Certificate for Commencement of business.
- It need not hold the statutory general meeting nor need it file the statutory report.
- Restrictions placed on the directors of the public limited company do not apply to its directors.
- The liability of its members is limited.

(3) The shares allotted to its members are also not freely transferable between them. These companies are not allowed to invite public to subscribe to its shares and debentures.

(4) It enjoys continuity of existence i.e. it continues to exist even if all its members die or desert it.

(5) Hence, a private company is preferred by those who wish to take the advantage of limited liability but at the same time desire to keep control over the business within a limited circle and maintain the privacy of their business.

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2.10.1 Advantages and Disadvantages of Private Limited Company

Advantages of Private Limited Company	Disadvantages of Private Limited Company
(1) Shares are not freely transferable	(1) Continuity of existence
(2) Not allowed to invite public to subscribe to its shares	(2) Limited liability
(3) Scope for promotional frauds	(3) Less legal restrictions
(4) Undemocratic control.	

2.11 JOINT STOCK COMPANY (PUBLIC LIMITED COMPANY)

Meaning

- A Joint Stock Company form of business organization is a voluntary association of persons to carry on business. Normally, it is given a legal status and is subject to certain legal regulations.
- It is an association of persons who generally contribute money for some common purpose. The money so contributed is the capital of the company. The persons who contribute capital are its members.
- The proportion of capital to which each member is entitled is called his share, therefore members of a joint stock company are known as shareholders and the capital of the company is known as share capital.
- The total share capital is divided into a number of units known as 'shares'.
- You may have heard of the names of joint stock companies like Tata Iron & Steel Co. Limited, Hindustan Lever Limited, Reliance Industries Limited, Steel Authority of India Limited, Ponds India Limited etc.
- The companies are governed by the Indian Companies Act, 1956. The Act defines a company as an artificial person created by law, having separate entity, with perpetual succession and a common seal.

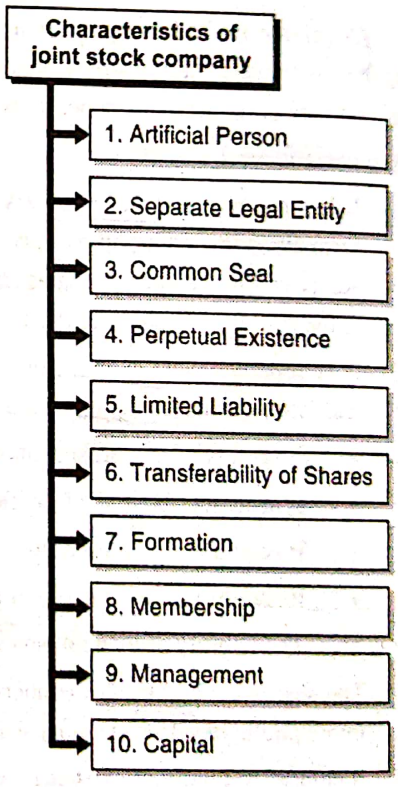

Fig. C2.8 : Characteristics of joint stock company

2.11.1 Characteristics Joint Stock Company

(1) Artificial Person :

A Joint Stock Company is an artificial person in the sense that it is created by law and does not possess physical attributes of a natural person. However, it has a legal status.

(2) Separate Legal Entity :

- Being an artificial person, a company has an existence independent of its members.
- It can own property, enter into contract and conduct any lawful business in its own name. It can sue and can be sued in the court of law. A shareholder cannot be held responsible for the acts of the company.

(3) Common Seal :

Every company has a common seal by which it is represented while dealing with outsiders. Any document with the common seal and duly signed by an officer of the company is binding on the company.

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(4) Perpetual Existence :

A company once formed continues to exist as long as it fulfills the requirements of law. It is not affected by the death, lunacy, insolvency or retirement of any of its members.

(5) Limited Liability :

The liability of a member of a Joint Stock Company is limited by guarantee or the shares he owns. In other words, in case of payment of debts by the company, a shareholder is held liable only to the extent of his share.

(6) Transferability of Shares :

The members of a company are free to transfer the shares held by them to anyone else.

(7) Formation :

A company comes into existence only when it has been registered after completing the formalities prescribed under the Indian Companies Act 1956. A company is formed by the initiative of a group of persons known as promoters.

