CHAPTER 1: THE NATURE OF ENTREPRENEURSHIP

1.1 INTRODUCTION

The word ‘entrepreneur’ is widely used, both in everyday conversation and as a technical term in management and economics. Its origin from a French word, ***entreprender***, where an entrepreneur was an individual commissioned to undertake a particular commercial project. A number of concepts have been derived from the idea of the entrepreneur such as entrepreneurial, entrepreneurship and entrepreneurial process. The idea that the entrepreneur is someone who undertakes certain projects offers an opening to developing an understanding of the nature of entrepreneurship. Undertaking particular projects demands that particular tasks be engaged in with the objective of achieving specific outcomes and that an individual take charge of the project. Entrepreneurship is then what the entrepreneur does. Entrepreneurial is an adjective describing how the entrepreneur undertakes what he or she does. The entrepreneurial process in which the entrepreneur engages is the means through which new value is created as a result of the project: the entrepreneurial venture.

Chapter Objectives

This chapter is concerned with developing a predominant and integrated perspective of the entrepreneur and entrepreneurship. It reviews the great variety of definitions given for the word entrepreneurship and also the different activities performed by the entrepreneur.

After completing this chapter, students will be able to:

- Define the term entrepreneurship and entrepreneur
- Identify types of entrepreneur
- Recognize the role of entrepreneurship in the economy
- Analyze the entrepreneurial competences
- Understand creativity and innovation

1.2 Historical Origin of Entrepreneurship

What is entrepreneurship? And who is an entrepreneur? These two questions are asked more frequently reflecting the increasing demand in the field of entrepreneurship. Offering a specific and unambiguous definition of the term entrepreneurship /entrepreneur presents a challenge. This is not because definitions are not available, but because there are so money. Here let us took in to the historical development of entrepreneurship so as to grasp the meaning of the word entrepreneurship.

During the ancient period the word entrepreneur was used to refer to a person managing large commercial projects through the resources provided to him.

In the 17th Century a person who has signed a contractual agreement with the government to provide stipulated products or to perform service was considered as entrepreneur. In this case the contract price is fixed so any resulting profit or loss reflects the effort of the entrepreneur. In the 18th Century the first theory of entrepreneur has been developed by Richard Cantillon. He said that an entrepreneur is a risk taker. If we consider the merchant, farmers and /or the professionals they all operate at risk. For example, the merchants buy products at a known price and sell it at unknown price and this shows that they are operating at risk. The other development during the 18th Century is the differentiation of the entrepreneurial role from capital providing role. The later role is the base for today's venture capitalist.

In the late 19th and early 20th Century an entrepreneur was viewed from economic perspectives. The entrepreneur organizes and operates an enterprise for personal gain. In the middle of the 20th Century the notion of an entrepreneur as an inventor as established. "The function of the entrepreneur is to reform or revolutionize the pattern of production by exploiting an invention or more generally untried technological possibility for producing new commodities or producing an old one in a new way or opening a new outlet for products by reorganizing a new industry."

The concept of innovation and newness are at the heart of the above definition. From the historical development it is possible to understand the fact that the perception of the word entrepreneur was evolved from managing commercial project to the application of innovation (creativity) in the business idea.

1.3 Definitions of Entrepreneurship and Entrepreneur

Here we will see some definitions of entrepreneurship and entrepreneur. Intuitively, it is know that entrepreneurship is the process and entrepreneur is the person undertaking entrepreneurial activity such as undertaking own business. Finally we will see the common attributes of the definitions of entrepreneurship and entrepreneur.

1. Entrepreneurship is the process of identifying opportunities in the market place, arranging the resources required to pursue these opportunities and investing the resources to exploit the

opportunities for long term gains. It involves creating incremental wealth by bringing together resources in new ways to start and operate an enterprise.

2. Entrepreneurship is the processes through which individuals become aware of business ownership then develop ideas for, and initiate a business.
3. Entrepreneurship can also be defined as the process of creating something different and better with value by devoting the necessary time and effort by assuming the accompanying financial, psychic and social risks and receiving the resulting monetary reward and personal satisfaction. In this case an individual should come up with something different and better in order to the named as entrepreneur.
4. Entrepreneurship is the art of identifying viable business opportunities and mobilizing resources to convert those opportunities into a successful enterprise through creativity, innovation, risk taking and progressive imagination.

Entrepreneurship is a practice and a process that results in creativity, innovation and enterprise development and growth. It refers to an individual's ability to turn ideas into action involving and engaging in socially-useful wealth creation through application of innovative thinking and execution to meet consumer needs, using one's own labor, time and ideas. Engaging in entrepreneurship shifts people from being "job seekers" to "job creators", which is critical in countries that have high levels of unemployment. It requires a lot of creativity which is the driving force behind innovation.

In general, the process of entrepreneurship includes five critical elements. These are:

1) The ability to perceive an opportunity.
2) The ability to commercialize the perceived opportunity i.e. innovation
3) The ability to pursue it on a sustainable basis.
4) The ability to pursue it through systematic means.
5) The acceptance of risk or failure.

Based on the above concepts of entrepreneurship, an entrepreneur can be defined as follows:

1) An entrepreneur is any person who creates and develops a business idea and takes the risk of setting up an enterprise to produce a product or service which satisfies customer needs.
2) An entrepreneur can also be defined as a professional who discovers a business opportunity to produce improved or new goods and services and identifies a way in which resources required can be mobilized.

3) An entrepreneur is an individual who: has the ability to identify and pursue a business opportunity; undertakes a business venture; raises the capital to finance it; gathers the necessary physical, financial and human resources needed to operate the business venture; sets goals for him/herself and others; initiates appropriate action to ensure success; and assumes all or a major portion of the risk!
4) An entrepreneur is a person who: create the job not a job-seeker; has a dream, has a vision; willing to take the risk and makes something out of nothing
5) Other definition, views the term entrepreneur from three perspectives; i.e. from the economist, psychologist and capitalist philosopher's point of view.
   i) To an economist an entrepreneur is one who brings resource, labor, materials, and other assets into combination that makes their value greater than before and also one who introduces changes innovations.
   ii) To a psychologist an entrepreneur is a person typically driven by certain forces need to obtain or attain something, to experiment, to accomplish or perhaps to escape the authority of others.
   iii) For the capitalist philosopher an entrepreneur is one who creates wealth for others as well, who finds better way to utilize resources and reduce waste and who produce job others are glad to get.

In general, entrepreneur refers to the person and entrepreneurship defines the process. Both men and women can be successful entrepreneurs; it has nothing to do with gender. All entrepreneurs are business persons, but not all business persons are entrepreneurs.

1.4 Types of Entrepreneurs

Entrepreneurship can take three different forms. They are:

1. **The individual entrepreneur:** An individual entrepreneur is someone who started; acquired or franchised his/her own independent organization. The major portion of this module is also devoted to describe the basic features and activities of the individual entrepreneur.
2. **Intrapreneur:** An Intrapreneur is a person who does entrepreneurial work within large organization. The process by which an intrapreneur affects change is called Intrapreneurship.

There are two facts about intrapreneurship

a. The Intrapreneur's context is often large and bureaucratic organization whereas the individual entrepreneur operates in the broader, more flexible economic market place.
b. Intrapreneurs are individuals who often engage in the entrepreneurial actions in large organizations without the blessing of their organizations.

3. **The Entrepreneurial Organization:** The entrepreneurial function need not be embodied in a physical person. Every social environment has its own way of filling the entrepreneurial function.

Individuals working in organizations have the potential for being, as do those working independently to start their own business. An organization can create an environment in which all of its members can contribute in some function to the entrepreneurial function.
An organization that creates such an internal environment is defined as entrepreneurial organization.

1.5 Role of Entrepreneurs in Economic Development

Entrepreneurial development is the most important input in the economic development of any country. The objectives of industrial development, balanced regional growth, and generation of employment opportunities are achievable through entrepreneurial development. Entrepreneurs are at the core of industrial development which results in greater employment opportunities to the unemployed youth, increase in per capita income, higher standard of living and increased revenue to the government in the form of income, sales tax, export duties, import duties etc. The entrepreneurs serve as a key to the creation of new enterprises, thereby rejuvenating economy and sustaining the process of economic development in the following ways:

1) **Improvement in per capita Income/Wealth Generation**: Entrepreneurs play a vital in the economic development of a region. From the fall of Rome (AD 476) to the eighteenth century, there was virtually no increase in per capita wealth generation in the West. With the advent of entrepreneurship, however, per capita wealth generation and income in the west grew exponentially by 20 Percent in the 1700s, 200 percent in the 1800s, 740 percent in the 1900 (Drayton, 2004).
2) **Generation of Employment Opportunities:** By creating a new business enterprise, entrepreneurs generate employment opportunities for others. Unemployment is a major issue, especially in the context of developing economies like Ethiopia. Educated youth often

are unable to get to get a suitable employment themselves. Thus, entrepreneurs not only self-employ themselves, but also create jobs for others.

3) **Inspire others Towards Entrepreneurship**: The team created by an entrepreneur for his new undertaking often provides the opportunity for the employees to have a first-hand experience of getting involved in an entrepreneurial Venture. An existing venture provides a number of entrepreneurial opportunities through forward and backward linkages, to these employees even to become entrepreneurs themselves. Thus, this process helps in forming a chain reaction of entrepreneurial activity which directly contributes to the health of the economy.
4) **Balanced Regional Development**: Entrepreneurs help to remove regional disparities in economic development. They set up the industries in the backward areas to avail various subsidies and incentives offered by the Central and State Governments, thereby balancing the economic growth in different regions in the country.
5) **Enhance the Number of Enterprise**: When new firms are created by entrepreneurs, the number of enterprises based upon new ideas/ concepts/ products in a region increases. Not only does an increase in the number of firms enhance the competition for new ideas, but greater competition across firms also facilitates the entry of new firms specializing in a particular new product or service. This is because the necessary complementary inputs are more likely available from small specialist niche firms than from large vertically integrated products (Jacobs, 1969).
6) **Provide Diversity in Firms**: Entrepreneurial activity often results into creation of a variety of firms in a region. These firms operate into diverse activities and it has been found that it is this diversity in firms which fosters economic development and growth rather than homogeneity. According to Jacobs (1969), it is the exchange of complementary knowledge across diverse firms and economic agents that yield an important return on new economic knowledge.
7) **Economic Independence**: Entrepreneurship is essential for self-reliance for a country. Entrepreneurs create industries that manufacture indigenous substitutes, thereby reducing the dependence on imports. Also, the goods are exported to other countries to earn foreign exchange. This import substitution and export promotion results in more economic independence to the country

8) **Combine Economic factors:** All the products bought and sold in an economy are a mix of three primary economic factors (the raw materials, nature offers up, the physical and mental labor people provide and capital (money). Now value is created by combing these three things together in a way which satisfies human needs.

9) **Provide Market efficiency:** Efficient means resources are distributed in an optimal way that is the satisfaction that people can gain from them is maximized. An economic system can only reach this state if there is competition between different suppliers. If a supplier is not using competition then they will tend to demand profit in excess of what the market would allow and reduce the overall efficiency of the system

10) **Accepting Risk:** Risk is the potential variation in terms of future outcomes. We do not know exactly what the future will bring. This lack of knowledge creates uncertainty. No matter how we plan there is always a possibility of adverse deviation from what we expect or hoped for. Here the primary function of the entrepreneur is to accept risk on behalf of other people.

11) **Maximize Investor's Return:** Entrepreneurs create and run organizations which maximize long-term profit on behalf of the investors which in turn generates overall economic efficiency.

1.6 Entrepreneurial Competence and Environment

Under this topic entrepreneurial mindset (that will address subtopics such as, who become an entrepreneur; qualities of successful entrepreneurs; entrepreneurial skills; the entrepreneur's task and wealth of the entrepreneur), and Entrepreneurship and Environment.

1.6.1 Entrepreneurial Mindset

1.6.1.1 Who Becomes an Entrepreneur?

Anyone with the following characteristics can be an entrepreneur.

1) **The Young Professional:** Increasingly young highly educated people often with entrepreneurial qualifications are skipping the experience of working for an established organization and moving directly to work on establishing their own ventures.

2) **The Inventor:** The inventor is someone who has developed an innovation and who has decided to make a career out of presenting that innovation to the market. It may be a new product or it may be an idea for a new service. It may be a high-tech or it may be based on a traditional technology.

3) **The Excluded:** Some people turn to an entrepreneurial career because nothing is open to them. Displaced communities and ethnic and religious minorities have not been invited to join the wider economic community due to a variety of social, cultural and political and historical reasons. As a result they may form their own internal networks, trading among themselves and, perhaps, with their ancestral countries.

1.6.1.2 Qualities of an Entrepreneur

In order to be successful, an entrepreneur should have the following qualities:

- Opportunity-seeking
- Persevering
- Risk Taking
- Demanding for efficiency and quality
- Information-seeking
- Goal Setting
- Planning
- Persuasion and networking
- Building self-confidence
- Listening to others
- Demonstrating leadership

1) Opportunity-seeking: An opportunity is a favorable set of circumstances that creates a need for a new product, service or business. It includes access to credit, working premises, education, trainings etc. An entrepreneur always seeks out and identifies opportunities. He/she seizes an opportunity and converts it into a realistic and achievable goal or plan.

2) Persevering: An entrepreneur always makes concerted efforts towards the successful completion of a goal. An entrepreneur perseveres and is undeterred by uncertainties, risks, obstacles, or difficulties which could challenge the achievement of the ultimate goal.

Activity 1.1: Understanding perseverance

Objective of activity: To enable students to internalize the concept of perseverance
The story of Thomas Edison (please adapt to the context) When he was young, Thomas Edison's parents took him out of school after his teachers declared that he was "stupid" and "unteachable." Edison spent his early years working and being fired from various jobs, culminating in his firing from a telegraph company at the age of 21. Despite these numerous setbacks, Edison was never discouraged from his true calling in life: inventing! Throughout his career, Edison obtained more than one thousand patents. And although several of these inventions such as the light bulb,

stock printer, phonograph and alkaline battery -- were groundbreaking innovations, the vast majority of them could be fairly described as failures. Edison is now famous for saying that genius is "1% inspiration and 99% perspiration." One of Edison's best examples of perseverance occurred after he was already a successful man. After inventing the light bulb, he began seeking an inexpensive light bulb filament. At the time, ore was mined in the Midwest of the United States, and shipping costs were very high. In order to minimize his costs with ore, Edison established his own ore-mining plant in Ogdensburg, New Jersey. For nearly ten years, he devoted his time and money to the enterprise. Edison also obtained 47 patents for innovations that helped make the plant run more smoothly. And even despite those inventions, Edison's core project failed because of the low quality of ore on the East Coast. However, despite that failing, one of those 47 inventions (a crushing machine) revolutionized the cement industry, and actually earned Edison back almost all of the money he had lost. Later, Henry Ford would credit Edison's Ogdensburg project as the main inspiration for his Model T Ford assembly line. And in fact, many believe that Edison paved the way for modern-day industrial laboratories. Edison's foray into ore-mining demonstrates that dedication can pay off even in a losing venture.
Instructions: Read the story of Thomas Edison for the students
Reflection questions: • What are the major challenges that Thomas Edison faced? • What were his achievements? • What are the causes for his success? • What do we learn from the story of Thomas Edison?

3) **Risk Taking:** The best entrepreneurs tend to:-

- ☞ Set their own objectives where there is moderate risk of failure and take calculated risks
- ☞ Gain satisfaction from completing a job well
- ☞ Not be afraid of public opinion, skepticism
- ☞ Take responsibility for their own actions

Importance of Risk-taking

- ☞ Build self confidence
- ☞ Create a feeling of leadership
- ☞ Create strong motivation to complete a job well

4) Demanding for Efficiency and Quality

Efficiency: Being efficient means producing results with little wasted effort.

Quality refers to:

1. The ongoing process of education, communication, evaluation and constant improvement of goods/services to meet the customer's need in a way that exceeds the customer's expectations;
2. A characteristic of the product or service that makes it fit to use. It makes a product, process, or service desirable.

3. The ability of a product or service to meet a customer's expectations for that product or service.

The importance of quality management in entrepreneurship is reflected in the income statement of the business. There is always a demand for quality products and efficient services. Quality plays an important role in this new era of globalization because it confers certain benefits which include:

- **Reduction of waste**: Striving to maintain quality means examining all processes that contribute to the creation of a product, to remove non-productive processes and waste. If businesses keep to their standard of maintaining the quality of the product, the number of defective products will be reduced. Consumers prefer to buy quality products. Hence the quality products/services help in increasing the share in market and ensure that they will not be returned.
- **Cost-effectiveness**: Striving to ensure quality helps businesses to minimize the chances that they will make mistakes. As a result, the costs of re-doing work or changing the product after it has been sold are greatly reduced.
- **An increase in market share**: Customers prefer to buy the same product again and again if they are satisfied with the quality. If they are satisfied with the quality of a product, then they will not only purchase the product/services more than once, but they will also recommend it to their friends. As a result, this contributes to an increase in the company's market share.
- **Better profitability**: Better quality of product satisfies customers. Increased customers means increase sales, increased shares in market and consequently increased profits.
- **Social responsibility**: By providing quality products and services, a company is more likely to be able to fulfill its responsibility to the community and meet standards set by government.
- **Reputation:** Quality of goods and services improves the reputation of the business for competition in the market and growth.

5) **Information-seeking:** Successful entrepreneurs do not rely on guesswork and do not rely on others for information. Instead, they spend time collecting information about their customers, competitors, suppliers, relevant technology and markets. Gathering relevant information is important to ensure that the entrepreneur makes well informed decisions. Information on the

area of market, supply, operations, finance, legislation, and infrastructure are important for entrepreneurs.

6) Goal Setting

A Goal - is a general direction, or long-term aim that you want to accomplish. It is not specific enough to be measured. It is large in scope, not necessarily time-bound, and is something that people strive for by meeting certain objectives which will hopefully add up to eventually achieving the goal.

Objectives - are specific and measurable. They are concise and specific. Think of the word "**object.**" You can touch it, it's there, it's actual, and it's finite.

An entrepreneur must have a goal and an objective which is specific, measurable, attainable relevant, and time bound (SMART).

- ☞ Specific: Great goals are well-defined and focused. The moment you focus on a goal, your goal becomes a magnet, pulling you and your resources toward it. The more focused your energies, the more power you generate.
- ☞ Measurable: A goal without a measurable outcome is like a sports competition without a scoreboard or scorekeeper. Numbers are an essential part of business. Put concrete numbers in your goals to know if you're on track.
- ☞ Attainable: Far too often, entrepreneurs can set goals which are beyond their reach. Dream big and aim for the stars but keep one foot firmly based in reality.
- ☞ Relevant: Achievable business goals are based on the current conditions and realities of the business climate. For example, you may desire to have your best year in business or increase revenue by 50%, but if a national economic crisis is looming and three new competitors just opened in your market, then your goals are not relevant to the realities of the market.
- ☞ Time-Based: Business goals and objectives just don't get done when there's no time frame tied to the goal-setting process. Whether your business goal is to increase revenue by 20% or to find two new clients, it is important to choose a time-frame to accomplish your goal.

7) Planning: Planning is making a decision about the future in terms of what to do, when to do, where to do, how to do, by whom to do and using what resources. An effective entrepreneur therefore usually plans his/her activities and accounts as best as they can for unexpected eventualities.

8) Persuasion and Networking

Persuasion is a way of convincing someone to get something or make a decision in your favor. It is inducing or taking a course of action or embracing a point of view by means of argument, reasoning, or entreaty; to convince; to succeed in causing a person to do or consent to something; to win someone over, as by reasoning or personal forcefulness; to cause to believe; to induce, urge, or prevail upon successfully.

Importance of Persuasion in Business

- ☞ We purchase goods from people
- ☞ We sell goods to people
- ☞ We need support from people
- ☞ We work with people.

Without people, be they are suppliers, workers, and most importantly customers, there is no business.

Networking is an extended group of people with similar interests or concerns who interact and remain in informal contact for mutual assistance or support. In a business environment where we are in, we network with customers, suppliers, competitors, various firms, different organizations, government offices and family, etc.

Factors that Affect Persuasion and Networking

- ☞ Socio-cultural background and perceptions
- ☞ Communication skills (both verbal and non-verbal).
- ☞ Negotiation skills

9) Building Self-confidence: Self-confidence is the state of being certain that a chosen course of action is the best or most effective given the circumstances. Confidence can be described as a subjective, emotional state of mind, but is also represented statistically as a confidence level within which one may be certain that a hypothesis will either be rejected or deemed plausible. Self-confidence is having confidence in oneself when considering a capability. Overconfidence is having unmerited confidence-believing something or someone is capable when they are not.

Characteristics of a Self-confident Person

A person with self-confidence may exhibit some of the following characteristics:

- ☞ Risk-taking: willing to take risks and go the extra mile to achieve better things.
- ☞ Independent: entrepreneurs like to be their own masters and want to be responsible for their own decisions.
- ☞ Perseverance: Ability to endure and survive setbacks and continue to build confidence in whatever you do in your business.
- ☞ Able to learn to live with failure. Entrepreneurs are going to make mistakes. They are human. But they learn from these mistakes and then move on.
- ☞ Ability to find happiness and contentment in work.
- ☞ Doing what you believe to be right, even if others mock or criticize you for it.
- ☞ Admitting mistakes and learning from them

Activity 1.2:

1) Think about your life so far, and list the five major achievements in personal life.

1.____________________________________ 2.____________________________________

3.____________________________________ 4.____________________________________

5.____________________________________

2) Think about your strengths in running your personal life. Write four of them which you are most proud of?

1.____________________________________ 3.____________________________________

2.____________________________________ 4.____________________________________

3) Think about what's important to you, and where you envision your business in the future. What is the goal of your business?

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4) Build the knowledge and skills that you need to succeed. What do you need to know, do or learn in order to accomplish the business goal stated above?

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5) How do you think you can acquire this knowledge and these skills so that you will be able to move forward confidently?

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6) When you are starting, do not try to do anything clever or elaborate. There is no need to be perfect – just enjoy doing simple things successfully and well. Focus on the basics, set small goals and achieve them, and you will find yourself accelerating towards success! So, what basics or initial steps will you take towards reaching your goal?

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10) Listening to Others: An entrepreneur does not simply impose his/her idea on others. Rather, he/she listens to other people in their sphere of influence, analyses their input in line with his/her own thinking and makes an informed decision.

11) Demonstrating Leadership: An entrepreneur does not only do things by him/herself, but also gets things done through others. Entrepreneurs inspire, encourage and lead others to undertake the given duties in time.

Self-assessment

Activity 3: Complete a self-assessment of your entrepreneurial qualities

Go through the statements below and score yourself to the best of your ability and as honestly as possible. Do not take too long thinking about any one answer, your first guess is probably the most accurate. Use the scoring key below.

Scoring:

5 – Always 4 – Often 3 – Sometimes 2 – Rarely 1 – Never

S. No	**Characteristic**	**1**	**2**	**3**	**4**	**5**
1.	I enjoy doing things on my own. Nobody has to motivate me to get started on a task.					
2.	If I make up my mind to do something, I don’t let anything stop me.					
3.	I do not hesitate to undertake risks related to creating and operating an enterprise.					
4.	I plan my time and resources well so I produce high quality products.					
5.	I assess the time and capacity I have before I commit to accomplishing a job.					
6.	I act upon the opportunities that needs and problems present.					
7.	I keep trying again and again despite great challenges and failure.					
8.	I work hard to try to foresee potential risks so as to prevent future risk.					
9.	I make personal sacrifices to complete jobs in order to keep my word and meet promised deadlines.					

10.	I always strive for improvement and progress despite feedback from people that they are satisfied with my work.					
11.	Before undertaking my job I try to gain as much information about it as I can, and verify the accuracy of the information I am receiving.					
12.	I set short and long-term goals for my personal life and business.					
13.	I do everything I can to accomplish set business goals, through careful planning and implementation.					
14.	I team up well with others for tasks which I cannot accomplish on my own.					
15.	I am able to make decisions on my own, incorporating the suggestions and ideas of others as part of that process.					
16.	I collect all the necessary information I need before I start a job or task.					
17.	I set goals based on the resources and skills I have.					
18.	I have the skills to persuade and communicate with people.					
19.	I regularly evaluate my job performance, looking for areas of improvement.					
20.	I am happy with my work and am confident that I will make progress and improvement in the future.					

Analysis of the Result

Analysis one: Each statement is focused on different entrepreneurial qualities as stated below.

- Question 1+ Question 6 = Opportunity-seeking
- Question 2+ Question 7 = Perseverance
- Question 3+ Question 8 = Risk-taking
- Question 4+ Question 10 = Demand for efficiency and quality
- Question 5+ Question 9 = Commitment to work contract
- Question 11+ Question 16 = Information-seeking
- Question 12+ Question 17 = Goal-setting
- Question 13+ Question 19 = Planning
- Question 14+ Question 18 = Persuasion & Networking
- Question 15+ Question 20 = Self Confidence

Now evaluate how you ranked yourself for that characteristic (based on your score for each of the questions). For example, if you rated yourself a “5” for both questions 1 and 6, then according to the key above, you have a strong opportunity seeking trait. If you rated yourself a “1” or a “2” for questions 14 and 18, then perhaps persuasion and networking are not among your strengths right now – and could be skills for you to work on.

Analysis two: Add up your total score from all the numbers you wrote in each row. Write your total sum here, and then interpret it below:

Total Sum = _____________

Result Interpretation:

Score	**Meaning**
< 50:	Limited entrepreneurial qualities at the moment. It does not mean you are not meant to be a businessperson. It only means that you should spend more time preparing yourself to handle any problems you might face once you start a business.
Between 50 – 80	Average - there are gaps that need to be filled or improved upon. You might consider upgrading your knowledge or skills. Consider taking some courses.
>80	Good entrepreneur - keep it up and continue to develop.

1.6.1.3 Entrepreneurial Skills

A skill is simply knowledge which is demonstrated by action. It is an ability to perform in a certain way. An entrepreneur is someone who has a good business idea and can turn that idea into reality. To be successful, an entrepreneur must not only identify an opportunity but also understand it in great depth. He or she must be able to spot a gap in the market and recognize what new products or services fill the gap. He or she must know what features it will have and why they will appeal to the customer. The entrepreneur must also know how to inform the customer about it and how to deliver the new offerings. All this calls for an intimate knowledge of a particular sector of industry. Turning an idea into reality calls upon two sorts of skills, these are:

I. General management skills and
II. People management skills

I) General Management Skills: These are skills required to organize the physical and financial resources needed to run the venture. Some of the most important general management business skills are:

- ***Strategy Skills* –** An ability to consider the business as a whole, to understand how it fits within its market place, how it can organize itself to deliver value to its customers, and the ways in which it does this better than its competitors.
- ***Planning Skills* –** An ability to consider what the future might offer, how it will impact on the business and what needs to be done to prepare for it now.

- ☞ ***Marketing Skills –*** An ability to see past the firm's offerings and their features, to be able to see how they satisfy the customer's needs and why the customer finds them attractive.
- ☞ ***Financial Skills –*** An ability to manage money; to be able to keep track of expenditure and to monitor cash-flow, but also an ability to assess investments in terms of their potential and their risks.
- ☞ ***Project Management Skills –*** An ability to organize projects, to set specific objectives, to set schedules and to ensure that the necessary resources are in the right plat of the right time.
- ☞ ***Time Management Skills –*** An ability to use time productively, to be able to priorities important jobs and to get things done to schedule.

II) People Management Skills: Businesses are made by people. A business can only be successful if the peoples who make it up are properly directed and are committed to make an effort on its behalf. An entrepreneurial venture also needs the support of people from outside the organization such as customers, suppliers and investors. To be effective, an entrepreneur needs to demonstrative a wide variety of skills in the way he/she deals with other peoples. Some of the more important skills we might include under this heading are:

- ☞ ***Communication Skills*** – An ability to use spoken and written language to express ideas and inform others.
- ☞ ***Leadership Skills*** – An ability to inspire people to work in a specific way and to undertake the tasks that are necessary for the success of the venture.
- ☞ ***Motivation Skills*** – An ability to enthuse people and get them to give their full commitment to the tasks in hand. Being able to motivate demands an understanding of what drives people and what they expect from their jobs.
- ☞ ***Delegation Skills*** – An ability to allocate tasks to different people. Effective delegation involves more than instructing. It demands a full understanding of the skills that people possess how they use them and how they might be developed to fulfill future needs.
- ☞ ***Negotiation Skills*** – An ability to understand what is wanted from a siturations, what is motivating others in that situation and recognize the possibilities of maximizing the outcomes for all parties.

All these different people skills are interrelated. Here entrepreneurial performance results from a combination of industry knowledge, general management skills; people skills and personal motivation (see the figure shown below). The successful entrepreneur must not only use these skills but learn to use them and to learn from using them. Entrepreneurs should constantly avoid their abilities in these areas, recognize their strengths and weaknesses, and plan how to develop these skills in the future.

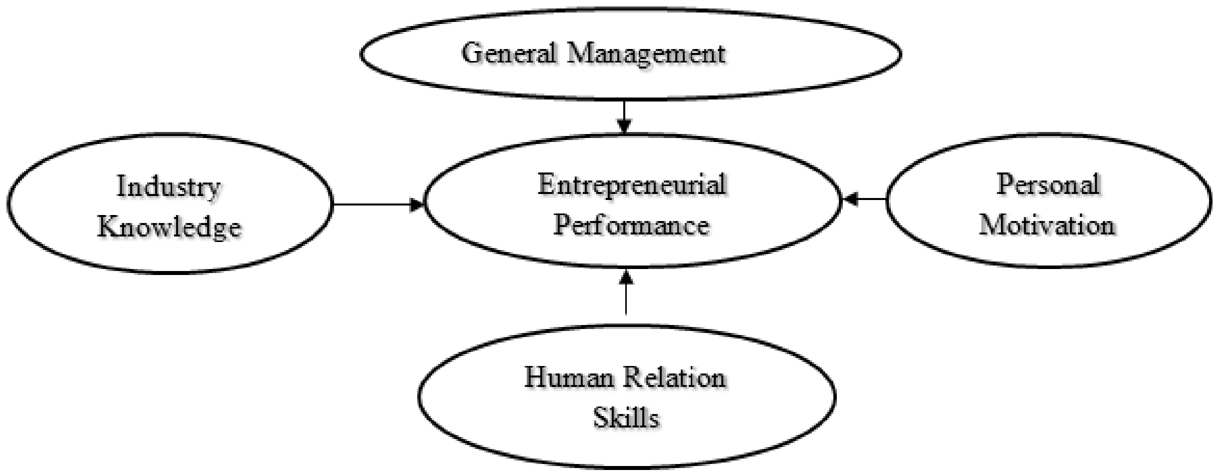

Fig1.1: entrepreneurial skills

1.6.1.4 The Entrepreneurial Tasks

We recognize entrepreneurs, first and foremost, by what they actually do – by the tasks they undertake. A number of tasks have been associated with the entrepreneur. Some of the more important are:

1) **Owning Organizations:** Ownership lies with those who invest in the business and own its stock – the principals, while the actual running is delegated to professional agents or managers. Therefore, if an entrepreneur actually owns the business then he is in fact undertaking two roles at the same time that of an investor and that of a manager. Here we can also recognize many people as entrepreneur even if they do not own the venture they are managing.
2) **Founding New Organizations:** The entrepreneur is recognized as the person who undertakes the task of bringing together the different elements of the organization (people, property, productive resource, etc.) and giving them a separate legal entity. The entrepreneur makes major changes in their organizational word.