(8) Membership :

A company having a minimum membership of two persons and maximum fifty is known as a Private Limited Company. But in case of a Public Limited Company, the minimum is seven and the maximum membership is unlimited.

(9) Management :

Joint Stock Companies have democratic management and control. Even though the shareholders are the owners of the company, all of them cannot participate in the management process. The company is managed by the elected representatives of shareholders known as Directors.

(10) Capital :

A Joint Stock Company generally raises a large amount of capital through issue of shares.

2.11.2 Advantages of Joint Stock Company

1. Limited Liability :

In a Joint Stock Company the liability of its members is limited to the extent of shares held by them. This attracts a large number of small investors to invest in the company. It helps the company to raise huge capital. Because of limited liability, a company is also able to take larger risks.

2. Continuity of existence :

A company is an artificial person created by law and possesses independent legal status. It is not affected by the death, insolvency etc. of its members. Thus it has a perpetual existence.

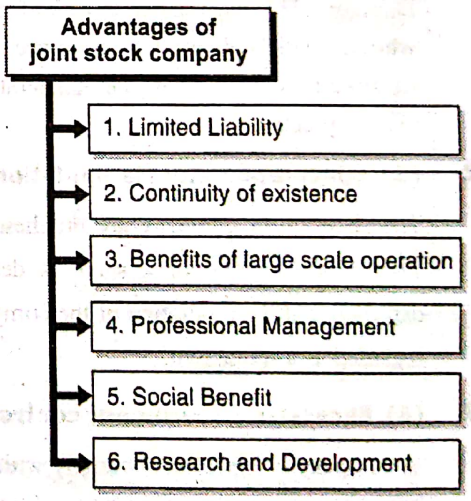

Fig. C2.9 : Advantages of joint stock company

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3. Benefits of large scale operation :

It is only the company form of organization which can provide capital for large scale operations. It results in large scale production consequently leading to increase in efficiency and reduction in the cost of operation. It further opens the scope for expansion.

4. Professional Management :

Companies, because of complex nature of activities and operations and large volume of business, require professional managers at every level of organization. And because of their financial strength they can afford to appoint such managers. This leads to efficiency.

5. Social Benefit :

A joint stock company offers employment to a large number of people. It facilitates promotion of various ancillary industries, trade and auxiliaries to trade. Sometimes it also donates money for education, health, community service and renders help to charitable and social institutions.

6. Research and Development :

A company generally invests a lot of money on research and development for improved processes of production, designing and innovating new products, improving quality of product, new ways of training its staff, etc.

2.11.3 Disadvantages of Joint Stock Company

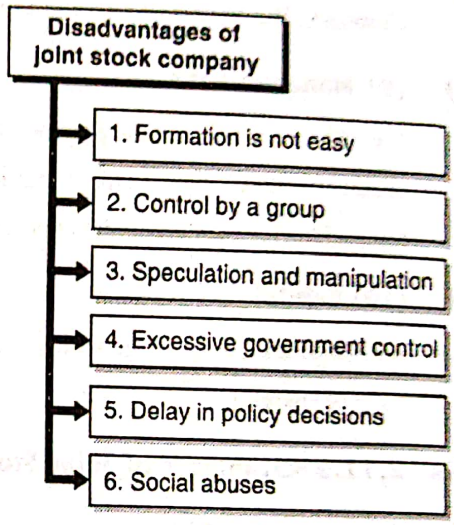

Fig. C2.10 : Disadvantages of joint stock company

(1) Formation is not easy :

The formation of a company involves compliance with a number of legal formalities under the companies Act and compliance with several other Laws.

(2) Control by a Group :

Companies are controlled by a group of persons known as the Board of Directors. This may be due to lack of interest on the part of the shareholders who are widely dispersed; ignorance, indifference and lack of proper and timely information. Thus, the democratic virtues of a company do not really exist in practice.

(3) Speculation and Manipulation :

The shares of a company are purchased and sold in the stock exchanges. The value or price of a share is determined in terms of the dividend expected and the reputation of the company. These can be manipulated, besides there is excessive speculation which is regarded as a social evil.

(4) Excessive government control :

A company is expected to comply with the provisions of several Acts. Non-compliance of these invites heavy penalty. This affects the smooth functioning of the companies.

(5) Delay in Policy Decisions :

A company has to fulfil certain procedural formalities before making a policy decision. These formalities are time consuming and, therefore, policy decisions may be delayed.