3) **Bringing Innovations to Market:** The idea of innovation encompasses any new way of doing something so that value is created. Innovation can mean a new product or service but it can also include a new way of delivering an existing product or service, new methods of informing the consumer about the product or new ways of organizing the company.
4) **Identification of Market Opportunity:** An opportunity is the gap in a market where the potential exists to do something better and create value. New opportunities exist all the time but they do not necessarily present themselves. If they are to be exploited they must be actively sought out. Note that opportunity always takes priority over innovation.
5) **Application of Expertise:** A slight more technical notion is that they have a special ability in deciding how to allocate scarce resources in situations where information is limited. It is their expertise in doing this that makes entrepreneurs valuable to investors.
6) **Provision of leadership:** Entrepreneurs can rarely drive their innovation to market on their own. They need the support of other people both from their organizations and from people outside such as investor customer and supplier.
7) **The entrepreneur as manager:** At the end of the day the entrepreneur is a manager. The distinction between an entrepreneur and ordinary manager may lie on what the entrepreneur manager manages, how they manage, their effectiveness and the effect they have as a manager not by the particular tasks they undertake.

1.6.1.5 Wealth of the Entrepreneur

Wealth is money and anything that money can buy. It includes money, knowledge and assets of the entrepreneur.

Who Benefits from the entrepreneur's Wealth?

No entrepreneur works in a vacuum. The venture they create touches the lives of many other people. To drive his/her venture forward, the entrepreneur calls up on the support of a number of different groups. In return for their support these groups expect to be rewarded from the success of the venture. Peoples who have a part to play in the entrepreneurial venture generally are called stakeholder. The stakeholder groups are; employees, investor, supplier, customer, the local community and government. Let us look at the benefits of each stakeholder.

1) **Employees:** They contribute physical and mental labor to the business. Success of the entrepreneurial venture depends on their effort and motivation. Therefore, they are rewarded with:

- ➢ Money – their wage or salary
- ➢ The possibility of owning a part of the firm through share schemes.
- ➢ A stage of which they can develop social relationships.
- ➢ The possibility of personal development.

2) **Investors:** These are the peoples who provide the entrepreneur with the necessary money to start the venture and keep it running. There are two main sorts of investors: stockholders and lenders. Stockholders are those who buy the stock of the company and are true owners of the firm. The actual return of the stockholders varies depending on how the business performs. Lenders, on the other hand, are people who offer money to the venture on the basis of it being a loan. They do not actually own a part of the firm and their return is independent of the businesses performance. They also take priority for payment over shareholders and face lower level of risk than the stockholders.
3) **Supplier:** They are the individuals and organizations who provide the business with the materials, productive assets and information it needs to produce its output. They are paid for providing these inputs.
4) **Customers:** Customers may need to make an investment in using a particular supplier. Changing supplier may involve switching costs and supplier, risk of quality and expenses incurred in changing over to new inputs. The entrepreneur may reward customers by offering quality products, fair prices, regular and consistency of supply, loan arrangement etc.
5) **The local community:** Business has physical locations. The way they operate may affect the people who live and other businesses which operate nearby.

A business has a number of responsibilities, which may be defined or not in national laws, to this local community. Such as:

- ☞ Not polluting their shared environment
- ☞ Contributing and sponsoring local development activities
- ☞ Contribution for political and cultural stabilities and economic improvements
- ☞ Acting in an ethical way.

6) **Government:** The responsibility of government is to ensure that businesses can operate in an environment which has political and economic stability. In addition, it provides central services such as education and health-care. These activities cost money to provide.

Therefore, government should be rewarded for its services. Hence, government taxes individuals and businesses.

1.6.2 Entrepreneurship and Environment

Business environment refers to the factors external to a business enterprise which influence its operations and determine its effectiveness. Business environment may be healthy or unhealthy. Healthy business environment means the conditions are favorable to the growth of business whereas unhealthy environment implies conditions hostile or unfavorable to business operations. Business and its environment interact with each other. Economic system and other conditions in the environment determine the success of business enterprises. The firm and its management have to adjust to the conditions prevalent around it. However, business enterprises try to influence and shape the environment. Successful working of business concerns improves the economic and social conditions in the country.

No business concern can ignore the environment around it except at its own peril. "The penalty of environ mental disregard is heavy. It not only reduces profit margins and makes opportunities for expansion slip, but it also arouses social hostility and makes social environment growingly inhospitable to business operations."

A study of business environment offers the following benefits:

1) It provides information about environment which is essential for successful operation of business firms.
2) It opens up fresh avenues for the expansion of new entrepreneurial operations. The entrepreneurs may come forward with new ideas and with new ventures when they find environment suitable to their enterprises.
3) Knowledge about changing environment enables businessmen to adopt a dynamic approach and maintain harmony of business operations with the environment.
4) By studying the environment entrepreneurs can make it hospitable to the growth of business and thereby earn popular support.

Thus, the entrepreneur should continuously study the nature of environment and its influence on business. However, mere study is not enough. Attempts must be made to influence the environment in order to make it congenial and favorable to entrepreneurial activities. The most successful entrepreneur is one who not only adjusts to the environment but also modifies the environment to suit his requirements through the direct and indirect influences he can exercise over the system.

1.6.2.1 Phases of Business Environment

Business environment may be classified into two broad categories; namely external; and internal environment

A) External Environment

It is the environment which is external to the business and hardly to influence independently. The following are the components of external environment:

i) Economic Environment

Economic environment is of multidimensional nature. It consists of the structure of the economy, the industrial, agricultural, trade and transport policies of the country, the growth and pattern of national income and its distribution, the conditions prevailing in industrial, agricultural and other sectors, the position relating to balance of trade and balance of payments, and other miscellaneous conditions of the economy. There is a close relationship between a business firm and the economic environment around it. The success of a business enterprise depends considerably upon the State and growth of the economy.

ii) Legal Environment

Business must function within the framework of legal structure. Therefore, an adequate knowledge of laws and rules is necessary for efficient managerial performance. When new laws are made and controls exercised through legal enactments, the first reaction of the business community is to oppose them and disobey them. Management should try to understand what should be the right laws and strictly obey them when so made. In addition, it can influence the government to change and improve the law and make it useful to the business community.

There are several business laws in our country. A working knowledge of these laws is very helpful for the entrepreneur. Such knowledge will keep them away from innocent breaches and resultant penalties. Some laws differ from region to region and amendments arc made from time to time. Therefore, the entrepreneur must always keep in touch with those who know the latest position in law. In addition, an entrepreneur should:

b) Read the books that enlighten on the legal side of business
c) Consult government agencies concerned with the implementation of business laws.
d) Retain labor law consultants.

iii) Political Environment

In a democratic country, politics cannot be ignored. Managers and entrepreneurs should understand the working of the political system. Such understanding and concern for national problems will help them in the long run in discharging their responsibilities to the satisfaction of the public.

Public opinion is very important and today's public opinion becomes tomorrow's legislation. Businessmen should, therefore, learn to take public opinion into account in the decision-making process. If business does not learn how to deal adequately with public opinion, it will face a disaster. This does not mean that business should surrender itself to public opinion. Rather, it implies intelligent response in order to change wherever necessary and a constructive approach to problems.

iv) Socio-Cultural Environment

It consist the social and cultural norms of a society in a given period of time. The variables that are appraised are values, beliefs, norms, fashions and fads of a particular society. It can help in understanding the level of rigidity/flexibility of a given society towards a new product/service/concept. Traditional culture should be protected in so far as it is not a hindrance to innovation, motivation, and development.

v) Demographic Environment

It assesses the overall population pattern of a given geographical region. It includes variables like age profile, distribution, sex, education profile, income distribution etc. The demographic appraisal can help in identifying the size of target customers.

B) Internal Environment

Internal environment is the environment which is under the control of a given organization. Following are the components of internal environment of a business:

- **ii) Raw Material:** It assesses the availability of raw material now and in the near future. If the availability of raw material is less now or would be less in future then the entrepreneur should give a serious thought to establishing a venture as the entire system can come to a standstill due to shortage of raw material.
- **iii) Production/Operation:** It assesses the availability of various machineries, equipment, tools and techniques that would be required for production/operation.

iv) **Finance:** It assesses the total requirements of finance in terms start-up expenses, fixed expenses and running expenses. It also indicates the sources of finance that can be approached for funding.

v) **Human Resource:** It assesses the kind of human resources required and its demand and supply in the market. This further helps in estimating the cost and level of competition in hiring and retaining the human resources.

As stated above, the objective of environmental scanning should be to gather information from as many sources as possible and to maximize this information for enhanced probability of success in the business.

1.6.2.2 Environmental Factors Affecting Entrepreneurship

A complex and varying combination of financial, institutional, cultural and personality factors determines the nature and degree of entrepreneurial activity at any time. The personal backgrounds of the entrepreneurs are determined mainly by the environment in which they are born and brought up and work. A multitude of environmental factors determine the entrepreneurial spirit among people. The entrepreneurs in turn create impact on the environment. The interaction between the entrepreneur and his environment is an ongoing process. At any given point of time, the entrepreneurs derive meanings from the environment prevailing at that time and try to adapt and/or change the environment to suit their needs.

Some of the environmental factors which hinder entrepreneurial growth are given below:

- Sudden changes in Government policy.
- Sudden political upsurge.
- Outbreak of war or regional conflicts.
- Political instability or hostile Government attitude towards industry.
- Excessive red-tapism and corruption among Government agencies.
- Ideological and social conflicts.
- Unreliable supply of power, materials, finance, labor and other inputs.
- Rise in the cost of inputs.
- Unfavorable market fluctuations.
- Non-cooperative attitude of banks and financial institutions.

Entrepreneurship is environmentally determined. The most important essential for entrepreneurial growth is the presence of a favorable business environment. A healthy business environment requires active social and cultural behavior of the people, efficient economic conditions, helpful motivating Government policies, etc. When environment mitigates entrepreneurship it must be modified.

1.7 Creativity, Innovation and Entrepreneurship

Creativity, innovation and entrepreneurship, have been recognized as important contributors to a nation's economic growth. These three terminologies are chronologically interrelated and it is very important to look in to them to get their full picture.

1.7.1 Creativity

Creativity is defined as the tendency to generate or recognize ideas, alternatives, or possibilities that may be useful in solving problems, communicating with others, and entertaining ourselves and others.

Creativity is the ability to come up with new idea and to identify new and different ways of looking at a problem and opportunities.

It is a process of assembling ideas by recombining elements already known but wrongly assumed to be unrelated to each other. This definition has several key elements that are worth considering:

- Process: creativity is a process (implying among other things, that it is more like a skill than an attitude, and that you can get better at it with practice)
- Ideas: creativity results in ideas that have potential value.
- Recombining: the creative process is one of putting things together in unexpected ways.

In order to be creative, you need to be able to view things in new ways of from a different perspective. Among other things, you need to be able to generate new possibilities or new alternatives. Tests of creativity measure not only the number of alternatives that people can generate but the uniqueness of those alternatives. The ability to generate alternatives or to see things uniquely does not occur by change; it is linked to other, more fundamental qualities of thinking, such as flexibility, tolerance of ambiguity or unpredictability, and the enjoyment of things heretofore unknown.

Thus, creativity is the development of ideas about products, practices, services, or procedures that are novel and potentially useful to the organization.

1.7.1.1 Steps in the Creative Process

Step1: Opportunity or problem Recognition: A person discovers that a new opportunity exists or a problem needs resolution.

Step2: Immersion: the individual concentrates on the problem and becomes immersed in it. He or she will recall and collect information that seems relevant, dreaming up alternatives without refining or evaluating them.

Step 3: Incubation: the person keeps the assembled information in mind for a while. He or she does not appear to be working on the problem actively; however, the subconscious mind is still engaged. While the information is simmering it is being arranged into meaningful new patterns.

Step 4: Insight: the problem-conquering solution flashes into the person's mind at an unexpected time, such as on the verge of sleep, during a shower, or while running. Insight is also called the Aha! Experience.

Step 5: Verification and Application: the individual sets out to prove that the creative solution has merit. Verification procedures include gathering supporting evidence, using logical persuasion, and experimenting with new ideas.

1.7.1.2 Barriers to Creativity

Be aware that there are numerous barriers to creativity, including:

1. searching for the one 'right' answer
2. focusing on being logical
3. blindly following the rules
4. constantly being practical
5. viewing play as frivolous
6. becoming overly specialized
7. avoiding ambiguity
8. fearing looking foolish
9. fearing mistakes and failure
10. believing that 'I'm not creative

1.7. 2 Innovation

Innovation lies at the heart of the entrepreneurial process and is a means to the exploitation of opportunity. It is the implementation of new idea at the individual, group or organizational level.

Innovation is a process of intentional change made to rate value by meeting opportunity and seeking advantage.

There are four distinct types of innovation, these are as follows:

- Invention - described as the creation of a new product, service or process
- Extension - the expansion of a product, service or process
- Duplication - defined as replication of an already existing product, service or process
- Synthesis - the combination of existing concepts and factors into a new formulation

1.7.2.1 The Innovation Process

1. **Analytical planning:** carefully identifying the product or service features, design as well as the resources that will be needed.
2. **Resources organization:** obtaining the required resources, materials, technology, human or capital resources
3. **Implementation:** applying the resources in order to accomplish the plans
4. **Commercial application:** the provision of values to customers, reward employees and satisfy the stakeholders.

1.7.2.2 Areas of Innovation

The following are some of the major areas in which valuable innovation might be made.

A. New product: A new product can be developed through new or existing technology. The new product may offer a radically new way of doing something or it may simply be an improvement on an existing item. The new product must offer the customer an advantage if it is to be successful.

B. New Services: A service is an act which is offered to undertake a particular task or solve a particular problem.

C. **New Production Techniques:** Innovation can be made in the way in which a product is to be manufactured. A new production technique should allow the end user to obtain the product at a lower cost, or a product of higher quality or better service in the supply of the product.

D. New Way of Delivering the Product or Service to the Customer: Customer can only use product/service they can access. A common innovation is to take a more direct routine by cutting out distributors or middlemen.

E. New Operating Practices: As with innovations in the production of physical products, innovation in service delivery must address customers need and offer them improved benefits, for example easier access to the service, a higher quality service, a more consistent service, a faster or less time consuming service etc.

F. New Means of Informing the Customer about the Product: People will only use a product or service if they know about it. Demand will not exist if the offering is not properly promoted to them. Promotion consists of two parts; a message what is said and a means – the route by which that message is delivered.

G. New Means of Managing Relationship within the Organization: Any organization has a wide variety of communication channels running through it. The performance of the organization will depend to a great extent on the effectiveness of its internal communication channels. These communication channels are guided by the organization's structure.

H. New Ways of Managing Relationships between Organizations: Organizations sit in a complex web of relationships to each other. The way they communicate and relate to each other is very important.

1.7.3 From Creativity to Entrepreneurship

Creativity is the ability to develop new ideas and to discover new ways of looking at problems and opportunities. **Innovation** is the ability to apply creative solution to those problems and opportunities in order to enhance people's lives or to enrich society.

Entrepreneurship = **creativity** + **innovation**.

Fig 1.2: Flow of Creativity, Innovation and Entrepreneurship

1.8 Summary

In this chapter a brief discussion is made on the term entrepreneurship and entrepreneur. The different roles and tasks of the entrepreneurs are also part of the discussion. The word entrepreneurship is defined as a process that involves creation of something different and better with values to target customers. Here the entrepreneur is someone who will undertake the activities of creating something different and commercialize it in a given business environment. The three forms of entrepreneurship are also distinguished as individual entrepreneurship, intrapreneurship and organizational entrepreneurship. A person to become an entrepreneur needs to possess entrepreneurial mindset through having qualities of successful entrepreneurs and entrepreneurial skills, and he/she also to understand and scan entrepreneurial environment. Now when the entrepreneur carries out the entrepreneurial process he/she will be able and expected to create wealth for him/herself and for others as well. For this the entrepreneurial should have general management and people management skills. Finally, the entrepreneur should play active role in the economic development through improving in per capita income, generating of employment opportunities, inspiring others towards entrepreneurship, balancing regional development, enhancing the number of enterprise, providing diversity in firms, assuring economic independence, combining of economic factors, providing market efficiency, by accepting risk and maximizing investors return.

1.9 Review Questions

1. Give at least two definitions for entrepreneurship and two for entrepreneur.

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2. Who are the potential candidates for entrepreneurship?

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3. Identify any five qualities of a successful entrepreneur

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4. Some people argue that “the only beneficiary of the entrepreneurial wealth is the entrepreneur him/herself” Do you agree? Why or why not?

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5. How do you define creativity, innovation? Relate it with entrepreneurship.

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6. Discus any four possible areas for innovation

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7. How do you relate entrepreneurship and environment?

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CHAPTER 2: BUSINESS PLANNING

2.1 INTRODUCTION

In the previous chapter, we dealt with the concept of Entrepreneurship. This unit will help you to understand the concept of opportunity identification and evaluation, business idea development and how to prepare a business plan. Virtually to start any type of business or expand the existing one needs to work on opportunity identification and evaluation, business idea development and then prepare business plan. Lack of proper opportunity identification and evaluation, idea development process and business planning are the most often cited reasons for business failure. The various sections and sub-sections of this chapter will also summarize opportunity identifying and evaluating processes, business idea development process, and the feasibility study, importance and preparation of a business plan.

Chapter Objectives

After completing this chapter, students will be able to:

- Identify opportunity in the environment,
- Evaluate the opportunities in the environment,
- Generate business idea,
- Explain the concept of business planning,
- Identify components of business plan,
- Develop business plan,

2.2 Opportunity Identification and Evaluation

Most authors agree that the initial stage in the entrepreneurial process is the identification and refinement of a viable economic opportunity that exists in the market. Without the recognition of an opportunity the entrepreneurial process is likely to result in failure.

Opportunity recognition corresponds to the principal activities that take place before a business is formed or structured. The opportunity identification and evaluation stage can be divided into five main steps namely; getting the idea/scanning the environment, identifying the opportunity, developing the opportunity, evaluating the opportunity and evaluating the team.

1) Scanning the Environment/ Getting the Idea

While scanning the environment it may be provide you with idea and business opportunities. Idea is a thought or suggestion about a possible course of action. Synonymous with "idea" are the terms thought, intention, scheme, suggestion, proposal, initiative, spur, impulse, brainwave, insight, concept and connotation. Whereas, opportunity is a favorable time or set of circumstances for doing something. Synonymous with opportunity are chance, opening and prospect. A business opportunity is a gap left in a market by those who currently serve it, giving a chance to others to add unrealized value by performing differently from and better than competitors in order to create new possibilities.

Business opportunities are distinguished from ideas; an idea is not synonymous with opportunity. The difference between an idea and an opportunity is that an opportunity is the possibility of occupying the market with a specific innovative product that will satisfy a real need and for which customers are willing to pay but idea is all about opinion about anything we can have. Successful venturing may well rest upon the ability of an individual to recognize or distinguish an opportunity from an idea.

2) Opportunity Identification

Opportunity identification is ability to see, to discover and exploit opportunities that others miss. It is the process of seeking out better ways of competing. It includes scanning the informational environment, being able to capture, recognize and make effective use of abstract, implicit and changing information from the changing external environments.

It is important for the entrepreneur to understand the cause of the opportunity. Is it technological change, market shift, government regulation, or competition? These factors and the resulting opportunity have a different market size and time dimension. The market size and the length of the window of opportunity form the primary basis for determining risks and rewards which serves for opportunity evaluation.

Opportunity identification is a very difficult task, as most opportunities do not just appear but rather result from an entrepreneur's alertness to possibilities. In developing countries, problems may be changed to business opportunities.

3) Opportunity Development

Having recognized the opportunity, timely adaptation of that opportunity to suit actual market need is key to new venture success. Opportunity development is the process of combining resources to pursue a market opportunity identified. This involves systematic research to refine the idea to the most promising high potential opportunity that can be transformed into marketable items.

4) Opportunity Evaluation

Opportunity screening and evaluation is a critical element of the entrepreneurial process. A professional executed evaluation can tell whether the specific product or service has the returns needed to justify the investment and the risk to be taken.

Opportunity screening and evaluation is perhaps the most critical element of the entrepreneurial process, as it allows the entrepreneur to assess whether the specific product or service has the returns needed for the resources required. This evaluation process involves looking at the creation and length of the opportunity, its real and perceived value, its risks and returns, its fit with the personal skills and goals of the entrepreneur, and its differential advantage in its competitive environment. According to experts, evaluating the opportunity must answer the questions listed in table 2.1 below:

Table 2.1: Business factors and questions for opportunity evaluation

Business factor	Questions for evaluation
Product or Service	Description of the product or service, its differentiator, purpose and the need it fills o What competitive advantage / benefits does the product have? o What is the required customer care support for this product/service? o Is the company able to produce product and supply required aftercare support?
Market Opportunity	o Where is the market demand? What is the target market? Is it generic or a niche? o Industry characteristics (growth rates, change, entry barriers). o What market share can the product reasonably expect today? In 2, 5 or 10 years? o Timing and length of the window of opportunity? o What competition exists in this market? Substitutes? How big is their turnover? o How accessible are the desired distribution channels?
Costing and Pricing	o How much will it cost to develop the product and commercialize it? o Where will the funds come from? o How do the pricing, costs and economies of scale compare with competitors? o How easy is it to acquire equipment, skills and other inputs required?
Profitability	o Where is the money to be made in this activity? What are the gross margins? o Would the return on investment be acceptable? What is the payback period? o What are the cash flow patterns and the source of working capital?
Capital Requirements	o How much capital (people, operating expense and assets) is required to start? o What are the long-term capital needs? o How much of the required capital is secured and where will the rest come from? o What securities are available to guarantee the required funds?

Business factor	Questions for evaluation
	o Is there a list of potential funders? In case the funders withdraw their capital?
Issues and risks	o What risks (real and perceived) are inherent with the product/service? o Industry based risks e.g. is the market on a decline? o Are there plans for surviving the death of the lead entrepreneur? o Unreliable forecasts? Inadequate cash flow? o Inability to grow with the demand or cope with shrinking sales? o Supplier and value chain management?

5) Assessment of the Entrepreneurial Team

Regardless of how right the opportunity may seem to be, it will not make a successful business unless it is developed by a team with strong skills. Gartner et al (1999:230) advices that once the opportunity has been evaluated, the next step is to ask pertinent questions about the people who would run the company. Such questions are illustrated in table 2.2:

Table 2.2: Team factors and questions for opportunity evaluation

Team factor	Questions for evaluation
Focus:	o Is the founder really an entrepreneur, bent on building a company? o Does the entrepreneur (or his team) have some experience (work or industry)? o Do they really like this product/sector? Do they really want this? o Can the team create products to suit that market need? o How stressful is the opportunity for the team?
Selling:	o Does the team have the necessary selling and closing skills?
Management:	o Who will work full time? Do your managers represent competitive advantage? o Does the team have the necessary management and technical skills? o If the required skills are not available, can they be acquired at competitive rates? o How is their relationship with the entrepreneur, commitment and motivation?
Ownership:	o Have the critical decisions about ownership and equity splits been resolved? o Are the members committed to these? o Does the owners have enough financial capital for required own contributions?

2.3 Business Idea Development

Brainstorming Cases on business Idea and Business Idea Identification is given as follow:

Case 1: Janet's Experience
Janet has a small farm and her husband works in a nearby mine, but even though both of them have jobs, they do not earn enough money to pay for their children's education. Janet decides to try and start her own business by rearing chickens to sell. She knows how to do it and her uncle gives her a loan of $400 to start the business. However, before she buys the chicks, someone tells her that there is a huge demand

for sunflower oil because of its lack of availability in the market. Traders are knocking on the doors of local farmers asking them to produce it. Thinking she can earn a lot more money from pressing sunflower seeds for oil, Janet changes her business idea and starts an oil pressing venture.

Janet has never grown a large quantity of sunflowers. She spends all the money from the loan to buy seeds, fertilizer and the oil pressing equipment. Since she uses most of the family farmland to grow sunflowers, there is less land to grow maize and vegetables for the family to eat. The chemicals from the fertilizer begin to make her children sick. She now has to buy more food for the family. It takes a lot of time and effort to process the oil, so, Janet has to employ someone to help her. A lot of other farmers have started growing sunflower seeds too. Therefore, by the time her oil is ready to sell, the market is already saturated with the good and Janet cannot find a buyer. To reduce her losses, Janet has to sell the oil at a very low price to a local shop. As a result, Janet makes very little money and she is not able to pay back the loan.

Reflection question: What is wrong with Janet's business idea? Why?

Case 2: Lily's Experience

Lily had been working in the assembly line of a garment factory for more than five years. Her salary was low and she was often required to work overtime. Lily's sister-in-law came to visit her and complained to Lily that she was unable to find any good clothes for her 12 year-old daughter. She said that the clothes in the stores all seem to be either made for younger children or for adults. After the visit, Lily decided to go around to the clothing shops in her town. She saw young teenage girls shopping in the stores, but she noticed that the number and variety of clothes geared to that age group was limited. She had already been thinking of quitting her job and opening her own business. Therefore, Lily decides to design some pretty clothes and dresses for young teenage girls. She makes some drawings of clothing that would appeal to that age group. She then takes her drawings to the local clothing shops, asking the owners if they would buy the dresses in the drawings, how much they would pay for them and how many they would buy. The shop owners seemed to be quite happy with her designs and said they would display her clothes. Lily then uses her savings to buy a sewing machine and some material to make her first batch. She works in the evening after getting off from work at the garment factory. All of the dresses she makes sell very well and the shops are willing to pay her in cash upon delivery. Lily then decides to quit her job to focus on her own business. Within six months, Lily starts receiving regular orders from the shops. She plans to buy one more sewing machine and hire one of her friends to work for her.

Reflection question: Why is Lily successful in her own business? What did she do that made her successful?

A **business idea** is a short and precise description of the basic operation of an intended business.

There are three types of business ideas. They are:

1. **Old Idea –** Here an individual copies an existing business idea from someone.
2. **Old Idea with Modification –** In this case the person accepts an old idea from someone and then modifies it in some way to fit a potential customer's demand.
3. **A New Idea –** This one involves the invention of something new for the first time

2.4 Business Idea Identification

Before you start a business, you need to have a clear idea of the sort of business you want to run. Your business idea will tell you:

- Which need will your business fulfill for the customers and what kind of customers will you attract?
- What good or service will your business sell?
- Who will your business sell to?
- How is your business going to sell its goods or services?
- How much will your business depend upon and impact the environment? A good business idea will be compatible with the sustainable use of natural resources and will respect the social and natural environment on which it depends.

All business ideas are not equally worth. Therefore, to identify promising business idea among others, it is important to answer the above raised questions. Let we see the explanation for the questions raised above.

2.4.1 The Need will Your Business Fulfill for the Customers

Your business idea should always have customers and their needs in mind.

It might be a good idea to start a day care center in the commercial area as many other parents may have the same need.

It might be a good idea to start a waste collection and recycling service in this area. Not only would the owner of this restaurant need the service, but many other residents in the area might need it as well.

Refer to the Cases of Janet and Lily Narrated in this Chapter:

Janet produced sunflower oil without knowing: ▪ Is there a need for oil? ▪ Who needs it? ▪ Why do they need sunflower oil and not another type of cooking oil? She, therefore, had no idea how big the demand for sunflower oil would be. Consequently, she could not find customers as the need had been fulfilled by the time she was able to supply her good.	Since **Lily** did her market research, she knows that pre-teens and teenage girls in her area have limited choice and access to clothing specifically designed for their age group. What they wear is either designed for younger children or for adults. Lily aims to fill the need by producing fashionable clothes that are suitable for their age group.

2.4.2 Good or Service will your Business Sell

Depending on your skills and the needs of the customers, you should decide which good or service your business will sell. Also, keep in mind that they must be goods or services that people are willing to pay for and at a price that will allow you to make a profit.

A good is an item that people pay for and use. It may be something you make yourself or it may be something you buy to resell. Tools, baked goods, clothes and retail items are all products. A service is something you do for people that they then pay you for. For example, delivering goods, banking, babysitting, repairing items, collecting recyclable waste from apartment buildings, operating tours, etc. are all services.

Refer to the Cases of Janet and Lily Narrated in this Chapter:

Janet grew sunflowers and produced sunflower oil without having any prior knowledge and experience. She was not aware of the challenges of the business, such as the toxics from fertilizers or the long processing time. Janet had no advantage that she could use in her sunflower business and she faced too many problems, so she was unable to make a profit.	**Lily** had significant experience in making clothes. She knew about sewing. However, she had no experience designing clothes, so she tested her competency by making some designs and showing them to the clothing store owners. She only opened her business after the first batch of dresses were accepted for display in the shops and then sold.

2.4.3 Identifies Potential Customer

Any business cannot succeed without customers. Therefore, it is essential that you know who your customers will be. Will you sell to a specific type of customer or to everyone in an area? There must be enough people who are able and willing to pay for your goods and services or the business will not survive.

Refer to the Cases of Janet and Lily Narrated in this Chapter:

Janet had no idea who the end customers of her sunflower oil might be. She just focused on producing the oil and thought that the shops will buy it from her. Therefore, she did not know how big the need was for her good. She also did not know if there were any competitors who were going to fulfill the same needs of the customers.	**Lily** knew that her customers will be teenage girls in her area. She researched the market by observing the clothes shops and the target customers to make sure that there was a real need that she could fulfill. She also knew that there was no competitor currently filling that need.