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(6) Social abuses :

A joint stock company is a large scale business organization having huge resources. This provides a lot of power to them. Any misuse of such power creates unhealthy conditions in the society e.g. having monopoly of a particular business, industry or product; influencing politicians and government in getting their work done; exploiting workers, consumers and investors.

Suitability of Joint Stock Company

- A joint stock company is suitable where the volume of business is quite large, the area of operation is widespread, the risk involved is heavy and there is a need for huge financial resources and manpower.
- It is also preferred when there is need for professional management and flexibility of operations. In certain businesses like banking and insurance, business can only be undertaken by joint stock companies.

2.12 CO-OPERATIVE SOCIETY

Meaning

- Any ten persons can form a co-operative society. It functions under the Cooperative Societies Act, 1912 and other State Co-operative Societies Acts.
- A co-operative society is entirely different from all other forms of organization discussed above in terms of its objective. The co-operatives are formed primarily to render services to its members. Generally it also provides some service to the society. The main objectives of co-operative society are (a) rendering service rather than earning profit, (b) mutual help instead of competition, and (c) self help in place of dependence. On the basis of objectives, various types of co-operatives are formed :

(a) Consumer co-operatives :

These are formed to protect the interests of ordinary consumers of society by making consumer goods available at reasonable prices. Kendriya Bhandar in Delhi, Alaka in Bhubaneswar and similar others are all examples of consumer co-operatives

(b) Producers co-operatives :

These societies are set up to benefit small producers who face problems in collecting inputs and marketing their products. The Weavers co-operative society, the Handloom owners cooperative society are examples of such co-operatives.

(c) Marketing co-operatives :

These are formed by producers and manufactures to eliminate exploitation by the middlemen while marketing their product. Kashmir Arts Emporium, J&K Handicrafts, Utkalika etc. are examples of marketing co-operatives.

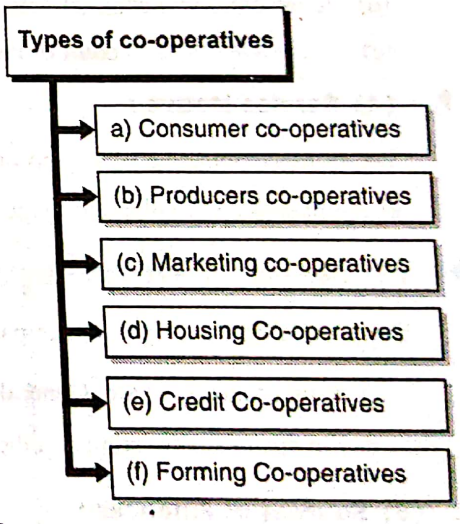

Fig. C2.11 : Types of co-operatives

(d) Housing Co-operatives :

These are formed to provide housing facilities to its members. They are called co-operative group housing societies.

(e) Credit Co-operatives :

These societies are formed to provide financial help to its members. The rural credit societies, the credit and thrift societies, the urban co-operative banks etc. come under this category.

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(f) Forming Co-operatives :

These are formed by small farmers to carry on work jointly and thereby share the benefits of large scale farming. Besides these types, other co-operatives can be formed with the objective of providing different benefits to its members like the construction co-operatives, transport co-operatives, co-operatives to provide education etc.

2.12.1 Characteristics of Co-operative Society

(1) Voluntary association :

Individuals having common interest can come together to form a co-operative society. Any person can become a member of such an organization and leave the same.

(2) Membership :

The minimum membership required to form a co-operative society is ten and the maximum number is unlimited. At times the cooperatives after their formation fix a maximum membership limit.

(3) Body corporate :

Registration of a society under the Co-operative Societies Act is a must. Once it is registered, it becomes a body corporate and enjoys certain privileges just like a joint stock company. Some of the privileges are :

(a) The society enjoys perpetual succession.

(b) It has its own common seal.

(c) It can own property in its name.

(d) It can enter into contract with others.

(e) It can sue others in court of law.

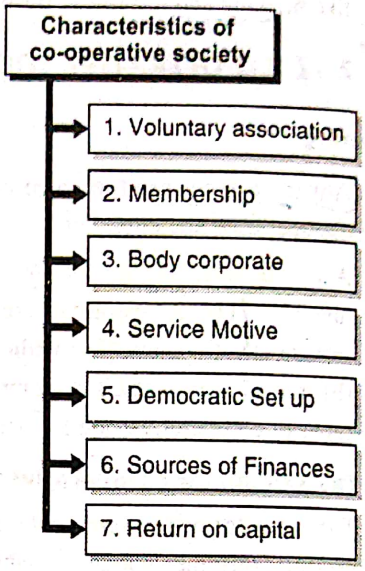

Fig. C2.12 : Characteristics of co- operative society

(4) Service Motive :

The primary objective of any co-operative organization is to render services to its members in particular and to the society in general.

(5) Democratic Set up :

Every member has a right to take part in the management of the society.

Each member has one vote. Generally the members elect a committee known as the Executive Committee to look after the day to day administration and the said committee is responsible to the general body of members.

(6) Sources of Finances :

A co-operative organization starts with a fund contribute by its members in the form of units called shares. It can also raise loans and secure grants from the government easily. One fourth of the profits of the co-operative are transferred to its fund every year.

(7) Return on capital :

The return on capital subscribed by the members is in the form of a fixed rate of dividend after deduction from the profit.

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2.12.2 Advantages of Co-operative Society

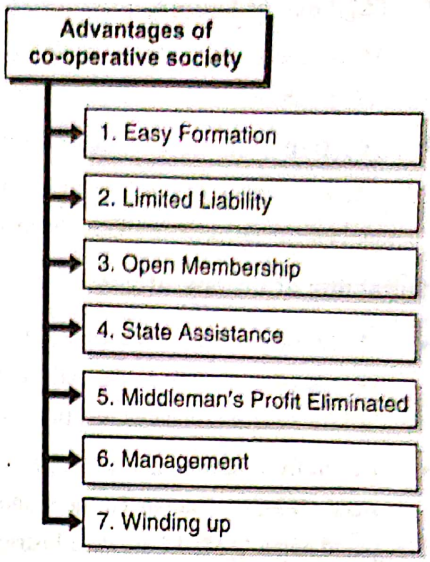

Fig. C2.13 : Advantages of co-operative society

- **(1) Easy Formation :**

  Formation of a co-operative society is easy as compared to a company. Any 10 persons can voluntarily form an association and get themselves registered with the Registrar of Co-operative societies.

- **(2) Limited Liability :**

  The liability of the members is limited to the extent of capital contributed by them.

- **(3) Open Membership :**

  There is no restriction on any individual to be a member of any co-operative.

- **(4) State Assistance :**

  Co-operatives get a lot of patronage in the form of exemptions and concessions in taxes and financial assistance from the state governments which no other organization gets.

- **(5) Middleman's Profit Eliminated :**

  Through the co-operative the consumers control their own supplies and by this means the middleman's profit is eliminated.

- **(6) Management :**

  A co-operative functions in a democratic manner. Each member has only one vote.

- **(7) Winding up :**

  The dissolution of a co-operative firm is quite difficult. It does not cease to exist in case of death, or insolvency or resignation of a member. It has thus a fairly stable life.

2.12.3 Disadvantages of Co-operatives Society

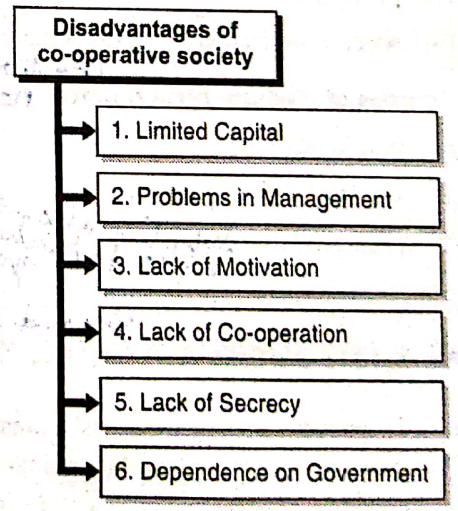

Fig. C2.14 : Disadvantages of co-operative society

- **(1) Limited Capital :**

  The amount of capital that a co-operative can generate is limited because of the membership remaining confined to a locality or region or a particular section of people.

- **(2) Problems in Management :**

  Generally it is seen that co-operative do not function efficiently due to lack of managerial talent.

- **(3) Lack of Motivation :** Co-operatives are formed to render service to its members than to earn profit. This does not provide enough motivation to manage the co-operatives effectively.