2.4.4 Strategy for **S**elling **G**oods or **S**ervices/ **H**ow is **Y**our **B**usiness **G**oing to **Sel**l **Good or Services?**

How are you going to sell your goods or services? If you plan to open a shop, you know how you will sell your product, but manufacturers or service operators can sell their products in many different ways. A manufacturer, for example, can sell either directly to customers, to retailers or to wholesalers.

Refer to the Cases of Janet and Lily Narrated in this Chapter:

Janet did not plan how to sell her product. When she made the oil, she just went around and tried to sell to retail shops.	From the beginning, **Lily** decided to sell her goods through clothes shops. She talked to the owners of these shops even before she started her business, to make sure they would sell her goods.

2.4.5 Relation between Business and Environment

Your business can only be sustainable in the long run if it works in harmony with the social and natural environment. How much does your business depend on the environment? Does it rely on the weather, soil or other natural resources? Does it need any specific type of labor from the local community? Does it need the local community to support it? What should you do to make sure that your business nurtures the natural environment and helps the local community? Will your business nurture the natural environment or will it have a detrimental impact? How would you minimize or reverse any negative effect that your business might have? This is discussed in detail in Chapter one of this module.

Activity 1: Now if you already have a business idea, describe your idea using the following form:

My business idea is: ....
Which need will my business fulfill? ....
What good/ service will I provide? ....
To whom will I sell? ....
How will I sell my good/ service? ....
How much will my business depend upon and impact the environment? ....

2.5 Methods for Generating Business Ideas

Brainstorming Cases on business idea generation is given as follow:

Case 3: Hamisi Experience

Hamisi worked for a gas stove importer for five years before he decided to open his own business. His aunt owns a successful hardware supply and rental shop, so she offered to be his financial partner and provide funds for his start-up. She does not want to be involved in the operation, but only to share the profit, while letting Hamisi run the business himself. Hamisi starts thinking about possible business ideas. He enjoys making sesame bags and wall hangings, which many of his friends admire. Therefore, at first he thinks about making and selling them to tourists as souvenirs. However, after talking to a number of

local shopkeepers, he learns that there are too few tourists in his area for such a business to be profitable.
Hamisi thinks about opening a gas stove shop, as he knows how to source imported gas stoves and he is familiar with the functions and quality of each brand. He does some market research and learns that there are quite a few gas stove shops in his area and their sales are low. They are offering various discount and promotional schemes, but none of their promotions have increased sales significantly. He decides that he better not enter such a tough market.

While still thinking about a business idea, Hamisi helps his aunt move to a new house. Although it is easy to find a van to rent, no one offers moving services, such as packaging, loading and unloading. Hamisi has to ask some of his friends to help him package and carry his aunt's furniture and belongings.

They spend a whole weekend looking for packaging and then disassembling the big items, wrapping and packing them, loading them in the van, unloading them at the new house and then unpacking and reassembling them. Hamisi wonders why there is not a moving company in the area. Realizing that this might be a business idea, Hamisi does some research on that field of business and then describes his business idea as follows :

My business idea: Home/ office packaging and moving service

• **Which need will my business fulfill?** Everyone I talk to agree that moving from house to house, or office to office is very difficult and time-consuming. There is no company in the area that provides packaging and moving services. Therefore, if I provide these needed services, my business will have a steady demand.

• **What good/service will I provide?** I intend to offer complete packaging and moving services for homes and offices. Although I have no experience running this type of business, I have some experience handling, storing and transporting goods. I learned these things while working with the gas stove importing company. I can ask my brother who is very good at process management to plan the operation. In addition, I can use a reliable transportation provider who often works for my aunt's shop.

• **To whom will I sell?** I intend to start by offering my services to all my relatives, friends, friends of friends and my aunt's customer base. I will then expand my business and advertise around the whole town.

• **How will I sell my service?** I can sell my service directly to the customers. Initially, I will introduce the service to all of my friends, relatives and my aunt's customer base. After I have done some moving for family and friends, I will expand my market and hang posters around areas where there are a lot of shops, offices, apartments and houses for rent.

• **How much will my business depend upon and impact the environment?**

My business will reuse the cartons and packaging several times so as to prevent waste.

Instruction: Read the Hamisi's Experience for the students.

Reflection question: What did Hamisi do to find his business idea?

Hamisi does not just focus on one idea:

- He looks around to find different business ideas that may be suitable to his areas of interest and will benefit from his knowledge and his working experience.
- He describes each of the different ideas clearly.
- While researching the different ideas, he found that some would not work because there is not sufficient need, there are not enough customers or the competition is fierce.
- While describing the idea, he also identified resources that he could leverage, such as his friend's knowledge, his aunt's customer base or a reliable transportation provider that he knows.

Every business idea should be based on knowledge of the market and its needs. The market refers to people who might want to buy a good or service; i.e. the customers. The market differs from place to place, depending on who lives in the area, how they live and for what goods or services they spend their money. When you understand the market in your area, you might recognize many business ideas that you may have previously ignored.

When generating business ideas, it is best to try to keep your mind open to everything. Your first goal is to think of as many ideas as possible and make a list of all the possible business opportunities. With a list, you will have more choices! You then can scan the list and nail down the idea(s) that sound most feasible to you and that you think will be most profitable.

There are many ways to come up with business ideas, such as surveying local businesses or asking existing business owners. The information gained from one approach may supplement another and help you to clearly describe your business ideas. Below, we will examine a few different approaches to generating business ideas.

1. Learn from successful business owners

You can learn a lot from people in your area who have already gone through the process of establishing a business. You should try to get the following information from them:

- What kind of idea did these businesses start with?
- Where did the ideas come from?
- How did they develop their ideas into successful businesses?
- How does the business profit and fit into the local environment?
- Where did they get the money to start their business?

When to meet successful business owners, use the Business Ideas Analysis Form shown below, to write down their answers to the above listed questions.

BUSINESS IDEAS ANALYSIS FORM

Name of business: ____

Goods or services to be sold: ____

Main customers: ____

When and why did the owner decide to start this business?

____

____

Why did the owner think it was a good idea to start that kind of business?

____

____

How did the owner learn what his potential customers wanted?

____

____

What strengths or assets did the owner use to start this business? (E.g., previous experience, training, family background, contacts, hobbies)

____

____

What problems did the owner face in setting up the business?

____

____

Has the business good or service changed over time?

____

____

What is the impact of the business on the natural environment and the community?

____

____

Notes:

____

____

2. Draw From Experience

2.1 Your own Experience

Look at the list of your interests, your experiences and your networks. Are there any possible business ideas that you can derive from your own past experience? Think about each type of experience.

Start with yourself. What has your experience been as a customer in the market place? Have you ever searched all day for some items that you could not find in any store in your area? Think about the goods and services you have wanted at different times and that you have had difficulty finding.

2.2 Other People's Experience

The people around you are potential customers. It is important to understand their experience trying to find goods and services that are unavailable or not exactly what they need. Listen carefully to what these people say about their shopping experience.

Ask your family and friends about the things they would like to find that are not locally available. Expand your social knowledge by talking to people from different age groups, social classes, etc. You can also visit community groups, colleges, etc. for a greater understanding of the market.

Here are some examples of comments that would help with your search for a business idea:

- "I cannot find a lunch box that keeps the food warm."
- "The choice of cooking pots in the shops is very limited."
- "There is no reliable way of sending gift packages to my friends and relatives living in the villages."
- "There is not enough entertainment in this town and the weekends are so boring."
- "I really need to buy some marketing textbooks, but there are no good bookstores in this town."
- "There is so much garbage on the streets. Somebody should do something about it."

3. Survey Your Local Business Area

Another way of discovering business ideas is to look around your local community. Find out what type of businesses are already operating in your area and see if you can identify any gaps in the market.

If you live in a village or small town, you may be able to identify all the fields of business in the whole town. Otherwise, you may need to focus on the preferred business fields and business types that you identified. This is an activity that will be much easier to do with a business partner or friend. Visit the closest industrial area, markets and shopping centers in your area.

4. Scanning Your Environment

You can use your creativity to find more business ideas in your area. Look at the list of existing local businesses. If the list has included most of the local markets, you may be able to learn about the industries or service providers on which the local economy relies.

It may be useful to think about business ideas by considering all the resources and institutions in your area. For example think about:

- Natural resources,
- Characteristics and skills of people in the local community,
- Import substitution,
- Waste products,
- Publications,
- Trade fairs and exhibitions ,

4.1 Natural Resources

Think of what is abundantly available in your area that could be made into useful products without harming the environment. Natural resources include materials from soil, agriculture, forest, mineral, water, etc.

Perhaps there is good clay soil in the area that can be used for making bricks. It may be used for other business ventures such as making plates, cups or tiles.

Think about a way to use this resource that would enable you to continue working with it for many years. In other words, make sure that your business idea will not exhaust the natural resource that would be the foundation of your business.

4.2 Characteristics and Skills of People in the Local Community

Consider whether the people in your area have some special characteristics or skills that could be useful for a business:

- Are there people in your community who are good artisans, tailors or carpenters or who have specific skills creating items unique to your area?
- Are there recent graduates looking for jobs who you could employ?
- Are there caregivers, nurses or people who could offer services to children, the elderly or the sick?
- Is your community digitally connected?
- Is the infrastructure in your community well developed?

4.3 Waste Products

Business opportunities can also be generated by using materials that have been previously used by both homeowners and businesses. Think about the possible use of waste materials for the production of other useful and marketable items. Recyclable waste products can be identified by analyzing certain items to see how they are discarded. Man-made waste has a detrimental effect on the environment. In most cases, companies are keen to work with entrepreneurs who can turn their waste products into valuable and marketable items.

Usually there is something that can be reused in things that we throw away. Recycling may be done with waste products that come from agricultural processing, household garbage, used machinery and appliances or industrial waste. People throw away food that could be used to make compost or animal feed. They also throw away paper, glass and aluminum that can be recycled. Think of things that can be made from what others thought was garbage.

Many industries dispose of useful materials. A clothing company might throw out small pieces of cloth that could be used to make something else. Plastics factories usually have materials left over that might be useful for insulation, stuffing for pillows or a new kind of fuel.

Is there a possibility that you could recycle something that is found in abundance in your neighborhood? Is there a way of using resources more efficiently? May be you could offer a service to help individuals or institutions dispose of their waste in a way that is environmentally-friendly or maybe you can make something new out of the waste.

4.4 Import Substitution

Can you think of anything that is imported that might be made locally? Some imported goods have high import duties, making them very expensive. You could investigate the possibility of operating a business that can easily make the imported goods locally.

4.5 Publications

Publications from the internet and other printed material may help you find ideas. There are many sites on the internet that you can visit to find out about business ideas as well as franchise businesses for sale. There are also web-based businesses that you can search from home if you have internet connection.

Newspapers are a great source of ideas. They often describe types of businesses that you could start or products that you could provide in your area. The classified advertisements may give your ideas, as well as articles about business trends in other places.

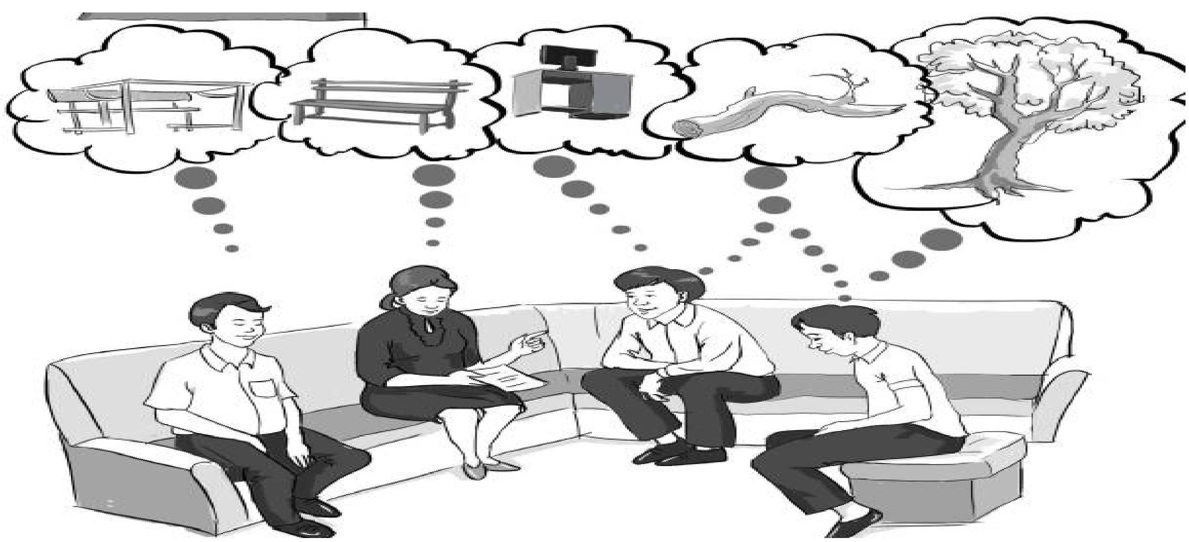
4.6 Trade Fairs and Exhibitions

Organizations hold trade fairs for different goods or services. Attending these fairs may give you exposure to a number of new business ideas that you had not previously considered. Be sure to attend any trade fair for fields of business in which you may be interested.

5. Brainstorming

Brainstorming means opening up your mind and thinking about many different ideas. You start with a word or a topic and then write down everything that comes to mind relating to that subject. You continue writing for as long as possible, putting down things that you think of, even if they seem irrelevant or odd. Good ideas can come from concepts that initially seem strange.

Brainstorming works best in a group. Get your family, friends or classmate together and ask them to help by writing down ideas they have when they hear the word or subject matter.



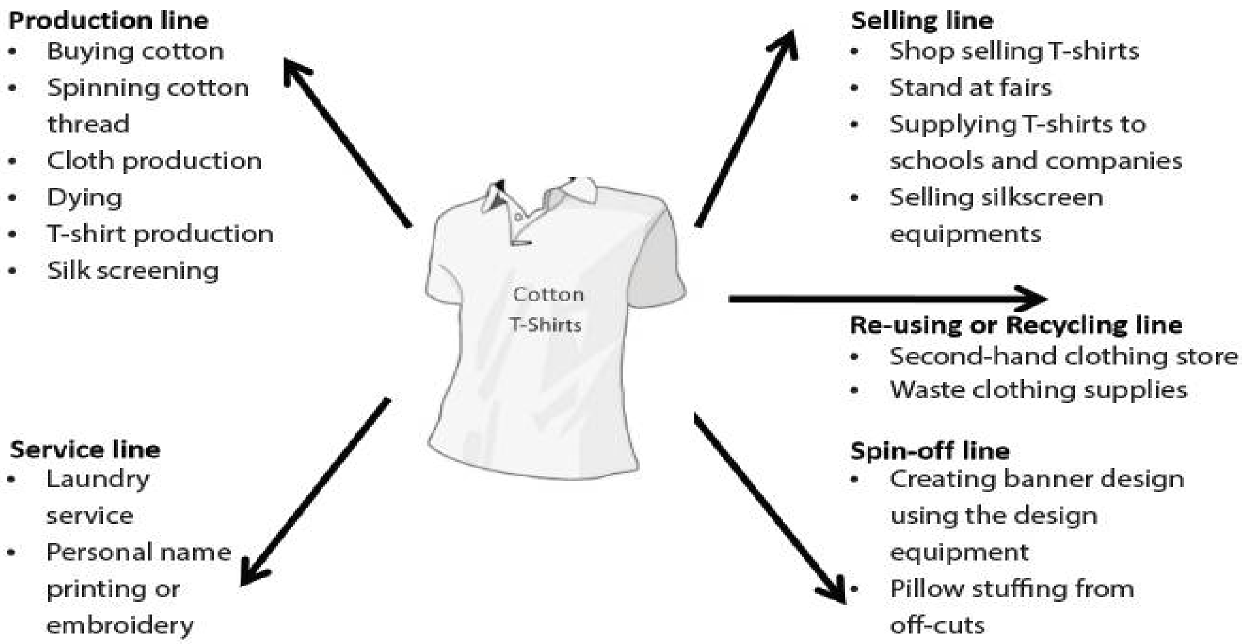
6. Structured Brainstorming

Structured brainstorming is when you think of the different processes that are involved in the operation of a particular business and the goods/services that can be offered with respect to those processes. This is different from thinking about random items related to a particular business field and type.

Try to think of all the businesses that are related to different aspects of a product:

- Those involved in production,
- Those involved in the selling process,
- Those involved in recycling or re-using materials,
- Those indirectly related (spin-offs),
- Those involved in servicing,

For example, you can think of different processes within each line. You continue until you have run out of ideas. Again, whatever comes to mind should be written down. Decide later if it is worthwhile or correct. Let's take the example of cotton T-shirts:



As far as all brainstorming exercises are concerned, it is essential to recall the basic rules of brainstorming: no criticizing or censoring of ideas, wild and turbulent sessions allowing the uninterrupted flow of ideas, no interruption once the basic idea of the exercise has been introduced, no shyness and no limitations.

7. Focus Group

Focus group is a group of individuals providing information on a structured format which is led by moderators. It is characterized by an open and in depth discussion: rather than simply asking questions to solicit student response. The moderator focuses the discussion in either Directive or non-directive manner. It is useful for both getting new idea on existing product or screening idea/concepts.

8. Problem Inventory Analysis

It is similar to focus group to generate new product ideas. The difference is rather than generating new idea themselves, consumers are provided with a list of problems in general product category. It is a method of obtaining "New Idea" and solutions by focusing on problems.

9. Free Association

One of the simplest methods that entrepreneurs can use to generate new ideas is free association. This technique is particularly helpful in developing an entirely new slant to a problem. First, a word or phrase related to the problem is written down, then another and another, with each new word attempting to add something new to the ongoing thought processes, thereby creating a chain of ideas ending with a new product/service idea emerging.

10. Forced Relationships

Forced relationships- as the name implies- is the process of forcing relationships among some product combinations. It is a technique that asks questions about objects or ideas in an effort to develop a new idea.

11. Attribute Listing

Attribute listing is an idea-finding technique that has the entrepreneur list the attributes of an item or problem and then look at each from a variety of viewpoints. Through this process, originally unrelated objects can be brought together to form a new combination and possibly a new product/service that better satisfies a need.

2.6 Business Idea Screening

Idea screening is the process to spot good ideas and eliminate poor one. To screen the business idea generated, three approaches are discussed as follow:

1) **Macro screening**: is aimed screening down ideas to 10. And the common criteria are:
    - Are my own competencies (see strength detector) sufficient?
    - Can I finance it to a large extent with my own equity?
    - Will people buy my product/service (i.e. is it needed and can people afford it)?
2) **Micro Screening**: is aimed screening down ideas into 3. The common criteria used for screening are:

- Solvent demand
- Availability of raw materials
- Availability of personal skills
- Availability of financial resources

3) Scoring the Suitability of Business Idea:

This approach is most appropriate when deciding on starting a business. When there are more than one possible business ideas and one needs to decide which one to follow, we use score business ideas (e.g., BI1, BI2, BI3) by assigning a rating from 1 to 3 for each question, with 3 being the strongest. After we score the ideas we sum the total and select the idea with the highest score.

S. No	**Questions**	**BI1**	**BI2**	**BI3**
1.	Are you familiar with the operations of this type of business?			
2.	Does the business meet your investment goals?			
3.	Does the business meet your income goals?			
4.	Does the business generate sufficient profits?			
5.	Do you feel comfortable with the business?			
6.	Does your family feel comfortable with the business?			
7.	Does the business satisfy your sense of status?			
8.	Is the business compatible with your people skills?			
9.	Is there good growth projected for the overall industry of the business?			
10.	Is the risk factor acceptable?			
11.	Does the business require long hours?			
12.	Is the business location-sensitive?			
13.	Does the business fit your personal goals and objectives?			
14.	Does this business fit your professional skills?			
Totals				

Notes: while to answer the above listed questions it is important to conduct survey. Collecting information on your business idea gives you an opportunity to promote your business idea and to present yourself as a potential entrepreneur. While to answer the above questions, there are four important groups that you should talk to:

- **Potential customers**: Their views are essential to your understanding of whether or not your proposed product is important to them and if you need to modify your idea to meet their needs.
- **Competitors, suppliers and entities with financial resources**: Their views will reveal the challenges of competition that you would face, as well as other issues related to your potential business.
- **Financial institutions**: Find out the lending requirements to determine whether borrowing for a new business is possible.
- **Key informants and opinion leaders**: These are people who would know a lot about the type and field of business you want to go into and/or a lot about your potential customers. Their views would give you a lot to think about and could also give you a better insight into the feasibility of your business idea.

When you have completed the summary of your business idea, you can go on to the next step to start your own business: Prepare a business plan for the proposed business.

2.7 Concept of Business Plan

Planning is the first and the most crucial step for starting a business. A carefully charted and meticulously designed business plan can convert a simple idea/innovation into a successful business venture.

A business plan is a road map for starting and running a business. A well-crafted business plan identifies opportunities, scans the external and internal environment to assess the feasibility of business and allocates resources in the best possible way, which finally leads to the success of the plan. It provides information to all concerned people like the venture capitalist and other financial institutions, the investors, the employees. It provides information about the various functional requirements (marketing, finance, operations and human resources) for running a business.

A business plan is the blueprint of the step-by-step procedure that would be followed to convert a business idea into a successful business venture. A business plan first of all identifies an innovative idea, researches the external environment to list the opportunities and threats, identifies internal strengths and weakness, assesses the feasibility of the idea and then allocates resources (production/operation, finance, human resources) in the best possible manner to make the plan successful:.

The objectives of a business plan are to:

- ☞ Give directions to the vision formulated by entrepreneur.
- ☞ Objectively evaluate the prospects of business.
- ☞ Monitor the progress after implementing the plan.
- ☞ Persuade others to join the business.
- ☞ Seek loans from financial institutions.
- ☞ Visualize the concept in terms of market availability, organizational, operational and financial feasibility.
- ☞ Guide the entrepreneur in the actual implementation of the plan.
- ☞ Identify the strengths and weakness of the plan.
- ☞ Identify challenges in terms of opportunities and threats
- ☞ Clarify ideas and identify gaps in management information about their business, competitors and the market.
- ☞ Identify the resources that would be required to implement the plan.
- ☞ Document ownership arrangements, future prospects and projected growths of the business venture.

2.8 Developing a Business Plan

2.8.1 Business Planning Process

A plan, which looks very feasible at the first instance, might actually not be when the details are drawn. Hence documenting the business plan is one of the early steps that an entrepreneur should take. As discussed above, the successful entrepreneur lays down a step-by-step plan that she/he follows in starting a new business. This business plan acts as a guiding tool to the entrepreneur and is dynamic in nature – it needs continuous review and updating so that the plan remains viable even in changing business situations. The various steps involved in business planning process are discussed here below:

1) Preliminary Investigation

Before preparing the plan entrepreneur should:

- ☞ Review available business plans (if any).

- ☞ Draw key business assumptions on which the plans will be based (e.g. inflation, exchange rates, market growth, competitive pressures, etc.).
- ☞ Scan the external environment and internal environment to assess the strengths, weakness, opportunities and threats.
- ☞ Seek professional advice from a friend/relative or a person who is already into similar business (if any).

2) Opportunity Identification and Idea Generation

Entrepreneurship is not just limited to innovation (generation of an entirely new concept, product or service, but it also encompasses incremental value addition to the concept/product/ services offered to the consumer, shareholder and employee).

Opportunity identification and business idea generation is the first stage of business planning process. It involves generation of new concepts, ideas, products or services to satisfy demand.

3) Environmental Scanning

Once a promising idea emerges through idea generation phase the next step is environmental scanning, which is carried out to analyze the prospective strengths, weakness, opportunities and threats of the business enterprise. Hence before getting into the finer details of setting up business it is advisable to scan the environment both external and internal and collect the information about the possible opportunities, threats from the external environment and strengths and weaknesses from the internal environment (the detail has been addressed in chapter one).

4) Feasibility Analysis

Feasibility study is done to find whether the proposed project (considering the above environmental scanning) would be feasible or not. It is important to demarcate environmental scanning and feasibility study at this point. Environmental scanning is carried out to assess the external and internal environment of the geographical area/areas where, entrepreneur intends to set up his business enterprise, whereas feasibility study is carried out to assess the feasibility of the project itself in a particular environment in greater detail.

5) Report Preparation

After environmental scanning and feasibility analysis, a business plan report is prepared. It is a written document that describes step-by- step, the strategies involved in starting and running a business.

2.8.2 Essential Components of Business Plan

I) **Cover Sheet:** Cover sheet is like the cover page of the book. It mentions the name of the project, address of the headquarters (if any) and name and address of the promoters.

II) **Executive Summary:** Executive summary is the first impression about the business proposal. As the saying goes, the first impression is the last impression. A careful presentation of information should be done to attract the attention of the evaluators. It should be in brief (not more than two or three pages) yet it should have all the factual details about the project that can improve its marketability. It should briefly describe the company; mention some financial figures and some salient features of the project. Generating interest in the minds of the readers is the prime motive of the executive summary.

III) **The Business:** This will give details about the business concept. It will discuss the objective of the business, a brief history about the past performance of the company (if it is an old company), what would be the form of ownership (whether it would be a single proprietor, partnership, cooperative society or a company under company law). It would also label the address of the proposed headquarters.

IV) **Funding Requirement:** Since the investors and financial institutions are one of the key bodies examining the business plan report and it is one of the primary objectives of preparing the business plan report, a careful, well-planned funding requirement should be documented. It is also necessary to project how these requirements would be fulfilled. Debt equity ratio should be prepared, which can give an indication about how much finance would the company require and how it would like to fund the project.

V) **The Product or Services:** A brief description of product/services is given in this subsection. It includes the key features of the product, the product range that would be provided to the customers and the advantages that the product holds over and above the similar products/ substitute products available in the market. It also gives details about the patents, trademarks, copyrights, franchises, and licensing agreements.

VI) **The Plan:** Now the functional plans for marketing, finance, human resources and operations are to be drawn.

1) **Marketing Plan:** Marketing mix strategies are to be drawn, based on the market research.

2) **Operational Plan:** The operational plan would give information about (i) Plant location: why was a particular location chosen? Is it in the vicinity of the market, suppliers, labor or does it have an advantage of government subsidies for that particular location or are there any other specific reasons for choosing the particular location?, (ii) Plan for material requirements, inventory management and quality control are also drawn for identifying further costs and intricacies of the business. Finally, the budget for operational plan is also drawn.
3) **Organizational Plan**: The organizational plan indicates the pattern of flow of responsibilities and duties amongst people in the organization, it provides details about the manpower plan that would be required to put life into the business and it would also enlist the details about the laws that would be governed in managing the employees of the organization. In the end the organizational plan is also budgeted.
4) **Financial Plan:** The financial plan is usually drawn for two to five years for an existing company. For a new organization the following projections are drawn:
    a) Projected Sales
    b) Projected Income and Expenditure Statement
    c) Projected Break Even Point
    d) Projected Profit and Loss Statement
    e) Projected Balance Sheet
    f) Projected Cash Flows
    g) Projected Funds Flow
    h) Projected Ratios

VII) Critical Risks: The investors are interested in knowing the tentative risks to evaluate the viability of the business and to measure the risks involved in the business. This can further give confidence to the investors as they can calculate the risks involved in the business from their perspectives as well.

VIII) Exit Strategy: The exit strategies would provide details about how the organization would be dissolved, what would be the share of each stakeholder in case of winding-up of the organization. It further helps in measuring the risks involved in investing.

IX) Appendix: The appendix can provide information about the Curriculum Vitae of the owners, Ownership Agreement and the like.

2.9 Sample Business plan Format

The business plan outlined below presents all necessary chapters in detail, including all necessary explanations in the context of Ethiopia.

Business plan outline

for micro-enterprises - Ethiopian application

Business Plan

1. **Full name** of the business operator...................................
2. **Address:** Woreda......................... Town..................

   Kebele.......................... House no.............
3. **Type of the plan/work/business** in which the operator is to be engaged.

   ....

4. Year of the plan: From.............................. to....................

5. Work premises at the disposal of the operator.................

....

....

Specify, if there is any problem:

....

6. Yearly sales plan:

Ser. no.	Product/service to be sold, marketed / year	Unit	Qua.	Unit price	Total price	Remark
	Total sales					

Months during which sales are expected to be high

....

....

....

1. **Equipment currently owned by the operator:**

Ser. no.	Type of equipment	Unit of measure	Qua.	Unit cost	Total cost	Remark
	Total cost of equipment					

8. Equipment to be purchased by the operator

Ser. no.	Type of equipment	Unit of measure	Qua.	Unit cost	Total cost	Remark
	Total cost of equipment					

9. Yearly raw material requirement:

Ser. no.	Type of raw material	Unit	Qua.	Unit price	Total price	Remark
	Total yearly raw material cost					

Source of raw material...

....

10. Other yearly operating expenses (e.g. labor expense, sales expense, depreciation expense, tax expense etc..)

Ser. no.	Types of expense	Amount of expense in Birr	Remark
	Total expense		

11. Yearly production/service plan:

Ser. no.	Types of production/service to be produced or rendered	Unit	Qua.	Unit cost	Total cost	Remark
	Total cost					

12. Financial plan:

Capital requirements	**Equity**	**Loan**	**Total**
Investment capital:			
Machinery + equipment Furniture + fixture Business premises Any other initial and significant outlay			
Working capital:			
· Salary/wage · Raw material and/or supplies · Rent · Maintenance · Business promotion · Other cash outlay to meet short-term and recurrent expenditure			
Total			

13. Yearly profit and loss plan

Profit + Loss Statement Format: Accounting

Business plan outline 2 for micro and small enterprises and start ups **Business plan outline** **For micro and small enterprises and start ups**
Executive summary **1.** Brief Description of the Project 2. Brief Profile of the Entrepreneur 3. Project's Contributions to the Economy 1. Sales and Marketing 1.1 Product description 1.2 Competitors' 1.3 Location 1.4 Market Area 1.5 Main Customers 1.6 Total Demand 1.7 Market Share 1.8 Selling Price 1.9 Sales Forecast 1.10 Promotional Measures 1.11 Marketing Strategy 1.12 Marketing Budget 2. Production 2.1 Production Process 2.2 Fixed Capital 2.3 Life of Fixed Capital 2.4 Maintenance and Repairs 2.5 Sources of Equipment 2.6 Planned Capacity 2.7 Future Capacity 2.8 Terms and Conditions of Purchase of Equipment 2.9 Factory Location and Layout

2.10 Raw Materials Needed

2.11 Cost of Raw Materials

2.12 Raw Materials Availability

2.13 Labor

2.14 Cost of Labor

2.15 Labor Availability

2.16 Labor Productivity

2.17 Factory Overhead Expenses

2.18 Production Cost

3. Organization and Management

3.1 Form of Business

3.2 Organizational Structure

3.3 Business Experience and Qualifications of the Entrepreneur

3.4 Pre-Operating Activities

3.5 Pre-Operating Expenses

3.6 Office Equipment

3.7 Administrative Expenses

4. Financial plan

4.1 Project Cost

4.2 Financing Plan and Loan Requirement

4.3 Security for Loan

4.4 Profit and Loss Statement

4.5 Cash Flow Statement

4.6 Balance Sheet

4.7 Loan Repayment Schedule

4.8 Break-even Point (BEP)

4.9 Return on Investment (ROI)

4.10 Financial Analysis

2.10 Summary

Virtually to start any type of business or expand the existing one needs to work on opportunity identification and evaluation, business idea development and then prepare business plan. Lack of proper opportunity identification and evaluation, idea development process and business planning are the most often cited reasons for business failure.