- **(4) Lack of Co-operation :**

  Co-operatives are formed with the very idea of co-operation. But, it is often seen that there is lot of friction and bickering among the members due to personality differences, ego clash etc.

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Equity Share – also known as ordinary shares or common stock, representing ownership in company

(5) Lack of Secrecy :

Maintenance of business secrecy is one of the important factors for the success of enterprise which the co-operatives always lack.

(6) Dependence on Government :

The inadequacy of capital and various other limitations make co-operatives dependant on the government for support and patronage in terms of grants, loans and subject themselves to interference.

Suitability of Co-operatives

- When the purpose of business is to provide service than to earn profit and to promote common economic interest, the co-operative society is the only alternative. Co-operatives are also preferred as it is easier to raise capital through assistance from financial institutions and government.
- Generally it seems that a co-operative society is suitable for small and medium size operations. However, the large sized 'IFFCO' [Indian Farmers and Fertilizers Cooperative] and the Kaira Co-operative Processing Milk under the brand name 'AMUL' are the illustrious exceptions.
- The entrepreneur requires finance for short as well as long term and for that there are various sources of finance available. The company will choose the appropriate sources of finance depending upon capital required and the term it is required for.

Sources of Finance

- The sources of finance for any business entity vary as per the period or term for which the finance is required. Every business entity requires finance for: long term, medium term and short term.

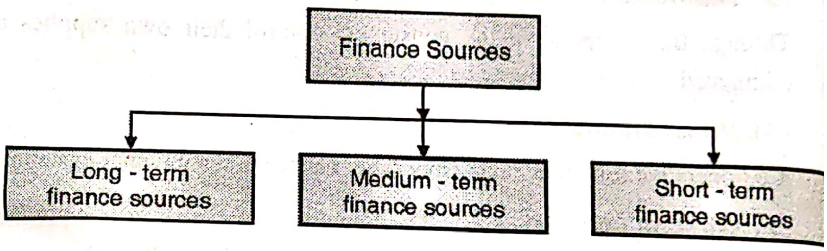

Fig. 2.12.1 : Sources of Finance

Sources of Long term finance

(1) Equity share (2) Preference share (3) Venture capital funding
(4) Asset securitization (5) Retained earnings (6) Bank Loans (7) Bonds

Portion of a company's net profits that are not distributed to shareholders

Sources of Medium term finance

(1) Debentures (2) Financial institutions (3) Foreign currency bonds
(4) State financial corporations (5) Lease financing. (6) Sources of Short term finance:
(7) Trade credit – Supplier allows buyer to purchase product (8) Commercial Banks (9) Bill Discounting
(10) Fixed deposits (period of 1 year or less) (11) Advances

Payment later

2.13 POLICIES GOVERNING SMES (Small and Medium Enterprises)

- To promote a vibrant business community and generate employment, the Government of India provides a host of subsidies and incentives for business. For any entrepreneur managing a start-up or an established business, it is important to know about these subsidies and incentives – so that these subsidies are availed while incurring capital expenditure to reduce capital cost, lessen interest burden and achieve break-even faster.
- We now present a list of 7 Must Know Subsidies for an Indian Entrepreneur.

Asset securitization – is the process of converting illiquid assets, like loans or receivables into marketable securities

Debenture – a type of debt instrument used by companies & govt's to raise capital from investors.

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Preference share : also called Preferred stock, a type of co share that pays dividends to shareholders before any divide are given to common shareholders

Credit Linked Capital Subsidy Scheme [CLCSS]

- Many of the Small Scale Industries (SSI) in India continue to manufacture goods and products with outdated technology and plant & machinery due to the lack of awareness about access to capital, quality standards and modern technology.
- However, the globalization and liberalization of the market, has necessitated upgradation and modernization of equipment to ensure survival and growth of the unit.
- Therefore in an effort to facilitate the technology upgradation of SSI in India, the Ministry of Small Scale Industries is operating a scheme for technology upgradation called the Credit Linked Capital Subsidy Scheme.
- The CLCSS provides 15% capital subsidy to SSI units on institutional finance availed by them for the induction of well established and improved technology in many of the sub-sectors/products approved under the scheme for a loan of upto Rs.1 crore.