Opportunity identification and evaluation are the initial stages of the entrepreneurial process and principal activities that take place before a business is formed or structured. The opportunity identification and evaluation process have five main steps namely, getting the idea/scanning the environment, identifying the opportunity, developing the opportunity, evaluating the opportunity and evaluating the team.

After opportunity is recognized, you need to have a clear idea of the sort of business you want to run. Your business idea will address: Which need will your business fulfill for the customers and what kind of customers will you attract?; What good or service will your business sell? Who will your business sell to? And how is your business going to sell its goods or services? All business ideas are not equally worth. Therefore, to identify promising business idea among others, it is important to answer the raised questions so that to proceed into the phase of preparing plan on the selected business idea.

Business plans help companies identify their goals and objectives and provide them with tactics and strategies to reach those goals. It is not historical document; rather, they embody a set of management decisions about necessary steps for the business to reach its objectives and perform in accordance with its capabilities. Business plans have several major uses. These include internal planning and forecasting, obtaining funding for ongoing operations or expansion, planned divestiture and spinoffs, and restructuring or reorganizing. While business plans have elements common to all uses, most business plans are tailored according to their specific use and intended audience.

Business plan is an outline of a business giving details of the finance, assets, staff, products or services and markets. It guides the entrepreneur, identifies possible problems and is also used in funding applications. The business plan sets out how the owner of a business intends to realize its objectives. Steps in a business plan include: Idea Generation, Environmental Scanning, Feasibility Analysis, Functional Plan (Marketing plan, financial plan, organizational plan and operational plan), Project Report Preparation, Evaluation, Control and Review.

2.11 Review Questions

1. List and discuss opportunity Identification steps.

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   ………………………………………………………………………………………………
2. Discuss the business idea Identification processes.

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   ………………………………………………………………………………………………
3. List at least three approaches of business idea generation and discuss them.

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   ………………………………………………………………………………………………
4. Discuss steps involved in business planning process.

   ………………………………………………………………………………………………

   ………………………………………………………………………………………………
5. Discuss the Components of Business Plan.

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   ………………………………………………………………………………………………

CHAPTER 3: BUSINESS FORMATION

3.1 INTRODUCTION

A business formation deals with the formalization and actual implementation of business ideas in to practice. In today's economic development/transformation, small businesses are creating new jobs even as large businesses continue eliminating jobs and they are more flexible than large ones in the products and services they offer. This chapter discusses the issues of business development and the different legal forms of business. In addition, the concept of MSEs in the Ethiopian and international context are discussed. The importance/roles of MSEs and a business formation deal with the formalization and actual implementation of business ideas in to practice. This chapter discusses the issues of business development and the different legal forms of business. In addition the concept of MSEs in the Ethiopian and international context are discussed. The importance/roles and set up of MSEs are discussed very well. Besides the success and failure factors of MSEs and the common problems of MSEs in Ethiopia are discussed. Furthermore, the chapter highlights the reality in the era of entrepreneurship environment as, not only are the skills and abilities important, but the entrepreneur also will need to consider the personality and character of each individual to create a viable organization culture.

Chapter Objectives

After completing this chapter, students will be able to:

- Explain the Concept of Business Development;
- Identify the Forms of Business Ownership;
- Analyze the Importance/Role of MSEs;
- Set Up Small Scale Business;
- Distinguish the Failure and Success Factors of MSEs;
- Identify the Problems of Small Scale Business in Ethiopia; and
- Develop Organizational Culture.

3.2 The Concept of Small Business Development

Specifying size and standard to define small business is necessarily arbitrary, because people adopt different standards for different purposes. Based on socio- economic conditions, countries define small business differently. But all may use size and economic criteria as a base to define small business. Size criteria include number of employees and the startup capital. Size does not always reflect the true nature of an enterprise; in addition, qualitative characteristics are used to differentiate small business from other business. The economic/control definition covers market share, independence and personalized management.

Micro and small enterprises (MSEs) cover a wider spectrum of industries and play an important role in both developed and developing economies. Ethiopia is no exception and MSEs occupy a prominent position in the development of the Ethiopian economy. While the small entrepreneurs can set up a unit even with less capital, enjoy quick returns and have the flexibility to handle the vagaries(change) of the market, they have to face many problems like lack of finance, poor operations management, lack of experience, poor financial management, etc,. The process of setting up a venture begins with searching for an opportunity. Identifying a good opportunity is a difficult task and involves scanning the environment and the use of creativity and innovation.

3.3 Forms of Business (A Short Explanation)

There are three basic legal forms of business formation with some variations available depending on the entrepreneurs' needs.

The three basic legal forms are:-

1) Proprietorship,
2) Partnership, and
3) Corporation, with variations particularly in partnerships and corporations.

Legal Forms of Business	Description
1) Proprietorship	Form of business with single owner who has unlimited liability, controls all decisions, and receives all profits.
2) Partnership	Two or more individuals having unlimited liability who have pooled resources to own a business
3) Corporation	Separate legal entity that is run by stockholders having limited liability

These three basic legal forms are compared with regard to ***ownership, liability, start-up costs, continuity, transferability of interest, capital requirements, management control, distribution of profits, and attractiveness for raising capital.***

It is very important that the entrepreneur carefully evaluate the pros and cons of the various legal forms of organizing the new venture. This decision should be made before the submission of a business plan and request for venture capital.

The comparison for the three basic legal forms against the aforementioned factors is briefly presented in the table below:-

Table 3.1 Factors in Three Forms of Business Formation

Factors	Basic Forms of Business Formation		
	Proprietorship	**Partnership**	**Corporation**
Ownership	• Individual	• No limitation on number of partners.	• No limitation on number of stockholders.
Liability of Owners	• Individual liable for business liabilities.	• In general partnership, all individuals liable for business liabilities. • Limited partners are liable for amount of capital contribution. • In limited liability partnership (LLP), there is no liability except when negligence exists.	• Amount of capital contribution is limit of shareholder liability.
Costs of Starting Business	• None, other than filing fees for trade name.	• Partnership agreement, legal costs, and minor filing fees for trade name.	• Created only by statute. • Articles of incorporation, filing fees, taxes, and fees for states in which corporation registers to do business.
Continuity of Business	• Death dissolves the business.	• Death or withdrawal of one partner terminates partnership unless partnership agreement stipulates otherwise. • Death or withdrawal of one of limited partners has no effect on continuity.	• Greatest form of continuity. • Death or withdrawal of owner(s) will not affect legal existence of business.
Transferability of Interest	• Complete freedom to sell or transfer any part of business.	• General partner can transfer his/her interest only with consent of all other general partners. • Limited partner can sell interest without consent of general partners. No transfer of interest in an LLP.	• Most flexible. Stockholders can sell or buy stock at will. Some stock transfers may be restricted by agreement.
Capital Requirements	• Capital rose only by loan or increased contribution by proprietor.	• Loans or new contributions by partners require a change in partnership agreement. • In LLP partnership, entity raises money.	• New capital raised by sale of stock or bonds or by borrowing (debt) in name of corporation.

Management Control	• Proprietor makes all decisions and can act immediately.	• All general partners have equal control, and majority rules. • Limited partners have limited control. • Can vary in an LLP.	• Majority stockholder(s) have most control from legal point of view. • Day-to-day control in hands of management, who may or may not be major stockholders.
Distribution of Profits and Losses	• Proprietor responsible and receives all profits and losses.	• Depends on partnership agreement and investment by partners.	• Shareholders can share in profits by receipt of dividends.
Attractiveness for Raising Capital	• Depends on capability of proprietor and success of business.	• Depends on capability of partners and success of business.	• With limited liability for owners, more attractive as an investment opportunity.

LLP- Limited Liability Partnership

3.4 Definition and Role/Importance of MSEs in Developing Countries

3.4.1 Definition of MSEs

Small businesses are playing an important role in the industrial economy of the world. These are particularly important in the developing economies. Small business is predominant even in developed countries such as USA, Japan etc.

There is a difference between small business owners and entrepreneurial ventures as well. An entrepreneurial venture often is a growth-oriented innovative company with product or service offerings that are new to the market. Small businesses could be entrepreneurial ventures. Most entrepreneurial ventures start as a small business.

However, some discernible characteristics still differ them. Most small businesses' owners work with known products and services aimed at incremental growth, and their innovation is focused on sales, marketing, and market expansion. Entrepreneurial ventures incorporate a different set of strategies. These entities are aimed at rapid growth and apply innovation and creativity at every node of the business process. They work with new offerings, and they face a lot more uncertainties; hence, their strategy calls for continuous work on mitigating uncertainty and risk reduction.

Specifying size and standard to define small business is necessary because people adopt different standards for different purposes. For example, legislators may exclude small firms from certain regulations and specify ten employees as the cut-off point. Moreover, a business may be described as "small" when compared to larger firms, but "large" when compared to smaller ones. For example, most people would classify independently owned gasoline stations, neighborhood restaurants, and locally owned retail stores as small business.

Similarly, most would agree that the major automobile manufacturers are big businesses. And firms of in-between sizes would be classified as medium on the basis of individual viewpoints. There are two approaches to define small business. They are: Size Criteria, and Economic/control criteria.

1. **Size Criteria**

Even the criteria used to measure the size of businesses vary; size refers to the scale of operation. Some criteria are applicable to all industrial areas, while others are relevant only to certain types of business. For instance, some of the criteria used to measure size are: number of employees; volume, and value of sales turnover, asset size, and volume of deposits, total capital investment, volume/value of production, and a combination of the stated factors.

Even though the number of employees-is the most widely used yardstick, the best criterion in any given case depends upon the user's purpose. To provide a clearer image of the small firms, the following general criteria for defining a small business are suggested by Small Business Administration (SBA).

- Financing of the business is supplied by one individual or a small group. Only in a rare case would the business have more than 15 or 20 owners.
- Except for its marketing function, the firm's operations are geographically localized.
- Compared to the biggest firms in the industry, the business is small.
- The number of employees in the business is usually fewer than 100.

This size criteria based definition of MSEs varies from country to country. All over the world, number of employees or capital investment or both has been used as the basis for defining MSEs.

2. **Economic/Control Criteria.**

Size does not always reflect the true nature of an enterprise. In addition, qualitative characteristics may be used to differentiate small business from other business. The economic/control definition covers:

- Market Share,
- Independence, and

- Personalized Management.
- Geographical Area of Operation.

All four of these characteristics must be satisfied if the business is to rank as a small business.

I) ***Market Share*: -** The characteristic of a small firm's share of the market is that it is not large enough to enable it to influence the prices of national quantities of goods sold to any significant extent.

II) ***Independence*: -** Independence means that the owner has control of the business himself/herself. It, therefore, rules out those small subsidiaries which though in many ways fairly autonomous, nevertheless have to refer to major decisions (e.g., on capital investment) to a higher level of authority.

III) ***Personalized Management:* -** It is the most characteristics factor of all. It implies that the owner actively participates in all aspects of the management of the business, and in all major decision-making process. There is little delegation of authority and one person is involved when anything material is involved.

IV) ***Technology*: -** Small business is generally labor intensive and only few are technology intensive.

V) ***Geographical Area of Operation*: -** The area of operation of a small firm is often local.

Generally, small business is a business that is privately owned and operated, with a small number of employees and relatively low volume of sales.

3.4.2 Role/Importance of MSEs in Developing Countries

Micro and Small Enterprises (MSEs) cover a wider spectrum of industries and play an important role in both developed and developing economies. Ethiopia is no exception and MSEs occupy a prominent position in the development of the Ethiopian economy. Over the years, the number of MSEs is growing from time to time and they need a strong support on Scio- economic and political ground. Some of the contributions are hereunder.

1) **Large Employment Opportunities:** MSEs are generally labor-intensive. For every fixed amount of investment, MSE sector provides employment for more persons as against few persons in the large scale sector. Thus in a country like Ethiopia where capital is scarce and labor is abundant, MSEs are especially important.
2) **Economical Use of Capital**: MSEs need relatively small amount of capital. Hence it is suitable to a country like Ethiopia where capital is deficient.

3) **Balanced Regional Development/ Removing Regional Imbalance**/: Generally small enterprises are located in village and small towns. Therefore it is possible to have a balanced regional growth of industries. Ethiopia is a land of villages.

Another problem is the continuous shifting of people from rural to urban areas which causes over-crowding in cities with slum conditions due to lack of social and medical amenities which require heavy investments. This problem can be solved by inducing people to set up micro and small firms in rural areas.

Large scale industries have the tendency to concentrate in big cities. As a result, semi urban and rural areas remain deprived of the benefits of industrialization. Moreover, undue concentration of large industries in urban areas creates several problems, e.g., pollution, shortage of civic facilities, etc. Due to lack of employment opportunities in the country side, people migrate in large numbers to big cities. Micro and small-scale units can be located in rural and semi urban areas to reduce regional disparities.

4) **Equitable Distribution of Wealth and Decentralization of Economic Power**: It removes the drawbacks of capitalism, abnormal profiteering, concentration of wealth and economic power in the hands of few etc.
5) **Unregulated Growth of Larg**e-scale industries results in concentration of economic· power in the hands of a few; and consequently, gross inequalities in the distribution of income and wealth will occur. On the other hand; income generated in a large number of small enterprises is dispersed more widely and its benefit is derived by the large segments of the society. This is due to wide spread ownership and decentralized location of small scale enterprises. In this way, small & medium scale enterprises bring about greater equality of income distribution. It is also argued that most of the micro and small scale units are either proprietary or partnership concerns. As a result, relations between workers and employers are more harmonious in micro and small enterprises than in large enterprises. Micro and small enterprises also encourage competitive spirit and generate the impetus to self-development.
6) **Dispersal over Wide Areas**- MSEs has a tendency to disperse over wider areas and they play a key role in the industrialization of a developing country.
7) **Higher Standard of Living**: MSEs bring higher national income, higher purchasing power of people in rural and semi-urban areas.

8) **Mobilization of Locals Resources/Symbols of National Identity**: The spreading of industries even in small towns and villages would encourage the habit of thrift and investment among the people of rural areas.

Small scale businesses are locally owned and controlled, and can strengthen family and other social systems and cultural traditions. They are perceived as valuable in their own right as well as symbols of national identity.

9) **Innovative and Productive /Simple Technology**: New but simple techniques of production can be adopted more easily by MSEs without much investment.

Small businesses are highly innovative though they do not maintain their own research and development.

10) **Less Dependence on Foreign Capital/ Export Promotion**: MSEs use relatively low proportion of imported equipment and materials. The machinery needed for these industries can be manufactured within the country. Micro and small scale enterprises are opening up fresh avenues in the export market in our world. Realizing the importance of the small and medium- scale sectors in the economy; the Ethiopian government has adopted several measures to speed up the growth of micro and small size enterprises.
11) **Promotion of Self Employment**: MSEs foster individual skill and initiative and promote self-employment particularly among the educated and professional class.
12) **Protection of Environment**: MSEs help to protect the environment by reducing the problem of pollution.
13) **Shorter Gestation Period**: In these enterprises the time-lag between the execution of the investment project and the start of flow of consumable goods is relatively short.
14) **Facilitate Development of Large Scale Enterprises**: MSEs support the development of large enterprises by meeting their requirements of inputs of raw materials, intermediate goods, spare parts etc. and by utilizing their output for further production.
15) **Individual Tastes, Fashions, and Personalized Services**: Small businesses have the flexibility to adapt quickly to changes in the business or technological environment.
16) **More Employment Creation Capacity***:* Economic planners have realized the necessity of encouraging micro and small enterprises because they require less capital but generate more employment. The micro and small scale sectors have the capacity to generate a much higher degree of employment than the large-scale sector. This is because micro and small

scale enterprises are labor intensive and thus create more employment with a given level of capital. More production needs more capital in such a situation. The micro and small firms will stand in good position because they are less capital intensive and more labor intensive.

3.5 Classification of Micro and Small Enterprises

1. **In Case of Manufacturing Enterprise (Manufacturing, Construction and Mining):**
   a) ***A Micro Enterprise*** is one in which the investment in plant and machinery (total asset) does not exceed birr100, 000 (one hundred thousand); and operates with 5 people including the owner.
   b) ***Small Enterprises*** is one in which the investment in plant and machinery (a paid up capital of total asset) of birr100, 000 (one hundred thousand) and not more than Birr 1.5 million; and operates with 6-30 persons.
2. **In Case of Service Enterprise (Retailing, Transport, Hotel and Tourism, ICT and Maintenance):**
   a) ***A micro enterprise*** is one with the values of total asset is not exceeding Birr 50,000(fifty thousands); and operates with 5 persons including the owner of the enterprise.
   b) ***Small Enterprises*** is one in which the total asset value or a paid up capital of birr100, 000 (one hundred thousand) and not more than Birr 1.5 million; and operates with 6-30 persons.

More clearly, the improved definition of MSE is presented in the table below.

Table 3.2 Improved Definitions of MSEs

Level of the Enterprise	Sector	Human Power	Total Asset
Micro Enterprise	Industry	≤ 5	$\leq$ 100000($6000 or E4500)
	Service	≤ 5	$\leq$ 50,000($3000 or E2200)
Small Enterprise	Industry	6-30	$\leq$ birr 1.5 million ($9000 or E70000)
	Service	6-30	$\leq$ birr 500,000 ($30000 or E 23000)

When ambiguity is encountered between manpower and total assets as explained above, total asset is taken as primary yardstick.

Priority Sectors and Sub-Sectors for MSEs Engagement In Ethiopia

1. ***Manufacturing* Sector-** This is the one which comprises textile and garment; leather and leather products; food processing and beverage; metal works and engineering wood works including furniture and ornaments service; and agro-processing.
2. **Construction Sectors-** This is the one which comprises **s**ub-contracting; building materials; traditional mining works; cobble stone; infrastructure sub-contract; and prestigious goods
3. **Trade Sectors- This** is the one which comprises whole sale of domestic products; retail sale of domestic products and raw materials supply.
4. **Service Sectors-** This is the one which comprises small and rural transport service; café and restaurants; store service; tourism service; canning/packing service; management service; municipality service; project engineering service; product design & development service; maintenance service; beauty salon; and electronics software development; decoration and internet café.
5. **Agriculture Sector (Urban Agriculture**) - This is the one which comprises modern livestock raring; bee production; poultry; modern forest development; vegetables and fruits; modern irrigation; and animal food processing.

- **Levels of MSEs in Ethiopia**

Start-up:- Start up level refers to enterprises that incorporate people who are interested to establish MSE and those who completed the required profession/skill from various institutions and innovated by legally either in the form of association or private. It is a level where an enterprise begins production and service under legal framework or legal entity.

Growth Level: - An enterprise is said to be at growth level when an enterprise become competent in price, quality and supply and profitable using the support provided. At this level, the enterprise man power and total asset is larger than at startup level; and use book keeping system.

Maturity Level: - Maturity level means when an enterprise able to be profitable and invest further by fulfilling the definition given to the sector and using the support provided.

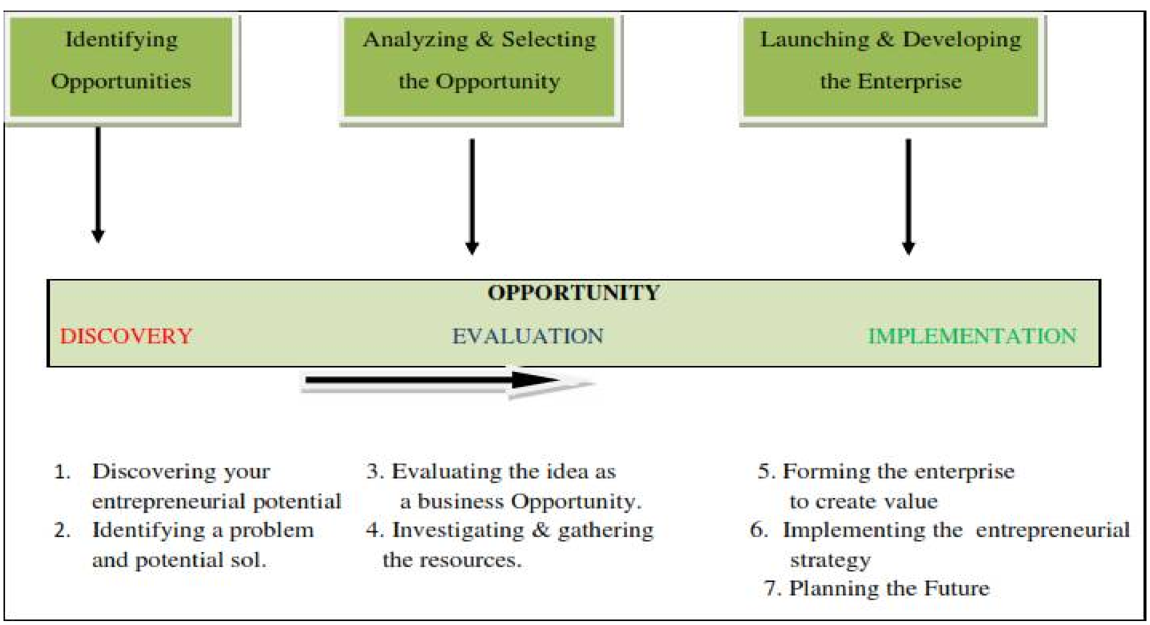
Growth- Medium Level:- An enterprise is said to be transformed from small to medium level of growth is when it enabled to be competent in price, quality and supply using the support given to the level.

3.6 Setting up Small Scale Business

Steps for Setting up the Entrepreneurial Venture

Once an individual decides to take up entrepreneurship as a career path, to be a job provider instead of a job seeker, s/he has to establish an enterprise. However, setting up of a small new enterprise is a very challenging as well as a rewarding task. Several problems are involved in this task. It is extremely important to take utmost care in identifying the product or service to be launched by the entrepreneur; otherwise it might prove to be a costly mistake. After tentatively identifying four to five ideas, s/he should go in for detailed assessment and feasibility study. This will help the entrepreneur to crystallize one idea in an objective and systematic manner, which will greatly enhance his/ her chances of success.

The entrepreneurial process of launching a new venture can be divided into three key stages of: Discovery; Evaluation; and Implementation. These can be further sub-divided into seven steps as shown below:



Discovery: The first stage of discovery is to identify opportunities that may form the basis of an entrepreneurial venture. It requires creative thinking to indentify issues that can benefit from an entrepreneurial vision. This stage can be divided into two steps:

Step 1 Discovering your entrepreneurial potential - the first step is to know more about your personal resources and attributes through some self-evaluation– what will you bring to the venture? What are your strengths and challenges? These will affect the type of venture you choose.

Step 2 Identifying a problem and potential solution – a new venture has to solve a problem and meet a genuine need.

Evaluation: By the end of first stage of discovery, you should have selected an idea worthy of further detailed investigation. The next stage evaluates if this all adds up to a feasible business in two further steps:

Step 3 Evaluating the idea as a business opportunity– find out information about the market need. Is the solution to this problem really wanted by enough customers? Investigate the feasibility of the proposed solution (technically, economically, socially, and legally).

Step 4 Investigating and gathering the resources – How will the product/service get to market? How will it make money? What resources are required?

Exploitation: By the end of the second stage of evaluation, you should have identified an opportunity that has reasonable prospects of success, and analyzed what is required to launch it. The next stage is to make the final preparations and launch it into the market. It can be developed in three further steps:

Step 5 Forming the enterprise to create value – set up a business entity and protect any intellectual property. Get ready to launch the venture in a way that minimizes risk and maximizes returns.

Step 6 Implementing the entrepreneurial strategy – activate the marketing, operating, and financial plans.

Step 7 Planning the future – look ahead and visualize where you want to go.

Environmental Analysis: Entrepreneurship does not exist in a vacuum. It is affected by and affects the environment. Relationship between entrepreneurship and environment is shown in the figure below.

Figure 3.1 Entrepreneurship vs Environment

As the economies are getting internationally integrated, for an analysis of the environment of entrepreneurship you would be required to develop an understanding of macroeconomic, and industry/sector specific factors.

a) Macro Environment

The macro environment of an entrepreneur consists of the political, technological, social, legal and economic environments. All of these are not immediate part of the entrepreneur's venture yet they have an impact on his/her enterprise.

b) Sectoral Analysis

After having understood the general environment in which the business has to take birth, it is important to study the sector or industry conditions in which the entrepreneur proposes to launch a venture. This will help to put the proposed venture in the proper context. The purpose of industry analysis is to determine what makes an industry attractive- this is usually indicated either by above normal profits or high growth rates. For such analysis one should study the history of the industry, the future trends, new products developed in the industry, forecasts made by the government or the industry. It is also advisable to study the existing or potential competition, threat of substitutes and entry barriers. Sometimes there might be bilateral agreements between countries regarding some sectors or government policy that is sector specific or some event that throw up challenges.

There might be certain constraints regarding availability of technology, manpower or raw materials, which are industry specific. Similarly, there might be certain strengths of a particular sector, which might outweigh some negative general trends. ***For instance,*** currently the cement and steel sector are on an upward swing with a favorable climate in the housing sector as well as government's thrust on the construction sector.

SWOT Analysis

At this stage, conducting a SWOT analysis will help the entrepreneur to clearly identify his/her own strengths and weaknesses as well as the opportunities and threats in the environment.

Strengths are positive internal factors that contribute to an individual's ability to accomplish his/her mission, goals and objectives. *Weaknesses* are negative internal factors that inhibit an individual's ability to accomplish his/her mission, goals and objectives. An entrepreneur should try to magnify his strengths and overcome or compensate for his/her weaknesses.

Opportunities are positive external options that an individual could exploit to accomplish his/her mission, goals and objectives. *Threats* are negative external forces that hinder an individual from accomplishing his/her mission, goals and objectives. These could arise due to competition, change in government policy, economic recession, technological advances etc. *Threats* in the environment can arise from competition, technological breakthroughs, change in government policies etc. S/he might possess certain unique skills or abilities, which along with his/ her knowledge and experience can provide him/ her cutting edge.

An analysis of the above can give the entrepreneur a more realistic perspective of the business, pointing out foundations on which s/he can build future strengths and remove obstacles. The hierarchical approach to the development of business idea is given below.

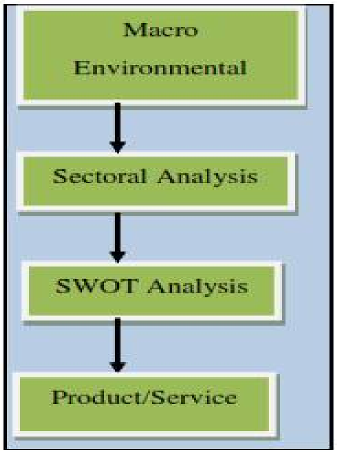


Figure 3.2 Hierarchical of Environmental Analyses

The entrepreneur has to use the opportunities provided by the environment, combine these with his/her unique strengths in terms of knowledge, skills, experience etc. and then take a decision to launch a particular product or service. The proposed product / service should be compatible with the capability of the entrepreneur, resources available in the environment and the need of the society.

3.7 Small Business Failure and Success Factors

3.7.1 Small Business Failure Factors

What Is Business Failure?

Even though business owners launch their ventures with the best of intentions and work long, hard hours, some businesses inevitably fail. Dun & Bradstreet, a financial research firm, defines a business failure as a business that closes as a result of either (1) actions such as bankruptcy, foreclosure, or voluntary withdrawal from the business with a financial loss to a creditor; or (2) a court action such as receivership (taken over involuntarily) or reorganization (receiving protection from creditors).

Causes of Business Failure

The rates of business failure vary greatly by industry and are affected by factors such as type of ownership, size of the business, and expertise of the owner. The causes of business failure are many and complex; however, the most common causes are inadequate management and financing.

Although financial problems are listed as the most common cause of business failure, consider management's role in controlling them. Could business failure due to industry weakness be linked to poor management? Yes, if the owner tried to enter an industry or market with no room for another competitor or responded only slowly to industry changes. High operating expenses and insufficient profit margins also reflect ineffective management. Finally, business failure due to insufficient capital suggests inexperienced management.

Inadequate Management: - *Business* management is the efficient and effective use of resources. For small business owners, management skills are especially desirable—and often especially difficult to obtain. Lack of experience is one of their most pressing problems. Small business owners must be generalists; they do not have the luxury of specialized management. On the one hand, they may not be able to afford to hire the full-time experts who could help avert costly mistakes. On the other hand, their limited resources will not permit them to make many mistakes and stay in business. As a small business manager, you will probably have to make decisions in areas in which you have little expertise.

Entrepreneurs are generally correct in pointing to internal factors as the reason for the failure of their businesses; these factors are the cause of 89 percent of such failures. Internal problems are those more directly under the control of the manager, such as adequate capital, cash flow, facilities/equipment inventory control, human resources, leadership, organizational structure, and accounting systems.

The manager of a small business must be a leader, a planner, and a worker. You may be a “top gun” in sales, but that skill could work against you. You might be tempted to concentrate on sales while ignoring other equally important areas of the business, such as record keeping, inventory, and customer service.