Subsidy for Establishing Cold Chain

- A strong and dynamic food processing sector plays a vital role in reduction in the wastage of perishable agricultural produce, enhancing shelf life of food products, enhancing income of farmers and creating surplus for the export of agro& processed foods. Therefore, in an effort to develop a strong food processing industry, the Ministry of Food Processing Industry provides a subsidy for establishing cold chain.
- The objective of this scheme is to provide financial assistance for integrated cold chain and preservation infrastructure facilities without any break from the farm gate to the consumer.
- It covers pre-cooling facilities at production sites, reefer vans, mobile cooling units as well as value addition centres which includes infrastructural facilities like processing/multi-line processing/collection centres, etc. for horticulture, organic produce, marine, dairy, meat and poultry etc.
- Financial assistance (grant-in-aid) of 50% the total cost of plant and machinery and technical civil works in general areas and 75% for NE region including Sikkim and difficult areas (J&K, Himachal Pradesh and Uttarakhand), subject to a maximum of Rs.10 crore is provided as financial assistance under this scheme.

Technology Upgradation Fund Scheme (TUFS) – Textile Sector

- The Textiles sector is the second largest provider of employment after agriculture. It contributes about 14% to industrial production, 4% to the GDP, and 17% to the country's export earnings. It provides direct employment to over 35 million people, which includes a substantial number of SC/ST, and women.
- Therefore, the Ministry of Textiles through its flagship scheme, the Technology Upgradation Fund Scheme(TUFS) has helped the industry scale new heights and improve technology to match global standards. Under the TUFS Scheme, Interest Reimbursement of 5% is provided on interest charged by the financial institutions or banks for textile technology upgradation projects.
- In addition, the scheme also provides for margin money and/or capital subsidy for investment in many types of textiles manufacturing equipment like powerlooms, common effluent treatment plants, garmenting machinery, machinery for technical textiles, handlooms, etc.

Subsidy for Acquiring Quality Management System

- With a competitive global market, implementation of quality standard has become mandatory for MSME units to successfully compete and improve profitability by optimizing internal processes.
- Therefore, in an effort to increase the adoption of quality standards by Indian MSME units, the Government of India provides a subsidy, wherein the cost of acquiring ISO Certifications like ISO 9000 and ISO 14001 is subsidized.
- The scheme provides for all units having an SSI Registration to have reimbursement of charges of acquiring ISO-9000/ISO-14001 certifications to the extent of 75% of the expenditure subject to a maximum of Rs.75,000/- in each case.

GDP – gross domestic Product

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Interest Subsidy for MSME Units in Gujarat

- The Gujarat State Government in an effort to boost industrial investment and make the state more investor friendly provides for interest subsidies to MSME units that are making new investment or existing units that are investing in capacity addition or diversification or existing units that are investing in modernization of machinery to newer technology. MSME's are the backbone of any economy and this subsidy is setup to make Gujarat among the highly industrialized state in the country today.
- Through this scheme, an interest subsidy of upto 7% for micro enterprises and 5% for small and medium enterprises is provided. An additional 1% interest subsidy is provided to youth having less than 35 years of age in case of first project. Woman entrepreneurs are also accorded priority. The maximum amount of interest subsidy provided per annum is Rs.25 lakhs for upto a period of 5 years.

Capital Subsidy for Solar Lighting and Small Capacity PV Systems

- The Government of India has launched the Jawaharlal Nehru National Solar Mission (JNNSM) to promote sustainable energy generation and support the growing need for energy in India while addressing India's energy security challenge. The JNNSM provides a host of subsidies and soft loans for the promotion and penetration of solar energy generation in the nation.
- Through the capital subsidy for solar lighting and small capacity PV systems, the JNNSM provides capital subsidy of upto 40% of the approved unit cost (benchmark cost) for solar lighting systems and small capacity Photovoltaic systems. Capital subsidy of 90% of the benchmark cost, would be available for special category states, viz. NE, Sikkim, J&K, Himachal Pradesh and Uttarakhand.

Support for International Patent Protection in Electronics & IT

- Department of Information Technology, MCIT, GOI has started a scheme to provide financial support to SMEs and Technology Start-Up units for international patent filing so as to encourage indigenous innovation and to recognize the value and capabilities of global IP and capture growth opportunities in the area of information technology and electronics.
- Through this scheme, all patent processing costs including Attorneys' Fees, Patent Office filing fees, Examination Fees, Patent Search cost, Additional cost for entering National Phase upto grant/issue is subsidized. The scheme provides reimbursement of upto 50% of the total patent cost. Support will be limited to Rs.15 lakhs or 50% of the total expenses incurred on filing each invention whichever is less. .

2.14 FINANCIAL INSTITUTIONS SUPPORTING ENTREPRENEURS

In addition to the above mentioned sources of finance for entrepreneurs the following financial assistance is provided by various financial institutes.

Industrial development Bank of India

2.14.1 Seed Capital Assistance

- The seed capital assistance scheme is designed by IDBI for professionally or technically qualified entrepreneurs and / or persons possessing relevant experience, skills and entrepreneurial traits.
- The project cost should not exceed Rs. 2 cores and the maximum assistance under the project will be restricted to 50% of the required promoters contribution or Rs. 15 lacs whichever is lower.
- The Seed Capital Assistance is interest free but carries a service charge of one percent for the first five year and 10% p.a. thereafter. However, IDBI will have the option to change interest at such rate as may be determined by IDBI based on the financial position and profitability of the company.
- The repayment schedule is fixed depending upon the repaying capacity of the unit with an initial moratorium upto five years.
- For projects with a project cost exceeding Rs. 200 lacs, seed capital may be detained from the Risk Capital and Technology Corporation Ltd. (RCTC). For small projects costing upto Rs. 5 lacs, assisted under the Natural Equity Fund of SIDBI may be availed.

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2.14.2 Government Subsidies

- The central and state governments provide subsidies to Industrial units located in backward areas.
- The central government has classified backward areas into three categories of districts: A, B and C., The central subsidy applicable to industrial projects in these districts are :
  (1) Category A Districts : 25 percent of the fixed capital investment subject to A maximum of Rs.25 lakh
  (2) Category B Districts : 15 per cent of the fixed capital investment subject to A maximum of Rs.15 lakh
  (3) Category C Districts : 10 per cent of the fixed capital investment subject to A maximum of Rs.10 lakh.
- The state governments also offer cash subsidies to promote widespread dispersal of industries within their states.
- Generally, the districts notified in the state subsidy schemes are different from those covered under the central subsidy scheme.
- The state subsidies vary between 5 per cent to 25 per cent of the fixed capital investment in the project, subject to a ceiling varying between Rs.5 lakh and Rs.25 lakh depending on the location.

Example : Satavahana Ispat Limited has been set up with the capacity to manufacture 1,20,000 tones of pig iron.

- The cost of project has been appraised by IDBI at Rs.5,450 lakh and is to be mainly financed through equity capital and term loans. The unit is also eligible for a State Government Subsidy (Andhra Pradesh) of Rs.20 lakh, which will also be a source of long-term finance.
- The unit is located at Anantapur District of Andhra Pradesh and falls into" Category backward area.

2.14.3 Sales Tax Deferments and Exemptions

- To attract industries, the state provides incentives, in the form of sales tax deferments and sales tax exemptions.
- Under the sales tax deferment scheme, the payment of sales tax on the sale of finished goods may be deferred for a period ranging between five to twelve years. Essentially, it implies that the project gets an interest-free loan, represented by the quantum of Sales Tax deferment period.
- Under the sales tax exemption scheme, some states exempt the payment of sales tax applicable on purchase of raw materials, consumables, packing and processing materials from within the state while used for manufacturing purposes.
- The period of exemption ranges from three to nine years depending on the state and the specific location of the project within the state.
- Lupin Chemicals Ltd has stated in their prospects that they are eligible for sales tax incentive for a period of five years or till they reach the ceiling of 60% of fixed capital investment whichever is earlier.

2.14.4 Unsecured Loans and Deposits

- Unsecured loans are normally provided by the promoters to fill the gap between the promoters contribution required by financial institutions and the equity capital subscribed to by the promoters.
- These loans are subsidiary to the institutional loans. The rate of interest chargeable on these loans is less than the rate of interest on the institutional loans.
- The loans cannot be taken back without the prior approval of the financial institutions.
- Deposits from the public, referred to as public deposits, represent unsecured borrowing of one to three years (five years in the case of non-banking finance companies) duration.
- Many existing companies prefer to raise public deposits instead of term loans from financial institutions because restrictive covenants do not accompany public deposits.
- However, it may not be possible for a new company to raise public deposits and it may be difficult to repay public deposits within three years.

Chapter Ends...

Bill discounting – a financial service where businesses sell their outstanding invoices to a financial institution (like a bank) before due date, receiving immediate cash in return for a discounted fee.

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