Inadequate Financing: - Business failure due to inadequate financing can be caused by improper managerial control as well as shortage of capital. On the one hand, if you don’t have adequate funds to begin with, you will not be able to afford the facilities or personnel you need to start up the business correctly. On the other hand, if you do possess adequate capital but do not manage your resources wisely, you may be unable to maintain adequate inventory or keep the balance needed to run the business.

There are a lot of ways to fail in business. You can extend too much credit. You can fail to plan for the future or not have strategic direction. You can overinvest in fixed assets or hire the wrong people. Identifying mistakes that can be made is merely one component of the problem. Figuring out how to avoid them is the hard part.

Other common causes of business failure include *Neglect, Fraud, and Disaster*.

- *Neglect* occurs whenever an owner does not pay a due attention to the enterprise. The owner who has someone else managing the business while s/he goes fishing often finds the business failing because of neglect.
- *Fraud* involves intentional misrepresentation or deception. If one of the people responsible for keeping the business’s books begins purchasing materials or goods for himself or herself using the business's money, the business might find itself bankrupt before too long.
- *Disaster* refers to some unforeseen happening. If a hurricane hits the area and destroys the property in the company's yard, the loss may require the firm to declare bankruptcy. The same is true for fires, burglaries, robberies, or extended strikes.

Business Termination versus Failure

There is a difference between a business termination and a business failure. A termination occurs when a business no longer exists for any reason. A failure occurs when a business closes with a financial loss to a creditor.

Reasons for a termination abound. The owner may have an opportunity to sell her business to someone else for a healthy profit, or be ready to move on to a new business or to retire, or s/he may have simply lost interest in the business. The market for the business's product may have changed or become saturated. Perhaps the owner has decided it would be more appealing to work for someone else. In other cases, businesses may change form. A partnership may be restructured as a corporation, or a business may move to a new location. Businesses that undergo such changes are considered terminated even though they continue in another form.

Mistakes Leading to Business Failure

No one likes to think about failing, yet many small business owners invite failure by ignoring basic rules for success. One of the most common mistakes is to neglect to plan for the future because planning seems too hard or time-consuming. Planning what you want to do with your business, where you want it to go, and how you're going to get there are prerequisites for a sound business. Of course, that doesn't mean you can't change your plans as circumstances dictate. Your plan should provide a road map for your business, showing you both the expressways and the scenic routes and the detours.

Another common mistake is failing to understand the commitment and hard work that are required for turning a business into a success. Having to work long hours and do things you don't enjoy because no one else is available to do them are part and parcel of owning a small business. Yet, when you have the freedom of being your own boss, the hard work and long hours often don't seem so demanding!

Still another mistake that small business owners make, particularly with rapidly growing businesses, is not hiring additional employees soon enough or not using existing employees effectively. There comes a point in the growth of a business when it is no longer possible for the manager to do it all, but s/he resists delegation in the belief that it means s/he is giving up control. It is important to recognize that delegating tasks to others isn't giving up control—it's giving up the execution of details.

The last type of mistake involves with finances. Inaccurate estimates of cash flow and capital requirements can swamp a business quickly. Figuring the correct amount of money needed for starting a business is a tough balancing act: Asking for too little may hinder growth and actually jeopardize survival, whereas asking for too much might cause lenders or investors to hesitate. An important rule to remember in terms of arranging financing or calculating cash-flow projections is to figure the unexpected into your financial plans. In this way, you can have more of a cushion to fall back on if things don't go exactly according to plan. After all, without the right amount of capital, it's impossible to succeed.

Business failure, then, is a serious reality. How can a small business owner avoid it? Difficult changes may be needed, and change requires leaders to overcome all sorts of human dynamics, like inertia, tradition, and head-in-the-sand hoping that things will get better. Strategic moments require courage, or at least a lack of sentimentality, which is rare.

It is in these moments that the best leaders find a mirror and ask themselves the defining question that the late, great Peter drucker posed nearly 40 years ago: "If you weren't already in your business, would you enter it today?" If the answer is no, Drucker said, you need to face a second tough question: "What are you going to do about it?" Every leader should heed this good advice and, if need be, follow it through to its conclusion, whether that will be to fix, sell, or close the business.

Reflection: For instance, starting a business does involve risk, but the assumption of risk is part of life. An Economic consultant, David Birch, conducted his research on 2007 and found the divorce rate was 3.7 per 1,000. Of every 10,000 students who start college, about 52 percent fail to graduate. Would you decide not to get married because the divorce rate is too high? Were you afraid to go to college because of the dropout rate? The point to remember is that if you have a clear vision, know your product and your market, and devote the time and effort needed, your small business, like many others, can succeed.

3.7.2 Small Business Success Factors

When large and small businesses compete directly against one another, it might seem that large businesses would always have a better chance of winning. In reality, small businesses have certain inherent factors that work in their favor. You will improve your chances of achieving success in running a small business if you identify your competitive advantage, remain flexible and innovative, cultivate a close relationship with your customers, and strive for quality.

It may come as a surprise, but big businesses need small businesses a symbiotic relationship exists between them. For instance, John Deere relies on hundreds of vendors, many of which are small, to produce component parts for its farm equipment. Deere's extensive network of 3,400 independent dealers comprising small businesses provides sales and service for its equipment. These relationships enable Deere, the world's largest manufacturer of farm equipment, to focus on what it does best, while at the same time creating economic opportunity for hundreds of individual entrepreneurs.

Small businesses perform more efficiently than larger ones in several areas. For example, although large manufacturers tend to enjoy a higher profit margin due to their economies of scale, small businesses are often better at distribution. Most wholesale and retail businesses are small, which serves to link large manufacturers more efficiently with millions of consumers spread all over the world.

Small business success factors can be seen the same as the efforts exerted in reversing the factors of failure. There are several positive steps in addition to planning that business owners can take to improve a firm's chance for success.

From the discussion about factors of failure, we can conclude that a proper attitude is important to ensure a customer orientation for quality and service; the owner must have a purpose for being in business and want to provide customers with value for their money; and having a variety of basic business skill is important (such as the ability to keep accounting records.) So, by understanding why business fail, entrepreneurs can discover ways to tilt the scales towards success. These success factors are categorized as:-

1. Conducive Environment;
2. Adequate Credit Assistance;
3. Markets and Marketing Support.

1. **Conducive Environment**

Successful small enterprises do not emerge, and thereafter survive and grow unless the environment is conductive. *Political, economic, technological and socio-cultural factors* in the environment impinge upon the life of the small enterprises and generate much of the needs required for their existence.

Political Climate: - The overall political climate in a country is important for the small scale entrepreneur to consider. Small scale entrepreneur will need positive and encouraging measures by government and political constituencies to establish private investment. Such measures could include liberal or nonrestrictive investment policy, creation of promotional agencies, creation of industrial estates and free trade zones and availability of low-cost loan capital for private investors.

The Economic Environment: - An analysis of the economic environment is particularly helpful in investment decision, market measurement and in forecasting.

The general state of the economy dictates what the small enterprise will need especially since it is handicapped in obtaining capital and credit owning to greater unit costs of small transactions, greater risks involved, etc. .

Technology: - Technological advances in the environment create new needs for the small entrepreneur as far as adaptation and adjustment is concerned.

Small scale entrepreneur needs to learn how to adjust to the new technological environment surrounding him/her, or needs to take a set of advance technologies and bring these to his/her own level in the small enterprise. Either way, constant reexamination is needed for possible utilization and improvement of existing technologies.

Socio-Cultural Environment: - Finally, the socio-cultural environment also creates a very important climate for the survival of the enterprises.

2. **Adequate Credit Assistance**

Small enterprise development cannot be ensured without arrangement for financing. Adequate and timely supply of credit is critical for new entrepreneurs to emerge especially from a wide base. A great majority of micro and smalbusiness activities have come about because of special financing programs offered to them.

Thus, requirements are less strict in terms of lower interest rates than the prevailing commercial rates; less collateral requirements and lower equity ratio; various assistance schemes such as preparing the project study; etc.

3. **Markets and Marketing Support**

Market for a small enterprise in a developing country can be quite a problem. The small business entrepreneur will be in competition not only with locally mass-produced goods but even imports.

Small enterprises can brand together and sell their products as one body through closely-knit associations or organizations. The government too can take an active part in marketing specific products or assisting small groups of entrepreneurs in selling their products.

3.8 Main Supporting Packages for MSEs Development in Ethiopia

When entrepreneurs are deciding to involve and develop MSEs in Ethiopia, they are more likely entitled with some supporting packages which include awareness creation about the sector; provision of legal services, to form legal business enterprises; providing Technical and business management training; financial support based on personal saving, 20/80 (the beneficiaries are save 20% and the MFIs provide Loan 80% of the projects); facilitate working premises; industry extinction services and BDS provision; bookkeeping and audit services.

3.9 Problems of Small Scale Business in Ethiopia

Small-scale businesses have not been able to contribute substantially to the economic development, particularly because of financial, production, and marketing problems. These problems are still major handicaps to their development. Lack of adequate finance and credit has always been a major problem of the Ethiopian small business.

Small-scale units do not have easy access to the capital because they mostly organized on proprietary and partnership basis and are of very small size. They do not have easy access to industrial sources of finance partly because of their size and partly because of the fact that their surpluses which can be utilized to repay loans are relatively small. Because of their size and partly because of the limited profit, they search for funds for investment purposes. Consequently, they approach traditional money lenders who charge extra high rate of interest hence small enterprise continue to be financially weak.

Small scale enterprises find it difficult to get raw materials of good quality at reasonable prices in the field of production. Furthermore, the techniques of production, which the enterprises have adopted, are usually outdated. Because of their poor financial position they are not able to buy new equipment, consequently their productivity suffers.

Small business's owner can avoid some of the common pitfalls that lead to business failure by knowing the business in depth; developing a solid business plan; managing financial resources; understanding financial statements; and learning to manage people effectively.

3.9 Organizational Structure and Entrepreneurial Team Formation

3.9.1 Introduction

We can perceive from the experiences of companies the importance of employees and their loyalty and commitment to the organization. Also significant to potential investors is the management team and its ability and commitment to the new venture.

Investors will usually demand that the management team not attempt to operate the business as a sideline or part-time venture while employed full time elsewhere. It is assumed that the management team is prepared to operate the business full time and at a modest salary. It is unacceptable for the entrepreneurs to try to draw a large salary out of the new venture, and investors may perceive any attempt to do so as a lack of psychological commitment to the business.

3.9.2 Designing the Organization

Generally, the design of the initial organization will be simple. In fact, the entrepreneur may find that he or she performs all the functions of the organization alone. This is a common problem and a significant reason for many failures.

The entrepreneur sometimes thinks that he or she can do everything and is unwilling to give up responsibility to others or even include others in the management team. In most cases when this occurs, the entrepreneur will have difficulty making the transition from a start-up to a growing, well-managed business that maintains its success over a long period of time.

Regardless of whether one or more individuals are involved in the start-up, as the workload increases, the organizational structure will need to expand to include additional employees with defined roles in the organization. Effective interviewing and hiring procedures will need to be implemented to ensure that new employees will effectively grow and mature with the new venture.

All the design decisions involving personnel and their roles and responsibilities reflect the formal structure of the organization. In addition to this formal structure, there is an informal structure or organization culture that evolves over time that also needs to be addressed by the entrepreneur.

For many new ventures, predominantly part-time employees may be hired, raising important issues of commitment and loyalty. However, regardless of the number of actual personnel involved in running the venture, the organization must identify the major activities required to operate it effectively.

The design of the organization will be the entrepreneur's formal and explicit indication to the members of the organization as to what is expected of them. Typically, these expectations can be grouped into the following five areas:-

- *Organization structure*- This defines members' jobs and the communication and relationship these jobs have with each other. These relationships are depicted in an organization chart.
- *Planning, measurement, and evaluation schemes*- All organization activities should reflect the goals and objectives that underlie the venture's existence. The entrepreneur must spell out how these goals will be achieved (plans), how they will be measured, and how they will be evaluated.
- *Rewards*- Members of an organization will require rewards in the form of promotions, bonuses, praise, and so on. The entrepreneur or other key managers will need to be responsible for these rewards.
- *Selection criteria*- The entrepreneur will need to determine a set of guidelines for selecting individuals for each position.
- *Training*- Training, on or off the job, must be specified. This training may be in the form of formal education or learning skills.

In a nutshell, the organization's design can be very *simple*-that is, one in which the entrepreneur performs all the tasks (usually indicative of a start-up) -or *more complex*, in which other employees are hired to perform specific tasks. As the organization becomes larger and more complex, the preceding areas of expectation become more relevant and necessary.

As the organization evolves, the manager or entrepreneur's decision roles also become critical for an effective organization. As an entrepreneur, the manager's primary concern is to adapt to changes in the environment and seek new ideas. When a new idea is found, the entrepreneur will need to initiate development either under his or her own supervision or by delegating the responsibility to someone else in the organization. In addition to the role of adaptor, the manager will also need to respond to pressures such as an unsatisfied customer, a supplier reneging on a contract, or a key employee threatening to quit. Much of the entrepreneur's time in the start-up will be spent "putting out fires."

Another role for the entrepreneur is that of allocator of resources. The manager must decide who gets what. This involves the delegation of budgets and responsibilities. The allocation of resources can be a very complex and difficult process for the entrepreneur since one decision can significantly affect other decisions. The final decision role is that of negotiator. Negotiations of contracts, salaries, prices of raw materials, and so on are an integral part of the manager's job, and since he or she can be the only person with the appropriate authority, it is a necessary area of decision making.

3.9.3 Building the Management Team and a Successful Organization Culture

In conjunction with the design of the organization, the entrepreneur will need to assemble the right mix of people to assume the responsibilities outlined in the organization structure.

Some of the issues identified in the organization design will be revisited here since they are not only critical to the building of the team but are just as important in establishing a positive and successful organization culture.

This strategy must be maintained through the stages of start-up and growth of the enterprise. There are some important issues to address before assembling and building the management team. In essence, the team must be able to accomplish three functions:-

- Execute the business plan;
- Identify fundamental changes in the business as they occur; and
- Make adjustments to the plan based on changes in the environment and market that will maintain profitability.

Although these functions may seem simple and easy to achieve, the people engaged and the culture promoted by the entrepreneur are critical in accomplishing these functions. As we underscored in the organization design section, the entrepreneur will first need to assume the responsibility of determining what skills and abilities are needed to meet the goals in the business plan. Not only are the skills and abilities important, but the entrepreneur also will need to consider the personality and character of each individual to create a viable organization culture.

The organization culture will be a blend of attitudes, behaviors, dress, and communication styles that make one business different from another. There is no specific technique for accomplishing this since every organization will be different. One thing that is important is that the entrepreneur(s) need to be able to delegate responsibility in order to create a vibrant organizational culture.

Let us explore some of the important considerations and strategies in recruiting and assembling an effective team and hence in creating an effective and positive organization culture.

- ***First***, the entrepreneur's desired culture must match the business strategy outlined in the business plan. It can be done by working with his/her staff to develop the Core Family Values that represent the key elements of the firm's culture and strategy. In other words, takes a hands-on approach to leadership but then steps away to let everyone make their own decisions regarding company strategy.
- ***Second***, the leader of the organization must create a workplace where employees are motivated and rewarded for good work.
- ***Third***, the entrepreneur should be flexible enough to try different things. This is not always possible in a very small organization but has been the successful strategy in the growth of Google. The leadership of this company has an abundance of talent, and the attitude of management is that this talent needs to be given enough flexibility to make decisions, as long as they do so within the model established by the company.
- ***Fourth***, it is necessary to spend extra time in the hiring process. There is sometimes a tendency to want to hurry the process of finding the appropriate skills to fill the organization's needs. As always happened, there is more to a person than his or her skills. Character is also an important factor in building an effective organization culture.

✓ ***Next***, the entrepreneur needs to understand the significance of leadership in the organization. Leadership should help establish core values and provide the appropriate tools so that employees can effectively complete their jobs.

✓ An approach such as, "We're all in this together, no one is bigger than anyone else, and here are the rules we live by," can lead to greater challenges and job satisfaction.

✓ A reward system can play an important role in providing consistent and positive behavior patterns.

All in all, finding the most effective team and creating a positive organization culture is a challenge for the entrepreneur but is just as critical as having an innovative, marketable product. It is an important ingredient in an organization's success.

3.10 Chapter Summary

- ☞ Launching a new venture and becoming an entrepreneur is an exciting and challenging task. Can you learn how to be an entrepreneur or are some people just born that way? Some have argued that great entrepreneurs like Anita Roddick and Mohammed Yunis are simply born with different qualities to the rest of us – and it is these qualities that explain their success as entrepreneurs. But we know that a key human quality is the ability to change and develop over time. This is good news for anyone who wants to become an entrepreneur because it will require you to adapt and change with the enterprise you are founding as it develops and faces challenges. Becoming an entrepreneur is a never ending lesson as new challenges arise that offer experiences in how to do and not to do things.
- ☞ Small businesses include a wide variety of business types that are independently owned, operated, and financed. By itself, each individual small business has relatively little impact in its industry.
- ☞ Small businesses provided the economic foundation on which the country's economy was built. Today these businesses are creating new jobs even as large businesses continue eliminating jobs. Small businesses are more flexible than large ones in the products and services they offer. Most real product innovations come from small businesses.
- ☞ As the population becomes more diverse, the owners and employees of small businesses are likewise becoming more diverse. Businesses owned by women and minorities are growing at a faster rate than the overall rate of business growth. Diversity is important in small business because a wide range of viewpoints and personal backgrounds can improve problem solving.
- ☞ Small and large businesses need each other to survive—they have a symbiotic relationship. This relationship provides opportunities to small businesses in that they can supply needed parts to large manufacturers and can distribute manufactured goods. Moreover, small businesses often pick up functions that large businesses outsource. Other opportunities exist for small businesses where they enjoy the advantage of being able to profitably serve smaller niches than can their larger counter-parts. For all these reasons, small businesses are rapidly becoming important players in international trade.

- ☞ Ineffective and inefficient management, which shows up in many ways, is the number one cause of business failure. Inadequate financing, industry weakness, inexperience, and neglect are other major causes.
- ☞ To prevent your small business from becoming another casualty noted in business failure statistics, you must begin with a clearly defined competitive advantage. You must offer a product or service that people want and are willing to buy. You must do something substantially better than your competition does it. You must remain flexible and innovative, stay close to your customers, and strive for quality.
- ☞ In conjunction with the design of the organization, the entrepreneur will need to assemble the right mix of people to assume the responsibilities outlined in the organization structure.
- ☞ In the era of entrepreneurship environment, not only are the skills and abilities important, but the entrepreneur also will need to consider the personality and character of each individual to create a viable organization culture.

3.12 Questions for Review and Discussions

1. How would you define small business?
2. Name a company that seems large but might be classified as small because it has relatively little impact on its industry.
3. Why are small businesses more likely than large businesses to be innovative?
4. How would you show that small business is becoming a more important part of the economy?
5. We compared the failure rate for small businesses with the divorce rate in marriage and the student failure rate in college. Are these fair comparisons?
6. Describe four causes of small business failure.
7. How does the quality of management relate to each of these causes?
8. Describe the techniques that a business with which you are familiar has used to prevent its failure.
9. Predict the future of small business. In what industries will it be most involved? What trends do you foresee? Will the failure rate go up or down? Will the importance of small business increase or decrease by the year 2030?

CHAPTER 4: PRODUCT/SERVICE DEVELOPMENT

4.1 INTRODUCTION

In Entrepreneur's business, product/service development is the term used to describe the complete process of bringing a new product or service in the market and it's an ongoing practice in which the entire business is looking for opportunities as new products provide growth promise to businesses that allow them to strengthen their market position. The new product development process involves the idea generation, product design, and detail engineering; and also involves market research and marketing analysis. Intense global competition, short product and technology lifecycles, unpredictable consumer buying patterns and possible market stagnation makes new product development a critical activity in most businesses. Hence, this chapter explores the new product development process and at the same time sketch outs the product development procedure in reality where consideration of real life situation and consumer insight are the main concern. Besides, the chapter; considering (often entrepreneur), because of their lack of understanding of intellectual property, ignore important steps that they should have taken to protect these asset; will describe all the important types of intellectual property which have become unique problems to the Patent and Trademark Office.

Chapter Objectives

After completing this chapter, students will be able to:

- Describe the Concept of Product and Services;
- List Product/Service Development Process; and
- Discuss the Intellectual Property Protection.

4.2 The Concept of Product/Service

Many entrepreneurs find it difficult to identify a new product/service or a new market opportunity. To start and expand a small venture, an entrepreneur needs to identify opportunities for domestic and/or international expansion. As the new venture grows and matures a need for different management skills can occur as well as for a new infusion of the entrepreneurial spirit (corporate entrepreneurship). Entrepreneurs like Richard China or Mal Mixon, CEO of Invacare, understands this axiom and effectively manages change by continually adapting organizational culture, structure, procedures, strategic direction, and products in both a domestic and an international orientation.

Organization's success is dependent on customer satisfaction and delight. Customer satisfaction is achieved through the development of product and service, which have all attributes required by the customer. A success product or services do not only have an attractive package design but should be also able to provide robust performance. Thus, product design must be practical enough for production and powerful enough to provide a competitive advantage.

The essence of product design is to satisfy customer and maximizes the value for the customer at minimum cost. The merchandise or service should also be able to meet primary needs and desire of the customer. This may not require development of new merchandise, but an enhancement to existing merchandise or service.

Most companies apparently are introducing a wide variety of smaller, more efficient, and more intelligent products, coupled with a leaner, more efficient approach to operation. The goal is to create products and services by identifying an emerging trend and to match that trend with the right technology and understanding of the purchasing dynamics.

A successful startup depends on its distinctive and compelling proposition. This is how merchandise or services stand out from the competition and are compelling to the young company‘s customers.

The merchandise or service will succeed most if it either eliminates an existing pain or adds significant tangible benefits. It is easier to sell/deliver a new merchandise/service that eliminates a well-known existing pain, as opposed to sell an item or service that doesn’t clearly solve a potential client’s pain.

There also seems to be a popular myth that anyone can be successful by simply working on any given idea or opportunity. This isn’t true! You can’t. Most businessmen are very knowledgeable about the merchandise before they start, since even experienced operators will run into unexpected troubles when they start their new business. Novices generally introduce more problems than they can deal with, which only undercuts their ability to be lean, fast or effective.

4.3 Product/Service Development Process

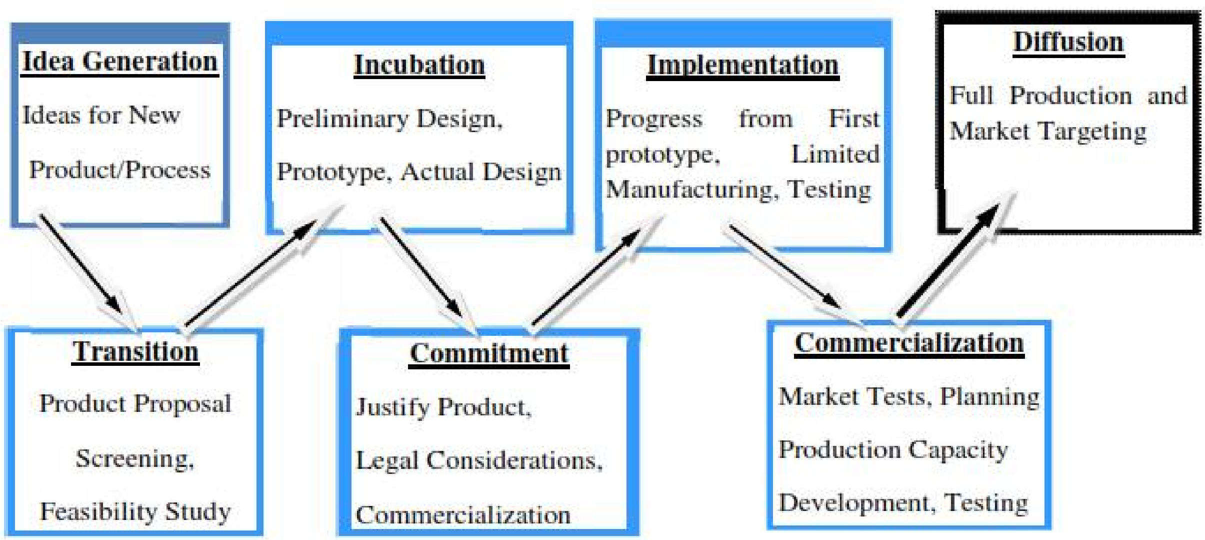
Once the opportunity is selected, and a business model has been designed, the next step is to develop a commercial version of the opportunity which in most cases is either a product or a service. One of the essential characteristics of a successful business is exemplified by its ability to continuously and rapidly develop new or improved versions of existing products that deliver values more than customers expect (*Palgrave, 2019.)*

Product development is the process through which companies react to market signals, respond to changes in customer demand, adopt new technologies, foray into new areas, and ensure continuous growth. It is a core process in achieving strategic objectives, renewal of the company business model and deterring competition from displacing the company from its market position.

Product/service development process is part of the overall new-venture creation process. Even though there are many models that advocate what the product/service generation process should look like, for this purpose we shall adopt four distinct stages.

These stages can be referred to as:

1. Idea Generation
2. Incubation
3. Implementation
4. Diffusion



The various stages of new product development process are explained next:

1. **New Idea Generation**

The new product development process starts with search for ideas. Companies have to encourage any new idea coming. The key to successful domestic and international entrepreneurship is to develop an idea that has a market for the new product/service idea conceived.

Some of the more fruitful sources of ideas for entrepreneurs include consumers, existing products and services, distribution channels, the federal government, and research and development.

2. **Idea Screening**

In the 2nd stage, the purpose is to lessen the number of ideas to few vital/valuable ideas. The ideas should be written down and reviewed each week by an idea committee who should sort the ideas into three groups- ***Promising Ideas, Marginal Ideas, and Rejects***: Each promising idea should be researched by committee member.

3. **Concept Development and Testing**

Attractive ideas must be refined into fast able product concepts since people do not purchase ideas but they buy concepts. Any product idea can be turned into several product concepts. The questions asked probably include:-

- Who will use the product?
- What benefits should the product provide?
- When will people consume the produced?

Concept Testing: - calls for testing product concepts with an appropriate group of target consumers/customers, and then getting the consumers' reactions. At this stage, the concepts can be in words or picture description.

4. **Marketing Strategy Development**

After testing the new product the concerned body must develop a preliminary marketing strategy plan for introducing the new product into the market. The marketing strategy will undergo further refinement in subsequent stages.

The marketing strategy plan consists of three parts: (1) Market size, structure, behavior ;(2) Planned price, distribution strategy, and marketing budget of the 1st year; and (3) Long run sales and profit goals, marketing mix strategy.

5. **Business Analysis**

After management develops product concept and marketing strategy, it can evaluate the proposals' business attractiveness. Management needs to prepare sales, cost and profit projections to determine whether they satisfy the company's objective or not.

Estimated Total Sales: - Management needs to estimate whether sales will be high enough to yield satisfactory profit.

*Estimating Cost and Profits***:** - After sales forecast the management should estimate the expected cost and profit at various levels of sales volume.

The company can use other financial measure to evaluate the merit of a new product proposal. The simplest is ***breakeven analysis***.

Activity
• *You are required to read on Breakeven Analysis and familiar with how it will be applied for the intended purpose.*

6. **Product Development**

If product concept passes the business test, it moves to R&D or engineering to be developed to one or more physical version of the product concept. Its goal is to find a proto type that the consumers/customers see as embodying the key attribute described in the product concept statement,

Scientists must not only design the products' required functional characteristics but also know how to communicate its psychological aspects through physical cues and how will the consumer/customer react to different colors, sizes, weight & other physical cues.

When the prototypes are ready, they must be put through regroups functions and consumer/customer tests. Functional tests are conducted under laboratory & field conditions to make sure that the product performs safely and effectively (Durability, Speed, Cost, etc) Consumer testing can take variety of forms, from bringing consumers/customers into laboratory to giving them samples to use in their homes.

7. **Market Testing**

After management is satisfied with the products' functional and psychological performance, the product is ready to be dressed up with the brand name.

The goals are to test the new product is more authentic consumer/customer settings and to learn how large the market is and how consumers/customers and dealers react to handling, using and repurchasing the actual product.

Most companies know that market testing can yield valuable information about buyers, dealers, marketing program effectiveness, market potential & other matters.

Test Marketing yields several benefits include more reliable forecast of future sale, and pretesting of alternative of future sale.

8. Commercialization

When (Timing):- In commercializing, market entry timing is critical. If the company hears about a competitor nearing the end of its development work, it will face three choices. The 1st choice is ***First Entry***. Under this category, the firm usually enjoys the "first mover advantage" of locking up key distributors & gaining reputation. The 2nd choice goes with ***Late Entry Strategy***- which has three advantages include:-

- The competition will have borne the cost of educating the market;
- The competing product may reveal fault that the late entrant can avoid; and
- The company can learn the size of the market.

The 3rd strategy- ***Parallel Entry-*** can be also chosen by the company to get in the market. The strategy to work, a prospective businessman can take the advantage of opting for the latest technology and production process and operate at higher volume of operation. This leads to reduced production cost and production of quality goods and services. A new businessman can thus provide improved quality goods and services at lower cost and further tap the market with an innovative marketing approach.

Where (Geographical Strategy):- The company must decide whether to launch the new product in a single locality, a region/several regions, in the national/international market.

To Whom (Target-Market-Prospect):- Within the rollout markets, the company must target its distribution and promotion to the best prospect group. Prime prospects for a new consumer/customer's product would ideally have the following characteristics:

- They would be early adapters;
- They would be heavy users;
- They would be Opinion leaders; and
- Could be reached at low cost.

*How (Introductory Markets Strategy)***:-** To sequence and coordinate many actives involved in launching a new product may/can use network-planning techniques such as ***Critical Path Scheduling (CPS).***

Activity:

- *Please read on Critical Path Scheduling technique and try to relate it with the how strategy.*

4.4 Legal and Regulatory Frameworks for Entrepreneurs

Since there are many options that an entrepreneur can choose in setting up an organization, it will be necessary to understand all the advantages and disadvantages of each regarding such issues as liability, taxes, continuity, transferability of interest, costs of setting up, and attractiveness for raising capital. Legal advice for these agreements is necessary to ensure that the most appropriate decisions have been made.

One of the challenges the novice entrepreneur will face as she goes into business understands the regulatory environment which is made up of numerous laws and regulations. To operate as a legal businessperson and protect the business from unnecessary suits and liabilities, the entrepreneur needs to understand the various laws that govern his/her business. Following are the key legal issues for the entrepreneur.

4.5 Intellectual Property Protection/Product/Service Protection

4.5.1 What is Intellectual Property?

Intellectual Property which includes patents, trademarks, copyrights, and trade secrets represents important assets to the entrepreneur and should be understood even before engaging the services of an attorney. Too often entrepreneurs, because of their lack of understanding of intellectual property, ignore important steps that they should have taken to protect these assets.

Intellectual property is a legal definition of ideas, inventions, artistic works and other commercially viable products created out of one's own mental processes. In the same sense that real estate titles establish ownership of tangible items, intellectual property is protected by such legal means as patents, copyrights, and trademark registrations. In order to enjoy the benefits arising from the exclusive ownership of these properties, the entrepreneur needs to protect these assets by the relevant law. This is the reason why' experts strongly recommend that those in creative fields seek protection through official registration of their intellectual properties.

4.5.2 Patents

An entrepreneur who invents a new thing or improves an existing invention needs to get legal protection for her invention through a patent right. A patent is a contract between an inventor and the government in which the government, in exchange for disclosure of the invention, grants the inventor the exclusive right to enjoy the benefits resulting' from the possession of the patent.

- Utility Patent: A utility patent protects any new invention or functional improvements on existing inventions.
- Design Patent: This patent protects the appearance of an object and covers new, original, ornamental, and unobvious designs for articles of manufacture. Like utility patents, design patents provide the inventor with-exclusive right to make, use and/or sell an item having the ornamental appearance protected by the patent. This patent is appropriate when the basic product already exists in the marketplace and is not being improved in function but only in style. These patents are particularly important to companies such as shoe producers and product package design firms that need to protect their ornamental designs.

A patent provides the owner with exclusive rights to hold, transfer, and license the production and sale of a product/process. It is an intellectual property right and It is issued by government to the inventor. This exclusive property right can be granted for a number of years depending on the countries laws and type of property. Patents are property rights that can be sold and transferred, willed as well as licensed and at times used as collateral.

What Can Be Patented Then?

- *Processes*: Methods of production, research, testing, analysis, technologies with new applications.
- *Machines*: Products, instruments, physical objects.
- *Manufactures*: Combinations of physical matter not naturally found.
- *Composition of matter*: Chemical compounds, medicines, etc.

4.5.3 Trademarks

A trademark may be a word, symbol, design, or some combination of such, or it could be a slogan or even a particular sound that identifies the source or sponsorship of certain goods or services.

These are distinctive names, marks, symbols or motto identified with a company's product or service and registered by government offices. Unlike the patent, a trademark can last indefinitely, as long as the mark continues to perform its indicated function. Trademarks unlike patents are periodically renewed unless invalidated by cancellations, abandonment, or other technical registration/renewal issues.

Benefits of a Registered Trademark

- It provides notice to everyone that you have exclusive rights to the use of the mark throughout the territorial limits of the country.
- It entitles you to sue in federal court for trademark infringement, which can result in recovery of profits, damages, and costs.
- It establishes incontestable rights regarding the commercial use of the mark.
- It establishes the right to deposit registration with customs to prevent importation of goods with a similar mark.
- It entitles you to use the notice of registration (®).
- It provides a basis for filing trademark application in foreign countries.

4.5.4 Copyrights

Copyright is a right given to prevent others from printing, copying, or publishing any original works of authorship.

Copyrights provide exclusive rights to creative individuals for the protection of literary or artistic productions. It protects original works of authorship including literary, dramatic, musical, and artistic works, such as poetry, novels, movies, songs, computer software, and architecture. They pertain to intellectual property. Usually copyrights are valid for the life of the inventor plus a few decades.

4.6 The Intellectual Property System in Ethiopia

Ethiopia became a party to the convention establishing the world Intellectual Property Organization (WIPO) in February 1998 right after some time the Country had joined the Nairobi Treaty on the Protection of the Olympic Symbol in 1981. It is a member of the Treaty establishing the Common Market for Eastern and Southern Africa (COMESA) which was formed in 1994, the Partnership Agreement between members of the African, Caribbean and Pacific (ACP) Group of States and the European Union (EU).

The Ethiopian Government established the Ethiopian Intellectual Property Office in the year 2003 containing the understated Objectives:-

- To facilitate the provision of adequate legal protection for and exploitation of intellectual property in the country;

- To collect, organize and disseminate technological information contained in patent documents and encourage its utilization;
- To study, analyze and recommend policies and legislation on intellectual property to the government; and
- To promote knowledge and understanding of intellectual property among the general public;

The existing laws and directives in Ethiopia in the field of Intellectual Property (IP) are the Patent Proclamation and the Implementing Regulation, the Copyright and Related Rights Proclamation and The Trademark Registration Directive.

According to the proclamation in order to be granted a patent, an invention must fulfill three conditions- (1) it must be new- It should never have been published or publicly used before; (2) It should be capable of industrial application- It must be something which can be industrially manufactured or used; and (3) It must be "non-obvious”- It should not be an invention which would have occurred to any specialist working in the relevant field.

The proclamation excludes the following from patentability:-

- Inventions contrary to public order or morality;
- Plant or animal varieties or essentially biological processes for the production of plants or animals; and
- Schemes, rules or methods for playing games or performing commercial and industrial activities and computer programs;
- Discoveries, scientific theories and mathematical methods; and
- Methods for treatment of the human or animal body by surgery or therapy as well as diagnostic methods practiced on the human or animal body.

Rights of a patentee include making, using and exploiting the patented invention in any other way. Any person who wants to use the patented invention has to get the authorization of the owner/inventor. The patentee does not have import monopoly right over the products of the patented invention in Ethiopia.

There are certain limitations of rights of the patentee included in the proclamation such acts done for non-commercial purposes; the use of the patented invention solely for the purposes of scientific research and experimentation; the use of patented articles on aircraft, land vehicles or vessels of other countries which temporarily or accidentally enter in to the air space, territory or waters of Ethiopia; acts in respect of patented articles which have been put on the market in Ethiopia by the owner of the patent or with his/her consent; the use of the patented invention for national security, nutrition, health or for the development of vital sectors of the economy, subject to payment of an equitable remuneration to the patentee; the duration of a patent is 15 years which may be extended for a further period of five years if proof is furnished that the invention is properly worked in Ethiopia.

Trademark Directive is issued in the country in 1986 with the following objectives in that it helps:-

- To centrally deposit trademarks which are used by local and foreign enterprises to distinguish their goods or services;
- To distinguish the products or services of one enterprise from those of other enterprises and prevent consumers from being victims of unfair trade practices;
- To provide information on trademark ownership and right of use when disputes arise between parties;
- To provide required information on trademarks to government and individuals; and
- Protection is granted after publication of cautionary notice;

Copyright is protected on the basis of the copyright and related rights proclamation issued in 2004. The proclamation gives protection to literary, artistic and scientific works which include books, pamphlets, articles, computer programs and other writings; speeches, lectures, addresses, sermons, and other oral works; dramatic, dramatic-musical works, pantomimes, choreographic works, and other works created for stage production; musical works, with or without accompanying words; audiovisual works and sound recordings works of architecture; works of drawing, painting, sculpture, engraving, lithography, tapestry, and other works of fine arts; photographic and cinematographic works; illustrations, maps, plans, sketches, and three dimensional works related to geography, topography, architecture or science; derivative works; and collection of works, collection of mere data (databases) whether readable by machine or other form.

The Proclamation gives protection to:

- Works of authors who are nationals of or have their habitual residence in Ethiopia;
- Works first published in Ethiopia; or works first published in another country and published within thirty days in Ethiopia;

- Audio-visual works whose producer has his headquarter or habitual residence in Ethiopia; and
- Works of architecture erected in Ethiopia and other artistic works incorporated in a building or other structure located in Ethiopia.

The author of a work shall be entitled to protection, for his work upon creation where it is an original work; and written down, recorded, fixed or otherwise reduced to any material form. Quality of the work and the purpose for which the work may have been created is not taken in to consideration.

The rights of performers, producers of phonograms and broadcasting organizations are also protected by law. Copyright is protected for the life of the author plus fifty years. Fifty years for the rights of performers and producers of sound Recordings and 20 years for the rights of broadcasting organizations.

4.7 Chapter Summary

- ☞ Entrepreneurs must always remember that marketing, advertising, or promotional activities are completely worthless, regardless of how clever, expensive, or perfectly targeted they are, unless one simple thing is accomplished--ask for the sale. This is not to say that being a great salesperson, advertising copywriting whiz or a public relations specialist isn't a tremendous asset to your business. However, all of these skills will be for naught if you do not actively ask people to buy what you are selling.
- ☞ Your business is all about your customers, or clients, period. Everything you do in business must be customer focused, including your policies, warranties, payment options, operating hours, presentations, advertising and promotional campaigns and website. In addition, you must know who your customers are inside out and upside down.
- ☞ Laws and regulations exist to protect competition, consumers, people in the workplace, and intellectual property; to allow bankruptcy; and to establish contracts.
- ☞ Too often entrepreneurs, because of their lack of understanding of intellectual property, ignore important steps that they should have taken to protect these assets. This informs will describe all the important types of intellectual property which have become unique problems to the Patent and Trademark Office.
- ☞ Patents, copyrights, and trademarks are legal way to protect intellectual property. A patent grants an inventor the exclusive right to make, use, and sell

- Since all business is regulated by law, the entrepreneur needs to be aware of any regulations that may affect his or her new venture and will need legal advice.

4.8 Questions for Review and Discussions

1. What advice would you give to a business colleague who is about to start a new high-tech firm that has developed a new accessory for computer tablets? Would you recommend that s/he seek a patent immediately?
2. Imagine that you have developed a unique formula for a soft drink that, upon entering a person's mouth, analyzes the drinker's DNA to determine his/her favorite flavor, and then the drink instantly realigns its chemical composition become that flavor. Describe as how you can best protect this trade secret? Will you patent it? Why or why not?
3. What factors should s/he consider in the process of debating whether a patent would be appropriate?
4. What rights does owning a patent protect? How do you get this protection?
5. What tests must an invention pass to receive a patent?
6. What is the difference between a copyright and a trademark? Between a trademark and a brand?

CHAPTER 5: MARKETING

5.1 INTRODUCTION

Business firms and non-profit organizations engage in marketing. Products marketed include goods as well as services, ideas, people, & places. Marketing activities are targeted at market consisting of product purchasers who may be individuals and groups that influence the success of an organization.

The foundation of marketing is exchange. In which one party provides to another party something of value in return for something else of value. In a broad sense, marketing consists of all activities designed to generate or facilitate an exchange intended to satisfy human needs. The concept of market is very important in marketing. The American marketing Association defines a market as "The aggregate demand of the potential buyers for product or a product or services ". Philip Kotler defines "A market as an area of potential exchanges". Thus, a market is a group of buyers and sellers interested in negotiating the terms of purchase/sale for goods or services. The negotiation work may be conducted face-to-face at a certain place or it may be done through other means of communication, such as correspondence, phone, cable, or it may be done through business middlemen, e.g., brokers and commission agents. This chapter discusses about marketing and its basic components.

Chapter Objectives:

By the end of this module, learners will be able to:

- Define marketing concepts.
- Analyze marketing philosophies.
- Describe the role of marketing in achieving the goals of a business enterprise.
- Assist in conducting marketing research.
- Make competitive analysis of the level,
- Implement marketing intelligence in their organization,
- Apply the various marketing mixes and strategies in their businesses.
- Understand and implement selling and customer service skills.

5.2 Meaning and Definitions of Marketing

Marketing can occur any time with one social unit (person or organization) who strives to exchange something of values with another social unit. Thus, the essence of marketing is a transaction or exchange. In this broad sense, marketing consists of activities designed to generate and facilitate exchange intended to satisfy human needs or wants.

Business firms and non-profit organization engaged in marketing. Products marketed include goods as well as services, ideas, people and places. Marketing activities are targeted at market consisting of product purchasers and also individuals and groups that influence the success of an organization. Marketing has been defined in various ways. The definitions that serve our purpose best are as follows:

1. Marketing is a social and managerial process by which an individual or group obtain what they need and want through creating, offering and exchanging of product of values with others (Philip Kotler,2012).
2. Marketing is the total business activity designed to plan, price, promote and distribute want satisfying products to target market to achieve organizational goal (William J.Stanton, 1984).
3. Marketing is the creation and delivery of standard of living to society (Paul. Mazor, 2005).
4. Marketing management is the process of planning and executing, the conception, pricing, promoting and distributing of ideas, goods and services to create an exchange that satisfy individual or group objectives (American marketing Association, 2015).
5. Marketing is the effort to identify and satisfy customers' needs and wants. It involves finding out who your customers are, what they need and want, the prices, the level of competition. It involves the knowledge and all the processes you undertake to sell your product.

The above definitions of marketing reset on the following core concepts: needs, wants and demands; products (Goods, Services and Idea), value, cost and satisfaction: exchange and transaction; Relationship and Networks; market; and marketers and prospects. Marketing answers the following questions:

- Who are my customers?
- What are my customer's needs and wants?

- How can I satisfy my customers'?
- How do I make a profit as I satisfy my customers?

Who are your customers?

Your customers are the people or other businesses that want your products/ services and are willing to pay for them. They include;

- People who are buying from you now.
- People you hope will buy from you in the future.
- People who stopped buying from you but you hope to get them back.

What are my customer's needs and wants?

An important point to note is that customers want to look at different products so that they can choose what they like best. Some customers want a different design and others want high quality and are willing to pay extra for that.

How can I satisfy my customers'?

You need to do everything to find out who your customers are and what they need and want in order to satisfy them improve your sales and make a profit. You need to find out;

- Products/services your customers want.
- Price your customers are willing to pay.
- Location of your business in-order to reach your customers (Place).
- Promotion to use to inform your customers and attract them to buy your products or services.

5.3 Core Concepts of Marketing

5.3.1 Needs, Wants and Demand

A person at any given time has a need. This need arises out of physical or psychological imbalances. Marketing starts with human needs and wants. People need food, air, water, clothing and shelter to survive. Beyond this, people have a strong desire for recreation, education and other services. Let see terms related with this as follow:

- ☞ **Need**: - Human Need is a state of deprivation of some basic satisfaction. People require food, clothing, shelter, safety and belonging and esteem.

- ☞ **Wants**: - Wants are desires for specific satisfiers of needs. Human wants are continually shaped and reshaped by social forces and institutions including churches, schools, families and business cooperation. Eg. A person needs food but wants spaghetti
- ☞ **Demands**: - Demands are wants for specific products that are backed by ability and willingness to buy them. Wants become demand when supported by purchasing power. Companies must therefore measure not only how many people want their product but, more importantly how many would actually be willing and able to buy it.
- ☞ **Product**: - is anything that can be offered to satisfy a need or want. Products broadly classify as tangibility and intangibility features.
- ☞ **Value**: - is the consumer's estimate of the products overall capacity to satisfy his or her needs.
- ☞ According to DeRose, value is "the satisfaction of customer requirement at the lowest cost of acquisition, ownership and use".
- ☞ **Cost**: - is the amount of money that are going to be expended or already incurred to acquire a product.
- ☞ **Exchange**: - is the act of obtaining a desired product from someone by offering something in return.
- ☞ **Transaction**: - is the trade of values between two parties.
- ☞ **Market: -** consists of all the potential customers sharing a particular need or want who might be willing and able to engage in exchange to satisfy their need or want.

5.4 Importance of Marketing

On the average, about 50 cents of each dollar we spend as consumers goes to cover marketing costs. The money pays for designing the products to meet our needs, making products readily available when and where we want them, and informing us about producers. These activities add want satisfying ability or what is called utility, to products.

A customer purchases a product because it provides satisfaction. That something that makes a product capable of satisfying want is its utility. And it is through marketing that much of a products utility is created. Then potential buyers must be informed about the products existence and the benefits it offers through various forms of promotion. The kinds of utility that marketing provides in the process are as follows:

1. Form Utility: Form utility is associated primarily with production- the physical or chemical changes that make a product more valuable. When timber is made into furniture, form utility is created. This is production, not marketing. However, marketing research may aid in decision making regarding product design, color, quantities produced, or some other aspect of a product. All of these things contribute to the product's form utility.

2. Place Utility: Place utility exists when a product is readily accessible to potential customers. So physically moving the products to a store near the customers add to its value.

3. Time Utility: Time utility means having a product available when you want it. Having a product available when we want it is very convenient but it means that the retailer must anticipate our desires and maintain an inventory. Thus, there are costs involved in providing time utility.

4. Information Utility: Information utility is created by informing prospective buyers that a product exists. Unless you know a product exists and where you can get it, the product has no value. Advertising that describes a sales person answering a customer questions about the durability of a product creates information utility. Image utility is a special type of information utility. It is the emotional or psychological values that a person attaches to a product or brand because of its reputation or social standing.

5. Possession Utility: Possession utility is created when a customer buys the product-that is, ownership is transferred to the buyer. Thus, for a person to consume and enjoy the product, a transaction must take place. This occurs when you exchange your money for a product.

Activity 5.1

Think of a recent purchase you made. How did the company provide you with the following utilities?

Form:

____

____

Time:

____

____

Place:

____

____

Ownership:

____

____

5.5 Marketing Philosophies

Large-scale marketing activities in the world did not take shape until the industrial revolution is the latter part of the 1800s. Clearly, marketing activities should be carried out under a well-thought out philosophy of efficient, effective and socially responsible marketing. There are five competing concepts under which organizations can choose to conduct their marketing activities: namely, the production concepts, the product concept, the selling/sales concept, the marketing concept, the societal marketing concept and the Relationship Marketing Concept.

1. The Production Concept

The production concept is one of the oldest concepts in business. The production concept holds that consumers will favor products that are widely available and low in cost. Managers of production-oriented organization concentrate on achieving high production efficiency and wide distribution. The assumption that consumers are primarily interested in product availability and low price holds in at least two situations. The first is where the demand for a product exceeds supply, as in many developing countries. Here consumers are more interested in obtaining the product that in its fine points, and supplies will concentrate on finding ways to increase production. The second situation is where the product's cost is high and has to decrease to expand the market.

2. The Product Concept

Other businesses are guided by the product concept. The product concept holds that consumers will favor those products that offer the most quality, performance or innovative features. Managers in product oriented organization focus their energy on making superior products and improving them over time. Under the concept, mangers assume that buyers admire well-made products and can appraise product quality and performance. In such situation, customers are ready to pay high prices for product extra features. Product-oriented companies often design their products with little or no customer input. They trust that their engineers will know how to design or improve the product.

3. The Selling Concept/Sales Concept

The selling concept (or sales concept) is another common approach. The selling concept holds that consumers, if left alone, will ordinarily not buy enough of the organization product. The organization must therefore undertake an aggressive selling and promotion effort. This concept assumes that consumers typically show buying inertia or resistance and must be coaxed into buying. It also assumes that the company has made available a whole battery of effective selling and promotion tools to stimulate more buying.

The selling concept is practiced more aggressively with unsought goods, those goods that buyers normally do not think of buying, such as insurance, encyclopedia, and funeral plots. Most firms practice the selling concept when they have over capacity. Their aim is to sell what they make rather than make what the market wants. Therefore, people are surprised what they are told that the most important part of marketing is not selling; selling is only the tip of marketing iceberg.

4. The Marketing Concept

The marketing concept is a business philosophy that challenges the three concepts we just discussed. Its central tents crystallized in the mid-1950s.

The marketing concept holds that the key to achieving organizational goals consists of being more effective than competitors in integrating marketing activities toward determining and satisfying the needs and wants of target markets.

The marketing concept has been expressed in many colorful ways:

“Meeting needs profitably”

“Find wants and fills them”

“Love the customers, not the product etc.”

Table 5.1 Selling and Marketing Concept Contrasted

Point of Difference	Selling	Marketing
Starting point	Factory	Market place
Focus	Existing product	Customer need
Means	Selling and promotion	Integrated marketing
End	Profit through Volume	Profit through satisfaction

5. The Societal Marketing Concept

The societal marketing concept holds that the organization should determine the needs, wants and interests of target markets. It should then deliver the desired satisfactions more effectively and efficiently than competitors in a way that maintains or improves the consumers and the society’s well-being. The societal marketing concept holds that the organization’s task is to determine the needs, want, and interests of target markets and to deliver the desired satisfactions more effectively and efficiently than competitors in a way that preserves or enhances the consumers and the society's wellbeing.

The societal marketing concept questions whether the pure marketing concept is adequate in an age of environmental problems, resource shortages, rapid population growth, worldwide economic problems, and neglected social services. It asks if the firm that senses, serves and satisfies individual wants is always doing what's best for consumers and society in the long run. According to the societal marketing concept, the pure marketing concept overlooks possible conflicts between short-run consumer wants and long run consumer welfare.

Table 5.2: Summary of the Evolution of Marketing

Production	▪ Consumers favor products that are available and highly affordable ▪ Improve production and distribution ▪ 'Availability and affordability is what the customer wants'
Product	▪ Consumers favor products that offer the most quality, performance and innovative features ▪ 'A good product will sell itself'
Sales	▪ Consumers will buy products only if the company promotes/ sells these products ▪ 'Creative advertising and selling will overcome consumers' resistance and convince them to buy'
Marketing	▪ Focuses on needs/ wants of target markets and delivering satisfaction better than competitors ▪ 'The consumer is king! Find a need and fill it'
Relationship marketing	▪ Focuses on needs/ wants of target markets and delivering superior value ▪ 'Long-term relationships with customers and other partners lead to success'

6. **Relationship Marketing**

Relationship marketing is the practice of building long term satisfying relations with key parties- customers, suppliers, distributors- in order to retain their long term preferences and business. The ultimate outcome of relationship marketing is the building of a unique company asset called a marketing network. In this case, customer experience rather than customer satisfaction is the most critical component in relationship marketing.

Activity 5.2

Make a statement to describe each of the stages in the evolution of marketing. You may consider the given examples before coming up with your own statements.

1. Production era

a. 'Cut costs. Profits will take care of themselves' 2. Product era a. 'A good product will sell itself' 3. Sales era a. 'Selling is laying the bait for the customer' 4. Marketing era a. 'The customer is King!' 5. Relationship marketing era a. 'Relationship with customers determine our firm's future' 6. Customer Relationship marketing a. Create networking with customers and develop the relationship to the highest level.

5.6 Marketing Information Systems

Every firm must organize the flow of information to its marketing managers. Companies are studying their manager's information needs and designing marketing information system to meet these needs.

A marketing information system consists of people, equipment and procedure to gather, sort, analyze, evaluate and distribute needed timely and accurate information to marketing decision makers. The marketing information system is illustrated as fig 5.1 below:

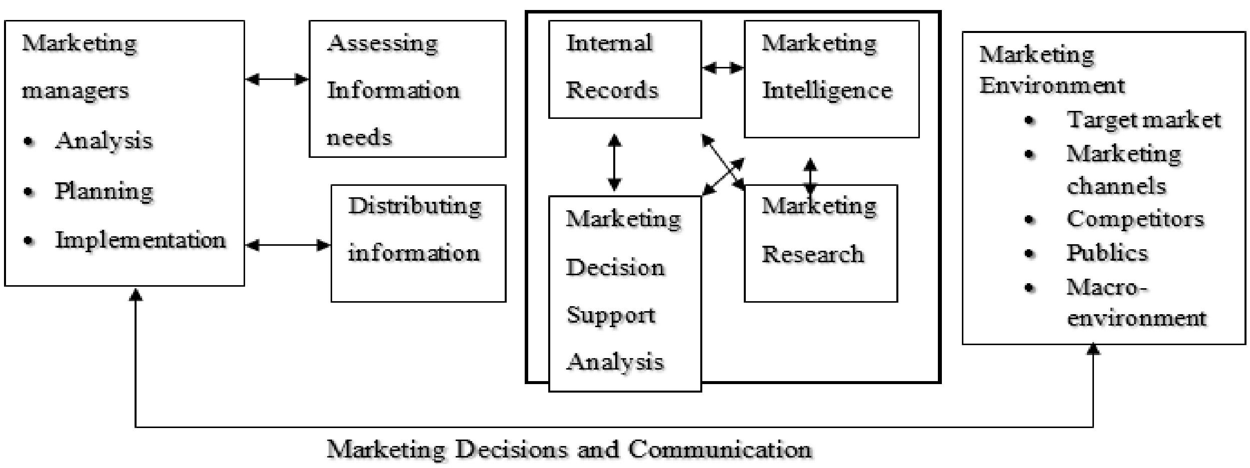


Figure 5.1 Marketing information systems

The marketing managers to carry-out their analysis, planning, implementation, and control responsibilities, they need information about development in the marketing environment. The role of the information system is to assess the manager's information needs, develop the needed information, and distribute the information is a timely fashion to the marketing managers. The needed information is developed through internal company records, marketing intelligence activities, marketing research, and marketing decision support analysis.

5.6.1 Marketing Research

Marketing research is the systematic and objective identification, collection, analysis, and dissemination of information for the purpose of assisting management in decision making related to the identification and solution of problems and opportunities in marketing. Thus, systematic planning is required at all the stages of the marketing research process. The procedures followed at each stage are methodologically sound, well documented, and, as much as possible, planned in advance. It uses the scientific method in that data are collected and analyzed to test prior thinking or hypotheses.

Marketing research is objective. It attempts to provide accurate, impartial information. Accordingly, marketing research involves the identification, collection, analysis, and dissemination of information.

5.6.1.1 The Role (Significance) Of Marketing Research In Decision Making

There are three Functional Roles of Marketing Research. These are:

- Descriptive Function - the gathering and presentation of statements of fact.
- Diagnostic (analytical) Function - The explanation of data.
- Predictive Function - Specification of how to use the descriptive and diagnostic research to predict the result of a planned marketing decision.

5.6.1.2 Marketing Research Components

Marketing researchers deal with many aspects of a market including the following:

- ☞ **Market size**: this deals with the number or value of units sold to a market in a given period.
- ☞ **Market Share**: this one is about a specific corporation's share of the market size out of the whole market of a product or products of the same purpose.
- ☞ **Market penetration**: this is a marketing strategy which is used to know when a company enters/penetrates a market with current products to get better market share by lowering the price of a product.
- ☞ **Brand equity research –** this research is conducted to know how favorably consumers view the brand.
- ☞ **Buyer decision processes research –** this part of marketing research activity is used to determine what motivates people to buy and what decision-making process they use.

5.6.1.3 Customer Satisfaction Research

In this type of research there are different types of research that are used to assess about customers.

- ☞ **Distribution channel audits** - to assess distributors' and retailers' attitudes toward a product, brand, or company.
- ☞ **Marketing effectiveness and analytics** - Building models and measuring results to determine the effectiveness of individual marketing activities.
- ☞ **Mystery Consumer or Mystery shopping –** here the researcher acts as a shopper. This is often used for quality control or for researching competitors' products.
- ☞ **Positioning research –** this research is mostly conducted to answer questions like
  - ✓ How does the target market see the brand relative to competitors?
  - ✓ What does the brand stand for?
- ☞ **Price elasticity testing –** here the objective of the research is to determine how sensitive customers are to price changes
- ☞ **Sales forecasting** - to determine the expected level of sales given the level of demand with respect to other factors like advertising expenditure, sales promotion etc.
- ☞ **Segmentation research** – this type of research helps to determine the demographic, psychographic, and behavioral characteristics of potential buyers.
- ☞ **Test marketing –** this is a small-scale product launch used to determine the likely acceptance of the product when it is introduced into a wider market.

5.6.1.4 Marketing Research Process

Since research is a process which consists of a number of steps to be accomplished in a logical and systematic manner marketing research consists of the following related phases:

Step 1: Define the research purpose or objectives

The following questions help to establish objectives:

- ➢ Where potential customers buy the product?
- ➢ Why they purchase there?
- ➢ What is the size of the market? How much of it can your business capture?
- ➢ How does your business compare with competitors?
- ➢ The impact of promotion on customers.
- ➢ What types of products are desired by potential customers?

Step 2: **Research Design Formulation**

The research design is a ***blueprint*** for conducting the marketing research. More formally, formulating the research design involves the following steps:

- Study period and place determination.
- Qualitative data collection methods.
- Methods of collecting quantitative data (survey, observation, and experimentation).
- Definition of the information needed.
- Questionnaire design.
- Measurement and scaling procedures.
- Sampling process and sample size.
- Plan of data analysis.

Step 3: **Gather at this stage secondary data**,

A data which is originally collected by others for their own purpose, but such data can be used by the researcher when it is relevant to the current study. Secondary data:

- Is less expensive.
- Can be acquired within or outside the venture.
- But, may be out-dated and less valid.

Step 4.Gather Primary Data

Primary data collection techniques can be categorized as;

- Observational techniques-do not involve contact with respondents.
- Focus groups.
- Experimentation-investigates cause and effect relationships.
- Survey techniques- generate data by asking people questions and recording their responses.

The following are examples of survey techniques.

A. Mail questionnaires: The researcher may send the questionnaires to research Participants.

B. Telephone interviews: Using the telephone numbers from telephone directory, the researcher may ask research participant via the telephone.

C. Personal interviews. The researcher may go to the research participants' address and may drop and pick the questionnaire or may interview the research participants.

Step 5: Data Processing and Analysis

Data processing includes the editing, coding, transcription, and verification of data. And data analysis, guided by the plan of data analysis, gives meaning to the data that have been collected. Research results should be evaluated and interpreted in response to the research objectives.

Step 6: **Report Preparations and Presentation**

At the end the research results will be written in a report form and presented to the concerned parties. The report includes:

- The specific research questions identified,
- Describes the research approach,
- The research design,
- The data collection methods, and sampling procedures,
- The data processing and analysis procedures,
- The major findings and suggestions for actions.
- In addition, an oral presentation should be made to management using tables, figures, and graphs to enhance clarity and impact.

5.6.2 Marketing Intelligence

Market intelligence is the systematic process of gathering, analyzing, supplying and applying information (both qualitative and quantitative) about the external market environment. Intelligence is evaluated information. Marketing intelligence is used to determine:

- Current and future market needs,
- Changes in the business environment that may affect the size and nature of the market in the future.
- Environment that may affect the size and nature of the market in the future.

5.6.2.1 The Importance of Marketing Intelligence

Marketing intelligence provides the following benefits;

- Market and customer orientation – promote external focus.
- Identification of new opportunities.
- Smart segmentation.
- Early warning of competitor moves.
- Minimizing investment risks.
- Quicker, more efficient and cost-effective information.

5.6.2.2 Ways to Undertake Marketing Intelligence

i. **Unfocused scanning:** Any information that may be useful is gathered without any specific purpose in mind.

ii. **Semi-focused scanning:** no specific purpose**.** The manager is not in search of particular pieces of information that he/she is actively searching but does narrow the range of media that is scanned. For instance, the manager may focus more on economic and business publications, broadcasts etc. and pay less attention to political, scientific or technological media.

iii. **Informal search: -** limited and unstructured attempt to obtain information for a specific purpose. For example, entering the business of importing frozen fish from a neighbouring country may make informal inquiries as to prices and demand levels of frozen and fresh fish.

iv. **Formal search: -** this is a purposeful search for information in some systematic way.

Marketing intelligence is carried out by the manager him/herself rather than a professional researcher. Scope of the search in this case is likely to be narrow and far less intensive (less rigorous) than marketing research.

5.6.3 Competitive Analysis

Competitive analysis refers to determining the strengths and weaknesses of competitors and designing ways to take opportunities or tackle threats posed by competitors.

5.6.3.1 Uses of Competitive Analysis

Competitive analysis is important for businesses since it has the advantages stated as follow:

- It helps management understand its competitive advantages/ disadvantages relative to competitors.
- It generates understanding of competitors' past, present (and most importantly) future strategies.
- It provides an informed basis to develop strategies to achieve competitive advantage in the future (e.g. how will competitors respond to a new product or pricing strategy?)
- It helps forecast the returns that may be made from future investments.

Competitive analysis is a method of gathering data about competitors from different sources. It should answer the following questions:

- Who are your competitors?
- What customer needs and preferences are you competing to meet?
- What are the similarities and differences between their products/services and yours?
- What are the strengths and weaknesses of each of their products and services?
- How do their prices compared to yours? How are they doing overall?
- How do you plan to compete? Offer better quality services? Lower prices? More support? Easier access to services? How are you uniquely suited to compete with them?

5.6.3.3 Steps of Competitive Analysis

Every business owner should have a complete understanding of the competitive landscape in the market. Competition is defined as any business that provides a similar service or product in the same market, region or industry. A strategic business owner not only knows who its competitor is but also understands the best way to position ahead of its competitor. The following provides a step-by-step process in creating your competitive analysis.

1) Identify your competitors: Determine both local and international competitors. Be sure to define the competitive landscape broadly. Your competitor includes anything that could draw customers away from your business.

2) Gather information about competitors: At this stage you need to know; what markets or market segments your competitors serve; what benefits your competitors offer; why customers buy from them; and as much as possible about their products and/or services, pricing, and promotion strategies.

4) Gathering Information on Competitors

To gather information about your competitor you can go either to your competitors' company site or to the company's Web site (if any) using which you can learn about; promotion strategies by visiting their business site; prices; your competitors' customers; vendors or suppliers, and their employees; trade shows; and publicly available information **-** from Newspapers, magazines, press releases and online publications.

5) Analyzing the Competition

After studying the information you have gathered about each of your competitors, ask yourself these primary questions:

- ☞ How are you going to compete with that company?
- ☞ Is there a particular segment of the market that your competitor has overlooked?
- ☞ Is there a service that customers or clients want that your competitors do not supply?

6) **Develop a pricing:** The last step in the process is to develop a pricing model that represents what you are offering the market and the value you bring to your target buyers. There are many factors that go into designing the appropriate pricing structure so you will need to do some research and evaluate what price levels your market will bear, your cost basis for the development of your product, how much you need to cover overhead and marketing costs and lastly how much profit you think is appropriate for what you are offering. Do not immediately think you have to price your products below your competition, people appreciate the value in your product and set your price accordingly.

The goal of your competitive analysis is to identify and expand upon your competitive advantage. To make your competitive analysis effective, transfer the weaknesses of your competitors into potential strengths for your business.

5.7 The Marketing Mix and Marketing Strategies

5.7.1 The 4 P's Of Marketing/The Marketing Mix

These are marketing variables that the marketing manager can manipulate as controllable variables. They include product, pricing, place (channel) and promotion.

1. Product: refers to goods/services produced for sale, the product /service should relate to the needs and wants of the customers. Some important questions you need to ask yourself include:

a) What products/services do I sell?
b) Why did I decide to sell these products?
c) Do I have the products customers want?
d) Do any of my products not sell well?
e) Do I stock products that do not sell well?

- ✓ Always listen to what your customers like and don't like. When their needs change, change your products and services to satisfy the new needs.
- ✓ Do more market research in order to provide those products or services and increase your sales.
- ✓ If your product is not selling well, think of new ideas like finding new customers.

2. Pricing: refers to the process of setting a price for a product/service. Your prices must be low enough to attract customers to buy and high enough to earn your business a profit. To set your price you need to:

- Know your costs.
- Know how much customers are willing to pay.
- Know your competitors price.
- Know how to make your prices more attractive

3. Place: means the different ways of getting your products or services to your customers. It is also referred to as distribution. If your business is not located near your customers, you must find ways to get your products/services to where it is easy for customers to buy. You can distribute your products to your customers through:

- Selling directly to the consumers of the products.
- Retail distribution and wholesale distribution.

4. Promotion: Refers informing your customers of your products and services and attracting them to buy them. Promotion includes advertising, sales promotion, publicity (non-paid promotion) and personal selling. Use advertising to make customers more interested in buying your products or services. Some useful ways of advertising include signs, boards, posters, handouts, business cards, pricelists, photos and newspapers.

You can use sales promotion (short term incentives) to make customers buy more when they come to your business, you could also:

- Ensure you maintain attractive displays.
- Let customers try new products.
- Have competitions.
- Give demonstrations.
- Sell complementary products (products that go together)

5.7.2 What Is Marketing Strategy?

A marketing strategy is a process that can allow an organization to concentrate its limited resources on the greatest opportunities to increase sales and achieve a sustainable competitive advantage.

Marketing strategy is a method of focusing an organization's energies and resources on a course of action which can lead to increased sales and dominance of a targeted market.

A marketing strategy combines product development, promotion, distribution, pricing, relationship management and other elements; identifies the firm's marketing goals, and explains how they will be achieved, ideally within a stated timeframe. Marketing strategy determines the choice of target market segments, positioning, marketing mix, and allocation of resources. It is effective when it is an integral component of the overall firm strategy, defining how the organization will successfully engage customers, prospects, and competitors in the market arena.

1. Pricing Strategy

Price is the value placed on what is exchanged. Something of value is exchanged for satisfaction and utility, includes tangible (functional) and intangible (prestige) factors. It can even be barter. Price is often the only element the marketer can change quickly in response to demand shifts.

It relates directly to total revenue   TR = Price * Quantity

Profit = TR – TC

Where, TR=Total Revenue, TC=Total Cost

Pricing strategies are subject to incredibly complex environmental and competitive forces. A company sets no single price, but rather a pricing structure that covers different items in its line. This pricing structure changes through time as products pass through their life cycles.

To come up with this situations marketers use dynamic pricing strategies. The following are some of pricing strategies mostly applicable in the real world scenario.

i) **Price Skimming**: this is a type of marketing strategy that firms use by charging the highest possible price that buyers who most desire the product will pay. It attracts a market segment that is more interested in quality, status, uniqueness etc. In this case, consumers' demand must be inelastic.

ii) **Penetration Pricing:** In this strategy, prices of products are reduced compared to competitors' price for the same product to penetrate into markets and to increase sales. However, the quality of the product should not be lower as compared to other competitors' product. It should be again noted that the cost of production should be lower to the extent that can enable the firm to get the desired profit. This is appropriate when the demand is elastic.

iii) **Cost-plus pricing:** Any amount that is above unit cost may be considered.

iv) **Mark-up pricing**: A certain percentage of the selling price is added to unit cost.

v) **Competition Oriented Pricing:** Considers competitors prices primarily; but the market type matters.

vi) **Odd-even pricing**: This is Psychological pricing method based on the belief that certain prices or price ranges are more appealing to buyers. This method involves setting a price in odd numbers (just under round even numbers) such as $49.95 instead of $50.00. Although not supported by any research findings, its proponents claim that the consumers see a $49.95 price as 'just in the price range of $40'rather than in the $50.

2. Promotion Strategies

Promotion is the communication of the company and its products to customers. Promotional strategy is choosing a target market and formulating the most appropriate promotion mix to influence it. An organization's promotional strategy can consist:

i) **Advertising**: It is any paid form of non-personal, one-way, mass communication about an organization, good, service, or idea by an identified sponsor.

ii) **Personal selling**: This is the two-way flow of communication between a buyer and seller, often in a face to face encounter, designed to influence a person's or group's purchase decision.

iii) **Public relations:** Public relation is a form of communication that seeks to change the perceptions of customers, shareholders, suppliers, employees and other publics about a company and its products.

iv) **Sales promotion**: This promotion type involves short term incentives of value such as discounts, free samples, and prizes to be offered to arouse interest of customers in buying the good/service. Businesses may use one of the above promotional mix elements to arouse the interest of customers and make them take action by informing, persuading and reminding about the goods and services that they provide to the market.

3. Distribution Strategies

A successful product or service means nothing unless the benefit of such a service can be communicated clearly to the target market. For product-focused companies, establishing the most appropriate distribution strategies is a major key to success, defined as maximizing sales and profits. Unfortunately, many of these companies often fail to establish or maintain the most effective distribution strategies. Problems that researchers identified include:

- Unwillingness to establish different distribution channels for different products,
- Fear of utilizing multiple channels, especially including direct or semi-direct sales, due to concerns about erosion of distributor loyalty or inter-channel cannibalization
- Failure to periodically re-visit and update distribution strategies.
- Lack of creativity, and
- Resistance to change.

As can be noted from the above points marketing channels are the most important actors for the effective and efficient distribution of products.

Marketing Channels are individuals/organizations involved in the process of making the product available for use or consumption by consumers. Channels are used to improve exchange efficiency. It is divided into Direct and Indirect channels.

- **Direct channels:** In this type of channel, producers and end users directly interact.
- **Indirect channels:** In this type of channel intermediaries are inserted between seller and buyer. Intermediaries include Merchant Wholesalers, retailers, dealers, agents, brokers; and manufacturer's branches and offices.

Decisions about marketing channels, which help producers deliver goods and services to their target markets, are among the most critical tasks facing management-because the channels that are chosen intimately affect all of the other marketing decisions. For example, the company's pricing depends on whether it uses a direct channel, discount merchants, or high-quality boutiques. Also, the firm's sales force and advertising decisions depend on how much training and motivation its dealers need.

The following factors should be considered to select the best channel under the condition of using best distribution strategy.

- ***Company Factors***: financial, human and technological capabilities of a company to do its business activities.
- ***Market Characteristics***: Geography, market density, market size, target market
- ***Product Attributes***: perishability, value and sophistication of the product
- ***Environmental Forces***: those forces that affect the business like competition, technology and culture.

5.8 Selling and of Customer Service

Many employees have unclear understanding of what customer service really is. There are indications everywhere that there are customer service problems that demand solutions. How service providers do their jobs, how fast and accurately they process paper works, how successfully they pursue accounts, and how effective they are in taking the next step to develop customer loyalty, will determine an organization's success in serving customers. It is because of these reasons that customer service delivery improvement programs fail in some instances.

Customer service is what happens between the customer determining his/her needs and receiving the desired benefits. However, most service providers do not appropriately understand what service delivery really means. For this reason, many organizations fail to improve the level of their customer service delivery.

5.8.1 The Concept of Service

Service refers to any activity undertaken to fulfil customer’s needs. It is any act or performance that one party can offer to another that is essentially intangible and does not result in the ownership of anything. Its production may or may not be tied to a physical product. Distinctive features of services include intangibility, inseparability, variability, and perishability as opposed to goods.

The feature of intangibility shows that pure services cannot be defined in terms of the physical dimensions; or the customer cannot see or feel them before purchase. The concept of inseparability, on the other hand, refers that production and consumption of services are inseparable; the 'sale' occurs just before both.

There are also features of variability and perishability associated in service. Services are highly variable, because they depend on who provides them, and when and where they are provided. In addition to this, services are produced and consumed at the same point, and are totally perishable right after use. Service cannot be reproduced as a concert object and it can vary from one moment to the next. Based on this concept, service is characterized as; situational, difficult to measure, subjective and influenced by the service provider.

Service is situational in the sense that what is good for one customer one day may be perceived differently by the same customer another day. There is also difficulty associated in measurement of service. This is because the higher one sets expectation by delivering service, the more the customers expect the next time they deal with the service provider.

Service is also subjective in the sense that an acceptable service for one customer may not be equally or totally acceptable by another customer. Finally, service is influenced by the service provider. If the service provider sets expectations effectively, the customer will probably be satisfied.

5.8.2 The Concept of Customer

Customer is a person or organization that buys a product or service either for use or for resale. Customers can be internal (e.g. member of the organization) or external (customers coming from outside). A thorough understanding of the concept of customer service enables organizations to provide quality service by using proper service management approaches.

5.8.3 Strategic Activities needed for Quality Customer Service Delivery

Organizations should identify important strategic activities to ensure consistent, efficient and excellent customer service delivery using continuous improvement philosophy. Especially, the following specific areas should be considered:

1. Establishing a clear customer service strategy.
2. Ensuring that correct people are in place, with the correct skills to deliver outstanding personal service.
3. Establishing clear material service delivery processes.
4. Improving in terms of process improvement, quality monitoring and recovery continuously.
5. Participatory Management.

5.8.4 Customer Handling and Satisfaction

Customer handling and satisfaction is a key for successful organizations. Managers and employees should work hand-in-hand to improve their service delivery programs. Existing customers must be satisfied with the existing service. Existing customers are also means of potential customers. What is expected from successful service providers in this regard are the following.

Poor service/defective service is the causes of loss and bankruptcy for many organizations. Many organizations, especially business organizations worried about the reduction of sales or profitability due to lost customers/ or gradual reduction of customers. Organizations invest huge cost to increase market share by using advertisement or different sales promotion techniques. But the first most important principle here is not losing a single customer.

Retaining existing customers, however, requires systematic handling. You have to make customer satisfaction your religion. Understand the importance of satisfying existing customers. Usually, organizations tried to increase sales by a much larger percentage than what they had planned, because of sales lost due to defecting customers.

In addition to retaining existing customers, originations should also strive to increase the number of customers. Organizations could possibly increase their market share by getting new customers. Attracting new customers is directly related to keeping existing customers satisfied.

The consequence of poor customer handling, therefore, is losing existing customers. Again, organizations invest huge resources to acquire new customers, who are later lost, resulting in a total loss of investment. There is unnecessarily spending money on advertising and marketing to get customers. Customer retention and satisfaction comes not from words, but from putting time, effort, and money to satisfy customers. Establish an information system to track lost customers and record your day-to-day progress. Also take into account that the major reasons to lose customers are:

- Poor service,
- Poor quality and
- Rude behaviour.

There are organizations that tend to lose a very high percentage of their customers every year. The majority of these customers are not even aware of this phenomenon. But we have to consider the fact that when we lose a customer, we don’t loose revenue and profits for just one year, but for a number of years, that is for the lifetime of the customer. Organizations should make the effort to retain every single customer. It is understandable when you lose a customer because of reasons that are beyond your control, but unpardonable when you lose one for poor service and an uncaring attitude towards the customer.

5.8.4.1 Considering Customers as an Invaluable Asset

The value of one customer is infinite, and you cannot possibly calculate it. This includes, sales to him in his lifetime as well as to customers he generates for you through word of mouth. This means, your most precious asset is your customer. We think of the immediate profit and ignore the future profits expected over the lifetime of the customer.

5.8.4.2 Reducing Customer Complaints

Every single complaint should be treated as an opportunity to improve the quality of your products and services. A complaining customer is a very fair person. Turn customer discontent to your advantage. Consider also the following research findings about customer satisfaction:

- 91% of customers who have major complaints decide they will never come back. But if the complaint is resolved quickly, 82% of them will return.
- Quick complaint resolution drops customer defection rate from 91% to 18%. It is better to have a complaining customer than no customer at all. It pays to resolve complaints quickly.
- There is no investment like investment in customer satisfaction.
- Treat the cost of satisfying a customer as an investment rather than as an expense. You will get unmatched returns through referrals, repeat purchases decreased operational costs and increased profits.
- In the customer's benefit lies our benefit.

Therefore, organizations should start tracking the cost of customer dissatisfaction to convince employees and management about the importance of keeping customers satisfied. Your competitive advantage will lie in retaining the customer longer than your competition. Because of a few disloyal customers, you cannot lose your faith in all your customers.

5.8.4.3 Place Yourself in The Customer's Shoes

You have the right to choose your customers but not the luxury to compromise on your level of service. Get rid of the unwanted customer but do it with tact. Part with the unwanted customer with a smile and a handshake. Place yourself in the customer's shoes. 'Do unto your customer as you would have done unto you'.

Activity 5.3

The following list consists of some MARKETING MYTHS. Tick the myths you thought about marketing before reading this section? Add some new myths you might have discovered (you may browse the Internet for more myths).

- Marketing and selling are synonymous,
- The job of marketing is to develop good advertisements,
- Marketing is pushing the product to the customers,
- Marketing is transaction-oriented than relationship-oriented,
- Marketing is a short-term business strategy,
- Marketing is an independent function of a business,
- Marketing is part of selling.

5.9 Chapter Summary

Business firms and non-profit organization engage in marketing. Products marketed include goods as well as services, ideas, people and places. Marketing activities are targeted at markets, consisting of product purchases and also individuals and groups that influence the success of an organization. The foundation of marketing is exchange, in which one party provides to another party something of value is return for something else of value. In a broad sense, marketing consists of all activities designed to generate or facilitate an exchange intended to satisfy human needs. In a business context, marketing is the total system of business activities designed to plan, price, promote, and distribute want satisfying products to target markets to achieve organizational objectives. Also, it is a social and managerial process by which an individual obtain what they need and want through creating, offering and exchanging of product of values with other.

A business philosophy called the marketing concept developed to aid companies with supply capabilities that exceed consumer demand. According to a marketing concept, a firm is best able to achieve its performance objectives by adopting a customer orientation and coordinating all of its marketing activities. More recently, the societal marketing concept has been proposed as a philosophy by which a company can satisfy its customers and at the same thing fulfil its social responsibility.

Marketing activities have undergone a series of successive stages. The evolution starts with a production orientation, passed through a product orientation followed by a sales orientation, then to marketing orientation and societal orientation stage. The main difference between marketing and selling is that selling emphasis is on the product; in marketing the emphasis is on customer's wants.

5.10 Review Questions

1. Define the term marketing? And explain the core concepts of marketing?
2. Identify and explain briefly the marketing philosophies?
3. Identify at least three distinctions between marketing and selling.
4. Discuss the importance of marketing Intelligence?
5. Discuss how to reduce customer dissatisfaction.

PRACTICAL ACTIVITY ON MARKETING

Activity name: Market simulation activity

Objective(s) of activity:

Participant will get to experience marketing through a live simulation.

At the end of the activity participants will be able to;

- Experience the interplay of factors influencing the market such as price, product, place and promotion
- Realize the difficulties new entrepreneurs have when entering the market place
- Observe the impact of different marketing strategies on the capturing of market share

Materials/ Handouts needed:

- Materials found in the classroom e.g. pens, mobile phones, bag, shoes etc.
- Pen
- Paper

Instructions:

1. Divide participants into buyers and sellers.
2. In the first round, four sellers set up shops in demarcated areas of the training room and sell their allocated products to the buyers at a set selling price.
3. The buyers are divided into high, middle and low-income groups. Each income group is given a limit on how much it can spend to purchase products.

Reflection questions:

- What are your thoughts on your experience of the exercise?
- What have you learnt about marketing and competition analysis during the exercise?
- What lessons can you apply in your business today?

Extension/ Simplification options:

1. One of the, buyers in this round is an entrepreneur who wants to start a business.
2. In the second round, he/she (entrepreneur) uses the opportunity to study the competition and potential customers and develop a marketing strategy that will ensure a profitable market share is captured.
3. In the second round the fifth seller enters the market and applies his/her marketing strategy.
4. The second round is less restrictive than the first round as selling prices, demarcated areas and products are not allocated to sellers. The fifth seller's success depends on the strategy applied, his/her selling ability and how the other competitors respond to their market shares being encroached upon .The role of the fifth seller is similar to that of the participants, after the training, as they are new entrepreneurs about to enter an existing market.

CHAPTER 6: BUSINESS FINANCING

6.1 INTRODUCTION

Sourcing money may be done for a variety of reasons. Traditional areas of need may be for capital asset acquisition- new machinery or the construction of a new building. The development of new products can be costly but capital may be required. Such developments are financed internally, whereas capital for the acquisition of machinery may come from external sources. In this day and age of light liquidity, many organizations have to look for short term capital in the way of loans, working capital etc., in order to provide a cash flow cushion. This chapter of the module discusses about financing of firms.

Chapter Objectives:

By the end of this module, trainees will be able to:

- Learn about the cost of starting an enterprise.
- Know the different sources of finance to start a business venture.
- Understand lease financing.
- Learn micro finances.
- Understand crowd funding.
- Know micro financing.
- Learn about traditional financing in Ethiopia.

6.2 Financial Requirements

All businesses need money to finance a host of different requirements. In looking at the types and adequacy of funds available, it is important to match the use of the funds with appropriate funding methods.

1) **Permanent Capital**

The permanent capital base of a small firm usually comes from equity investment in shares in a limited company or share company, or personal loans to form partners or to invest in sole proprietorship. It is used to finance the start - up costs of an enterprise, or major developments and expansions in its life - cycle. It may be required for a significant innovation, such as a new product development.

Equity from private investors may also be sought to take a small firm into the medium or large size category or as an exit route for the original investors. Ideally, permanent capital is only serviced when the firm can afford it; investment in equity is rewarded by dividends from profits, or a capital gain when shares are sold. It is not therefore a continual drain from the cash flow of a company, such as a loan, which needs interest and capital repayments on a regular basis. Equity capital usually provides a stake in the ownership of the business, and therefore the investor accepts some element of risk in that returns are not automatic, but only made when the small firm has generated surpluses.

2) Working Capital

It is short-term finance. Most small firms need working capital to bridge the gap between when they get paid, and when they have to pay their suppliers and their overhead costs. Requirements for this kind of short-term finance will vary considerably by business type. For example, a manufacturer or small firm selling to other businesses will have to offer credit terms, and the resulting debtors will need to be financed; the faster the growth, the more the debtors, and the larger the financial requirement.

A retailer, a restaurant, a public house, or other types of outlet selling directly to the public will often collect cash with the sale, however, earns the cash flow will be advantageous. In some cases, this will be sufficient to finance the start - up of a small firm, so that suppliers are effectively financing the business.

However, even these types of business may need working capital to fund temporary loses, caused by seasonal fluctuations, or to cope with prepayment of expenses such as rent payable in advance. Although short-term finance is normally used to fund the trading of a business, it is also sometimes needed to purchase assets, which are short-lived such as company vehicles, which may be changed every 4 or 5 years.

3) Asset Finance

It is medium to long term finance. The purchase of tangible assets is usually financed on a longer-term basis, from 3 to 10 years, or more depending on the useful life of the asset. Plant, machinery, equipment, fixtures, and fittings, company vehicles and buildings may all be financed by medium or long-term loans from a variety of lending bodies.

6.3 Sources of Financing

Financial resources are essential for business, but particular requirements change as an enterprise grows. Obtaining those resources in the amount needed and at the time needed can be difficult for entrepreneurial ventures because they are generally considered more risky than established enterprises. As we shall see, financing means more than merely obtaining money; it is very much a process of managing assets wisely to use capital efficiently.

Managing assets effectively is crucial because underwriting assets creates liabilities that, if uncontrolled, can devastate a business. Cash is the most important asset to manage, and to generate cash, business must generate sales. In order to generate sales, most businesses must have inventory and facilities. Service enterprises need offices and staff, and manufacturers face more extensive requirements, including plant and equipment. Assets management for the start-up entrepreneur is a matter of determining what is needed to support sales, and then gaining access to those assets at the optimum cost. The term "gaining access" is used because there are alternatives other than a cash purchase of assets. Equipment can be leased, for example, and office furniture can be rented. Manufactured products initially can be subcontracted rather than made, thereby avoiding the expense of procuring materials, equipment, and plant facilities. Entrepreneurs, therefore, have choices about what assets to obtain, when they must be obtained, and how to gain access to them.

The critical issue in financing is to assure sufficient cash flow for operations, as well as to plan financing that coincides with changes in the enterprise. Businesses obtain cash through two general sources, equity or debt, and both can be obtained from literally hundreds of different sources. The various sources of finance may be broadly be classified as follows:

6.3.1 Internal Sources (Equity capital)

Owner's capital or owner's equity represents the personal investment of the owner(s) in a business and it is sometimes called risk capital because these investors assume the primary risk of losing their funds if the business fails. However, if the venture succeeds, they also share in the benefit.

Sources of Equity Capital

1. ***Personal saving:*** The first place entrepreneurs should take for startup money is in their own pockets. As a general rule, entrepreneurs should provide at least half of the start- up funds in the form of equity capital.
2. ***Friends and relatives:*** After emptying their own pockets, entrepreneurs should turn to friends and relatives who might be willing to invest in the business. The entrepreneur is expected to describe the opportunities and threats of the business.
3. ***Partners:*** An entrepreneur can choose to take on a partner to expand the capital formation of the proposed business.
4. ***Public stock sale (going public):*** In some case, entrepreneurs can go public by selling share of stock in their corporation to outsiders. This is an effective method of raising large amounts of capital.
5. ***Angels:*** These are private investors (or angles) who are wealthy individuals, often entrepreneurs, who invest in the startup business in exchange for equity stake in these businesses.
6. ***Venture capital companies*****:** Are private, for profit organizations that purchase equity positions in young business expecting high return and high growth potential opportunity. They provide start -up capital, development funds or expansion funds

Comparison of Angles and Venture Capitalist

Angels	**Venture Capitalists (VCs)**
• Individuals who wish to assist others in their business venture, • Usually found through networks, • Reasonable expectations on equity position and ROI, • Often passive, but realistic perspective about business venture, Exit strategy is important,	• Finance, small scale new technology and any risky idea. • Funds are more specialized versus homogeneous • High expectations of equity position and ROI,

ADDITIONAL REMARKS ON SAVING

WHAT ARE SAVINGS?

Savings are money or other assets kept over a period of time, usually not to be consumed immediately but in the future. Savings can be kept in a bank or any other safe place where there is no risk of loss, spending, or making profit.

Savings can be done through

- **Small but regular deposits –** this happen when someone has decided to sacrifice current consumption (use of assets, e.g. of money and goods) in order to increase the availability of assets for future consumption. It therefore involves postponing expenditures in order to accumulate a sizeable amount of resources for future use.
- **Automatic deductions from salaries, wages or income** - this type of saving is not voluntary. It is a system used by most employers under the labour law.

Advantage of saving

- To provide for specific needs in the future
- To have access to monetary or other assets whenever needed
- To ensure financial independence
- To make one's own resources inaccessible for others without one's approval
- To safely store surplus
- To acquire skills for proper money management and self-discipline
- To qualify for certain types of loans

Investments

These are monetary assets purchased in the hope that they will generate income, reduce costs, or appreciate in the future. In short, investment means the use of money to make more profit in the future.

Personal Budget

A **personal budget** is a finance plan that allocates future personal income towards expenses**,** Savings and debt repayment.

How to prepare a personal budget for saving purposes?

Identify your sources of income and how much you earn from each source

- Add up to get total income per month.
- Track all your expenses daily, weekly or monthly
- Then divide them by categories
- For daily expenses, multiply each by four to get monthly expenses and add them to get a monthly total for daily expenses
- Take the total income per month and subtract the monthly total for daily expenses. The difference can be taken as savings. If the difference is negative or the expenses exceed the income then:
    - o Cut back your expenses
    - o Adjust your expenses

6.3.2 External Sources (Debt capital)

Borrowed capital or debt capital is the external financing that small business owner has borrowed and must repay with interest. There are different sources as discussed here below:

I) **Commercial banks**: Commercial banks are by far the most frequently used source for short term debt by the entrepreneur. In most cases, commercial banks give short term loans (repayable within one year or less) and medium term loan (maturing in above one year but less than five years), long term loans (maturing in more than five years).

To secure a bank loan, an entrepreneur typically will have to answer a number of questions, together with descriptive commentaries.

- ☞ What do you plan to do with the money?
- ☞ When do you need it?
- ☞ How much do you need?
- ☞ For how long do you need it?
- ☞ How will you repay the loan?

Bank Lending Decision:-The small business owner needs to be aware of the criteria bankers use in evaluating the credit worthiness of loan applications. Most bankers refer to the five C's of credit in making lending decision. The five C's are capital, capacity, collateral, character, and conditions.

1. ***Capital:*** A small business must have a stable capital base before a bank will grant a loan.
2. ***Capacity:*** The bank must be convinced of the firm's ability to meet its regular financial obligations and to repay the bank loan.
3. ***Collateral:*** The collateral includes any assets the owner pledges to the bank as security for repayment of the loan.
4. ***Character:*** Before approving a loan to a small business, the banker must be satisfied with the owner's character. The evaluation of character frequently is based on intangible factors such as honesty, competence, willingness to negotiate with the bank.
5. ***Conditions:*** The conditions surrounding a loan request also affect the owner's chance of receiving funds. Banks consider the factors relating to the business operation such as potential growth in the market, competition, location, and loan purpose. Another important condition influencing the banker's decision is the shape of the overall economy including interest rate levels, inflation rate, and demand for money.

The higher a small business scores on these five Cs, the greater its chance will be of receiving a loan. In the Ethiopian context, collateral is very critical.

II) Micro Finances: provide financial services mainly to the poor ,micro and small enterprises(detail to be discussed later in part 6.7)

III) Trade Credit: It is credit given by suppliers who sell goods on account. This credit is reflected on the entrepreneur's balance sheet as account payable and in most cases it must be paid in 30 to 90 or more days.

IV) Equipment Suppliers: Most equipment vendors encourage business owners to purchase their equipment by offering to finance the purchase.

V) Account receivable financing: It is a short term financing that involves either the pledge of receivables as collateral for a loan.

VI) Credit unions: Credit unions are non-profit cooperatives that promote savings and provide credit to their members. But credit unions do not make loans to just any one; to qualify for a loan an entrepreneur must be a member.

VII) Bonds: A bond is a long term contract in which the issuer, who is the borrower, agrees to make principal and interest payments on specific date to the holder of the bond. Bonds have always been a popular source of debt financing for large companies in the western world.

VIII) Traditional Sources of Finance: "Idir", "equib" (detail to be discussed later in 6.5)

LOCAL CASE

THE STORY OF ABDELA'S FAMILY

Abdella and his wife Fatuma live in a small rural trading center near to Dessie. Abdella is a tailor who has had a successful tailoring business ever since he learnt the skill from his father at his young age. His wife Fatuma raises vegetables that she sells at the weekly market. Part of the produce is consumed by the family, which includes three sons and two daughters.

Their oldest son Abdi has recently returned home to start a new life, after his contract work in a factory at Kombolcha town. Abdi appealed to his parents for a loan to start up a mini fast food selling in the trading center. He decided on this business because he was fairly knowledgeable about food business, having done some part-time work in a restaurant while he was in Kombolcha. Abdi also observed that there were no many fast food providers nearby. He lacked his father's tailoring skills because he went to work in Kombolcha when he was young. Abdi's wife, Amina grew up in town and she does not have the knowledge of vegetable growing like her mother-in law Fatuma.

Abdella and his wife are reluctant to lend their son the fifty thousand birr he requested because they noticed recently that their sewing machines, which have served them well for many years, is no longer working properly. They have taken it to a repairer in Kombolcha several times and recently were told that once it stopped working it might not be fixed. Therefore, Abdella and his wife do not want to withdraw money from their savings account at the Commercial Bank as they need it to buy new sewing machines. Moreover, they want to keep some money for emergency cases that. They know that their son Abdi spent the terminal benefits he collected from the factory instead of investing it in some business. So they wondered why they should support their son's business idea. However, Abdi is now hanging around town unemployed. As a result, Abdella and his wife have to provide food and lodging for Abdi, Amina and their two children until they get earning for themselves.

Abdi recently attended a training course on business skills and he assures his parents that he has learnt some skills that help him manage the business successfully. Among others, one thing that he learnt is to think about all the family's needs for capital than just the new business activity planned to be started. And he tells his parents that he would like to discuss with them before they make final decision on his loan request.

Instruction to the instructor:

Break the participants into small groups of four persons each. Allow each group about 30 minutes to decide what the family should do. At the end of the given time, have all the participants come back together into a large group.

A spokesperson for each small group should tell the large group what they decided, and why. After each presentation, discuss the decision taken, answering all these questions:

- What are the advantages of the decision taken?
- What are the disadvantages?
- Does this decision expose the family to a lot of risks?
- Are there any alternatives that would be less risky?

Some of the identified alternatives might be loans from moneylenders, a bank, NGO,MFI or relatives savings associations or personal savings.

Next Step:

Tell the participants that they are going to discuss the advantages and disadvantages of the different sources of funds that they would consider for starting and operating their business using a matrix. This should help them come out with the less risky source.

- Tell participants to go and collect local materials
- Ask one participant to draw a table similar to the matrix below. Solicit for the different sources of funds from the participants.
- Place the local material in the table according to the rate that each source of finance according the criteria set on the columns
- Add up the score in the row and place the ratting and select the one with highest score to be the best financing.

Example:

	Interest	Accessibility	Repayment period	Score	Rating
Borrowing from relatives					
Loan from Banks					
Loan from MFIs					
Loan from VSLA					
Personal Saving					
Business people					

4=Excellent 3=Very good 2=Average 1=Fair 0=Poor

(VSLA=Village Saving and Loan Associations),MFIs=Micro Finance Institutions)

The facilitator should ensure that the points below are covered.

- Loans from moneylenders usually have high interest. This makes it more difficult to earn a profit from the activity.
- Banks may have a lower interest rate, but have a lot of requirements that poor people have trouble fulfilling.

- (Funding from MFI's should be emphasized with a clear explanation on the common basic requirements from these institutions;
    - Interest
    - Repayment frequency
    - Meetings
    - Group securities)
- Loans from all sources must be repaid. If the business fails, the borrower will lose some of his assets. In the case of Banks, a loan in default must be repaid by the other members of the group.
- Loans from a revolving fund.
- Using own savings is less risky than using loans.

Processing and Generalizing: The process of the financial plan preparation and its usefulness for entrepreneurial activities are being reviewed and discussed

6.4 Lease Financing

Lease financing is one of the important sources of medium- and long-term financing where the owner of an asset gives another person, the right to use that asset against periodical payments. The owner of the asset is known as lessor and the user is called lessee. The periodical payment made by the lessee to the lessor is known as lease rental. Under lease financing, lessee is given the right to use the asset but the ownership lies with the lessor and at the end of the lease contract, the asset is returned to the lessor or an option is given to the lessee either to purchase the asset or to renew the lease agreement.

6.4.1 Types of Lease

Depending upon the transfer of risk and rewards to the lessee, the period of lease and the number of parties to the transaction, lease financing can be classified into two categories. Finance lease and operating lease.

1) Finance Lease

It is the lease where the lessor transfers substantially all the risks and rewards of ownership of assets to the lessee for lease rentals. In other words, it puts the lessee in the same condition as he/she would have been if he/she had purchased the asset. Finance lease has two phases: The first one is called primary period. This is non-cancellable period and in this period, the lessor recovers his total investment through lease rental. The primary period may last for indefinite period of time. The lease rental for the secondary period is much smaller than that of primary period.

From the above discussion, following features can be derived for finance lease:

- A finance lease is a device that gives the lessee a right to use an asset.
- The lease rental charged by the lessor during the primary period of lease is sufficient to recover his/her investment.
- The lease rental for the secondary period is much smaller. This is often known as peppercorn rental.
- Lessee is responsible for the maintenance of asset.
- No asset-based risk and rewards are taken by lessor.
- Such type of lease is non-cancellable; the lessor's investment is assured.

2) Operating Lease

Lease other than finance lease is called operating lease. Here risks and rewards incidental to the ownership of asset are not transferred by the lessor to the lessee. The term of such lease is much less than the economic life of the asset and thus the total investment of the lessor is not recovered through lease rental during the primary period of lease. In case of operating lease, the lessor usually provides advice to the lessee for repair, maintenance and technical knowhow of the leased asset and that is why this type of lease is also known as service lease. Operating lease has the following features:

- The lease term is much lower than the economic life of the asset.
- The lessee has the right to terminate the lease by giving a short notice and no penalty is charged for that.
- The lessor provides the technical knowhow of the leased asset to the lessee.
- Risks and rewards incidental to the ownership of asset are borne by the lessor.
- Lessor has to depend on leasing of an asset to different lessee for recovery of his/her investment.

Advantages and Disadvantages of Lease Financing

At present leasing activity shows an increasing trend. Leasing appears to be a cost-effective alternative for using an asset. However, it has certain advantages as well as disadvantages.

The advantages of lease financing from the point of view of lessor are summarized below:

- ☞ **Assured Regular Income:** Lessor gets lease rental by leasing an asset during the period of lease which is an assured and regular income.
- ☞ **Preservation of Ownership:** In case of finance lease, the lessor transfers all the risk and rewards incidental to ownership to the lessee without the transfer of ownership of asset. Hence the ownership lies with the lessor.
- ☞ **Benefit of Tax:** As ownership lies with the lessor, tax benefit is enjoyed by the lessor by way of depreciation in respect of leased asset.
- ☞ **High Profitability:** The business of leasing is highly profitable since the rate of return based on lease rental, is much higher than the interest payable on financing the asset.
- ☞ **High Potentiality of Growth:** The demand for leasing is steadily increasing because it is one of the cost efficient forms of financing. Economic growth can be maintained even during the period of depression. Thus, the growth potentiality of leasing is much higher as compared to other forms of business.
- ☞ **Recovery of Investment:** In case of finance lease, the lessor can recover the total investment through lease rentals.

Lessor suffers from certain limitations which are discussed below:

- ☞ **Unprofitable in Case of Inflation**: Lessor gets fixed amount of lease rental every year and they cannot increase this even if the cost of asset goes up.
- ☞ **Double Taxation:** Sales tax may be charged twice. First at the time of purchase of asset and second at the time of leasing the asset.
- ☞ **Greater Chance of Damage of Asset:** As ownership is not transferred, the lessee uses the asset carelessly and there is a great chance that asset cannot be useable after the expiry of primary period of lease.

6.5 Traditional Financing in Ethiopian (Equib/Edir, Etc.)

While Ethiopia has one of the least-developed formal financial sectors in the world, it possessed a rich tradition in indigenous, community-based groups such as savings and credit associations and insurance like societies. These "iqub" and "idir" groups provide a source of credit and insurance outside the formal sector but much rooted in Ethiopian society. The contributions of these groups, especially iqub, to economic growth is difficult to quantify but can be assumed to play an important role. Iqub is a traditional means of saving in Ethiopia and exists completely outside the formal financial system. An iqub is a form of savings.

People voluntarily join a group and make a mandatory contribution (every week, pay period or month or example). The "pot" is distributed on a rotating basis determined by a drawing at the beginning of the iqub. Amounts contributed vary according to the ability of the participants. Iqub is widespread, especially in urban areas. Iqub offers a savings mechanism for the "unbanked" group in Ethiopia, both urban dwellers who do not have access to a traditional bank within a reasonable distance from their dwelling. Ethiopia has one of the lowest bank penetration rates in the world, with less than one bank branch for every 100,000 residents. Currently, real interest rates are significantly negative -- at least negative 12% so iqub has advantages over the formal financial system for participants. Ethiopian banks have been paying negative real interest rate for more than 25 years.

Additionally, the social and communal aspects of iqub give participants a confidence that they may not have in Ethiopia's shaky financial system. Most formal banks require a high level of collateral and/or a guarantor for loans, which discourages start-up borrowers and does not allow for borrowing for personal needs. In the absence of loans from formal banks, Ethiopians also turn to loan sharks (Arata Abedari in Amharic) who require guarantors and charge as much as 120% per year interest.

Iqub can be a driver of economic growth and development. At lower levels, a study by Tegegne Gebre Egziabher and Mulat Demeke (year) of the Institute for Development Research at Addis Ababa University examined small business owners in rural towns. The study found that the group surveyed most frequently used their payout for expanding their business (41% of participants). At higher levels, a prominent local businessman described iqubs in Addis Ababa with payouts in excess of 15 million birr (over $500,000). They stated that much of the construction boom in Addis is being financed with iqub rather than through the formal banking system. The central bank governor has told researchers that only 5% of the country's total loan portfolio is in construction loans, Iqub is filling a vital role in providing capital for physical infrastructure expansion.

While '*Iqub*' is a means of savings and may be substitute for formal banking credit, "Idirs" are burial societies that provide a traditional form of insurance. Idir contributions are used to pay for expenses in the event of the death of a family member. Idir is the only means, other than personal savings, to pay for these expenses. Idir contributions are generally small compared to Iqub, usually around Br.10-25 per month. Some idirs provide additional coverage, for example, in cases of illness, destruction of a member's house or death of livestock. Due to their ubiquity and influence in their communities, Idir associations are also forming the basis for some foreign assistance programs, particularly those focused on HIV/AIDS treatment and prevention.

Ethiopia's formal financial system is extremely underdeveloped and for the most part confined to cities and larger towns. The traditional systems of Iqub and Idir are perhaps centuries old, yet continue to play a vital role in Ethiopia's finance. Quantifying the magnitude of funds held in these systems, particularly in iqub, is difficult. However, based on both the formal studies and anecdotal information sources, iqub provides an alternative savings and loan structure rooted in tradition, practicality and availability that acts as an engine for a portion of Ethiopia's economic growth.

6.6 Crowd Funding

Crowd funding is a method of raising capital through the collective effort of friends, family, customers, and individual investors or even from the general public. This approach taps into the collective efforts of a large pool of individuals primarily online via social media and crowd funding platforms and leverages their networks for greater reach and exposure.

6.6.1 How is Crowd Funding Different?

Crowd funding is essentially the opposite of the mainstream approach to business finance. Traditionally, if you want to raise capital to start a business or launch a new product, you would need to pack up your business plan, market research, and prototypes, and then shop your idea around to a limited pool or wealthy individuals or institutions. These funding sources included banks, angel investors, and venture capital firms, really limiting your options to a few key players. You can think of this fundraising approach as a funnel, with you and your pitch at the wide end and your audience of investors at the closed end. Fail to point that funnel at the right investor or firm at the right time, and that’s your time and money lost.

Crowd funding platforms, on the other hand, turns that funnels on-end. By giving you, the entrepreneur, a single platform to build, showcase, and share your pitch resources, this approach dramatically streamlines the traditional model. Traditionally, you'd spend months sifting through your personal network, vetting potential investors, and spending your own time and money to get in front of them. With crowd funding, it's much easier for you to get your opportunity in front of more interested parties and give them more ways to help grow your business, from investing thousands in exchange for equity to contributing Br.500 in exchange for a first-run product or other reward.

6.6.2 The Benefits of Crowd funding

From tapping into a wider investor pool to enjoying more flexible fund raising options, there are a number of benefits to crowd funding over traditional methods. Here are just a few of the many possible advantages:

Reach**:** By using a crowd funding platform like Fundable, you have access to thousands of accredited investors who can see, interact with, and share your fund raising campaign.

Presentation**:** By creating a crowd funding campaign, you go through the invaluable process of looking at your business from the top level its history, traction, offerings, addressable market, value proposition, and more and boiling it down into a polished, easily digestible package.

PR & Marketing**:** From launch to close, you can share and promote your campaign through social media, email newsletters, and other online marketing tactics. As you and other media outlets cover the progress of your fund raise, you can double down by steering traffic to your website and other company resources.

Validation of Concept**:** Presenting your concept or business to the masses affords an excellent opportunity to validate and refine your offering. As potential investors begin to express interest and ask questions, you'll quickly see if there's something missing that would make them more likely to buy in.

Efficiency**:** One of the best things about online crowd funding is its ability to centralize and streamline your fund raising efforts. By building a single, comprehensive profile to which you can funnel all your prospects and potential investors, you eliminate the need to pursue each of them individually. So instead of duplicating efforts by printing documents, compiling binders, and manually updating each one when there's an update, you can present everything online in a much more accessible format, leaving you with more time to run your business instead of fundraising.

6.6.3 Types of Crowd Funding

Just like there are many different kinds of capital round raises for businesses in all stages of growth, there are a variety of crowd funding types. Which crowd funding method you select depends on the type of product or service you offer and your goals for growth. The 3 primary types are donation-based, rewards-based, and equity crow funding.

1) **Donation-Based Crowd Funding**

Broadly speaking, you can think of any crowd funding campaign in which there is no financial return to the investors or contributors as donation-based crowd funding. Common donation-based crowd funding initiatives include fund raising for disaster relief, charities, nonprofits, and medical bills.

2) **Rewards-Based Crowd Funding**

Rewards-based crowd funding involves individuals contributing to your business in exchange for a "reward," typically a form of the product or service your company offers. Even though this method offers backers a reward, it's still generally considered a subset of donation-based crowd funding since there is no financial or equity return.

3) **Equity-Based Crowd Funding**

Unlike the donation-based and rewards-based methods, equity-based crowd funding allows contributors to become part-owners of your company by trading capital for equity shares. As equity owners, your contributors receive a financial return on their investment and ultimately receive a share of the profits in the form of a dividend or distribution.

6.7 Micro Finances

6.7.1 What is Micro Finance?

Microfinance is a term used to describe financial services, such as loans, savings, insurance and fund transfers to entrepreneurs, small businesses and individuals who lack access to banking services with high collateral requirements. Essentially, it is providing loans, credit, access to savings accounts – even insurance policies and money transfers to small business owners, entrepreneurs (many of whom live in the developing world), and those who would otherwise not have access to these resources.

Dr. Mohammad Yunus is considered a pioneer of modern microfinance. He experimented with making small loans, which he funded himself, to women in Bangladesh making bamboo furniture who had previously relied on loans with unfair and predatory terms to purchase raw materials. He discovered these very tiny loans, which traditional banks did not want to make due to the perceived risks and costs, could make a disproportionate difference to a poor person and given the chance they would pay them back creating a viable business model. He would go on to found Grameen Bank in 1983 and win the Nobel Peace Prize in 2006 for his invention of micro finance.

6.7.2 Importance of MFIs

Microfinance is important because it provides resources and access to capital to the financially underserved, such as those who are unable to get checking accounts, lines of credit, or loans from traditional banks. Without microfinance, these groups may have to resort to using loans or payday advances with extremely high interest rates or even borrow money from family and friends. Microfinance helps them invest in their businesses, and as a result, invest in themselves.

While microfinance can certainly benefit those stateside, it can also serve as an important resource for those in the developing world. For example, cell phones are being used as a way to bring financial services such as micro lending to those living in Kenya. In fact, women are major microfinance borrowers, making up 84 percent of loans in 2016, according to the 2017 Microfinance Barometer. Most of these women – around 60 percent – live in rural areas.

The microfinance industry is also growing rapidly. In 2016, there were 123 million microfinance borrowers, for a total of $102 billion in loans. India accounted for most of these borrows, followed by Vietnam, Bangladesh, and Peru.

While some have lauded microfinance as a way to end the cycle of poverty, decrease unemployment, increase earning power, and aid the financially marginalized, some experts say that it may not work as well as it should, even going so far as to say it’s lost its mission. Others argue that microfinance simply makes poverty worse since many borrowers use microloans to pay for basic necessities, or their businesses fail, which only plunges them further into debt.

For example, in South Africa, 94 percent of all microfinance loans are used for consumption, meaning, the funds are used to pay for basic necessities. This means borrowers aren’t generating new income with the initial loan, which means they have to take out another loan to pay off that loan, and so forth and so forth. This translates into a lot more debt. However, other experts say that microfinance can serve as a valuable tool for the financially underserved when used it properly. They also cite the industry's high repayment rate as proof of its effectiveness. Either way, microfinance is an important topic in the financial realm, and if done correctly, could be a powerful tool for many.

6.7.3 Micro Finances in Ethiopia

Micro-finance in Ethiopia has its origin in traditional informal method used to accumulate saving and access credit by people who lacked access to formal financial institutions. Ethiopia has also more 38 MFIs (in 2018) and practice is one of the success stories in Africa even though there are certain limitations.

The history of formal establishment of Ethiopia Micro finance institution is limited to about less than twenty years (since 2000). The first groups of few MFIs were established in early 1997 following the issuance of Proclamation No. 40/1996 in July 1996. The objective of the MFIs is basically poverty alleviation through the provision of sustainable financial services to the poor who actually do not have access to the financial support services of other formal financial institutions.

The microfinance industry is growing in terms of number and size. The MFIs in Ethiopia have been able to serve the productive poor people mainly with savings, credit, money transfer, micro-insurance and other related services. Governmental and other developmental organizations have played a vital role for impressive performance the microfinance sector in the country.

The known micro finance institutions in different regions of Ethiopia with more than 90% market share are

1. Amhara Credit and Savings Ins. (ACSI) S.C.
2. Dedebit Credit and Savings Ins. (DECSI) S.C.
3. Oromiya Credit and Savings Ins. S.C (OCSCO).
4. Omo Credit and Savings Ins. S.C.
5. Addis Credit and Savings Institution S.C.(ADCSI)

6.7.3.1 Types of Activities Carried Out by Ethiopian MFIs

According to Article 3(2) of the aforementioned proclamation, MFIs are allowed to carry out the following activities:

- Accepting both voluntary and compulsory savings as well as demand and time deposits.
- Extending credit to rural and urban farmers and people engaged in other similar activities as well as micro and small scale rural and urban entrepreneurs.
- Drawing and accepting drafts payable within Ethiopia Micro-insurance business as prescribed by NBE,
- Purchasing such income generating financial instruments as treasury bill and other income generating activities,
- Acquiring, maintaining and transferring any movable and immovable property including premises for carrying out its business,
- Supporting income generating projects of urban and rural micro and small scale operators,
- Rendering managerial, marketing, technical and administrative advice to customers and assisting them to obtain services in those fields,
- managing funds for micro and small scale business,
- Providing money transfer services,
- Providing financial leasing services,

6.8 Chapter Summary

When entrepreneurs have an idea of starting a business, they should first learn about the cost of starting an enterprise. The cost of starting an enterprise should comprises of cost of permanent capital, medium term capital and working capital. In financing their ventures, they should be clear with the different sources of finance. The internal sources of finance includes mainly Personal saving, Friends and relatives, Partners, Public stock sale (going public),Angels and Venture capital companies. The external sources of finance comprises of sources from Commercial banks, Bonds, Credit unions, Account receivable discount financing, Equipment Suppliers and Trade Credit.

In most countries including Ethiopia lease financing is becoming the common source of medium- and long-term financing where the owner of an asset gives another person, the right to use that asset against periodical payments. The owner of the asset is known as lessor and the user is called lessee. Besides the modern financing traditional financing has a paramount importance and has a long history in mobilizing huge amount of finance in Ethiopia. "Iqub" and

"Idir" groups provide a source of credit and insurance outside the formal sector but much rooted in Ethiopian society. The contributions of these groups, especially iqub, to economic growth is difficult to quantify but can be assumed to play an important role.

Crowd funding is a method of raising capital through the collective effort of friends, family, customers, and individual investors. This approach taps into the collective efforts of a large pool of individuals-primarily online via social media and crowd funding platforms—and leverages their networks for greater reach and exposure.

Microfinance is a term used to describe financial services, such as loans, savings, insurance and fund transfers to entrepreneurs, small businesses and individuals who lack access to traditional banking services

Micro-finance in Ethiopia has its origin in traditional informal method used to accumulate saving and access credit by people who lacked access to formal financial institutions.

The known micro finance institutions in different regions of Ethiopia are Addis CSI in Addis Ababa, Oromia CSI in Oromia, Amhara CSI in Amhara, Dedebit CSI in Tigrai and Omo CSI SNNP regions are the known ones.

6.9 Review Questions

1) List and elaborate capital requirements for long-term, medium term and working capital.
2) Identify the common internal and external sources of finance and which of these sources are commonly used in your locality. Discuss this with the closer business operator in your locality.
3) Getting loan from commercial banks is more challenging. Elaborate and state the requirement that banks request to provide loan.
4) Explain the pros and cons of lease financing to the lesser and the lessee.
5) Elaborate the traditional financing system is Ethiopia emphasizing their contribution to community.
6) Elaborate the feasibility and applicability of crowd funding in Ethiopia.
7) Micro finances in different regions of Ethiopia are established with the mission of supporting the poor. Evaluate.

PRACTICAL ACTIVITY

Mary's family budget

Mary is employed in a company where she earns Br.4,000 per month as a part-time employee. She also has her own business saloon and boutique where she gets Br.1,500 and Br.2,500 respectively every month.

She has a husband (Abate) who is employed under a private company with a salary of Br.10,000 per month. He receives a bonus and allowances of Br. 2,500. The couple has two kids - Adisu and Sara - both of whom are primary school pupils. Adisu is in Grade Four and Sara is in Grade One. Mary and Abate pay Br.1,000 every month for their tuition fees. They also pay Br.200 for the school bus, Br.150 for sports and games, Br.300 for books and library services. They spend Br.1,600 every month for food. They pay Br.300 for postal services, Br.300 for electricity bills and Br.200 for water bills. They also buy house detergents at Br.100 every month and pay Br.800 for car maintenance and Br.1500 for fuel. They also go shopping once per month and spend Br.1,000. They pay Br.1,500 salary every month for a house maid and Br.1,000 for a gardener. Rent costs them Br.1,200 per month, and car insurance costs Br. 1200 per year. Mary and Abate want to build their own house. They decide to prepare a budget to find out how much they can save every month. Mary starts to prepare budget by tracking their income and expenditure for a month.

Required : Prepare a budget and monthly saving plan for Mary's Family

CHAPTER 7 MANAGING GROWTH AND TRANSITION

7.1 INTRODUCTION

This chapter discusses about managing growth and transition to more formalization of organization. Entrepreneurs at the initial stage focus on resource mobilization. However, once companies reach to growth stage, they must continue to grow with proper management and leadership. The success of an entrepreneur in this process depends upon controllable and uncontrollable variables. In developing countries such as Ethiopia, the environment is not business friendly and a lot of challenges will start to emerge as the business grows. This chapter discusses about the challenges of growth, business ethics and corporate social responsibility.

Chapter Objectives

After completing this chapter, students will be able to:

- ❖ Identify factors that affect business growth,
- ❖ Understand business expansion strategies,
- ❖ Know & internalize business ethics & social responsibilities.

7.2 Timmons Model of Entrepreneurship

- **What key aspects does an entrepreneur need to manage to start and grow a business?**

To answer this question, we used Timmons basic model of entrepreneurship as indicated in Figure 7.1. This model identified the internal and external factors that determine the growth of business.

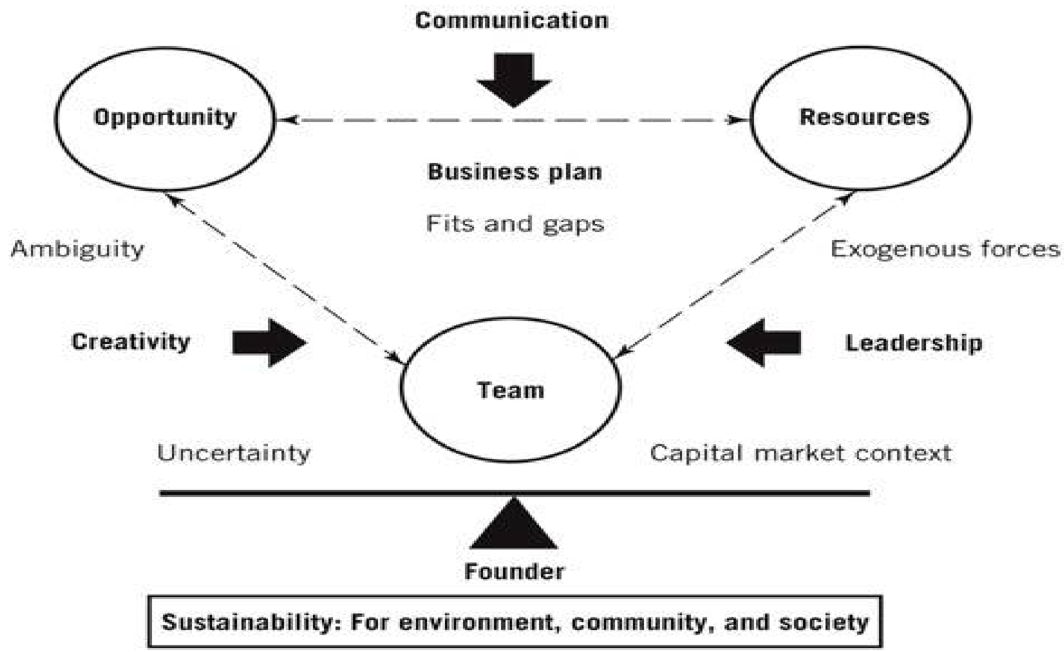


Figure 7.1 Timmons model of entrepreneurship

Jeffry Timmons (2006) developed the Timmons model of entrepreneurship through his doctoral thesis. Further research and case studies have since enhanced the model, which works as a guide for entrepreneurs to increase their chances of success. According to Timmons, success in creating a new venture is driven by a few central themes that dominate the dynamic entrepreneurial process: it takes **opportunity**, a lead **entrepreneur** and an **entrepreneurial team**, **creativity**, **being careful with money**, and an **integrated, holistic, sustainable and balanced approach to the challenges ahead**. These controllable components of the entrepreneurial process can be assessed, influenced and altered. The entrepreneur searches for an opportunity, and on finding it, shapes the opportunity into a high-potential venture by drawing up a team and gathering the required resources to start a business that capitalizes on the opportunity, the entrepreneur risks his or her career, personal cash flow and net worth

According to the model, for an entrepreneur to create a successful venture, they must balance three key components indicated earlier as elaborated here below:

1. **Opportunities**: rather than developing a perfect business plan, Timmons suggests that the entrepreneur's first and most important step is to identify and evaluate a solidly viable market opportunity, where after the business plan and funding will follow. Problems in the environment become opportunities for entrepreneurs.

   As stated earlier, Timmons model dictates that the entrepreneurial process does not start with business plan, money, strategy, networks or team. The Timmons model believes strongly that entrepreneurship is nothing but opportunity driven. Opportunities are more essential than the talent or competence of lead entrepreneur and the team because a right opportunity identified ensures long- term success of the business. A good idea does not necessarily bring about a great business. An excellent idea is found when product or services could be positioned to create or add values to customer, remains attractive, durable and timely. For example, quality problems in education created tutorial programs in residential areas for parents and their children. The shortage and problems of housemaids created daycare centers in residential areas for working mothers. These become a business in Ethiopian cities. Weaknesses in student textbook preparation in Ethiopian schools created the opportunity of preparing supplementary textbooks by business operators for which questions banks and solved problems are developed.

2. **Teams**: once an opportunity has been identified, it is critical to gather a good team of people to unlock the potential of the opportunity. Team members do have defined roles. For instance, the success of a football team is determined by the qualities of team members as goal keeper, defense, midfield and attacking teams. Likewise, people in the team have different roles, weaknesses and strengths. No one is complete in all aspects. Teams do have also evolutionary stages for maturity.

   A highly effective lead entrepreneur should be able to put the best talent together after identifying the opportunity and gathering required resources. The sizes and the background of the team are contingent upon the size and nature of opportunity. According to Timmons model, a good team can lead to great success and a badly formed team can waste great idea which is disaster to any form of business. Among all resource, only a good team can unlock a high potential with any opportunity and manage the pressure related to growth.

The two major roles of the team, relative to the other critical factors are:

- Removing the ambiguity and uncertainty of the opportunity by applying creativity (inventiveness).
- Providing leadership to manage the available resources in the most effective manner by interacting with exogenous (external) forces and the capital market context that keeps changing constantly.

3. **Resources:** finding and managing appropriate resources requires different skills than finding and managing good people, but it is equally important for eventual success. Resources may

include tangible and intangible resources. Knowledge, goodwill, information, etc., are intangible resources. Buildings, land, information technology, human resource, money, etc., are tangible resources.

Timmons suggests that balancing, or successfully juggling, these three dynamic factors is key to achieving business success. These factors are to be primarily managed through creativity, communication and leadership, to help bring the opportunity to a viable business model. Entrepreneurs, or aspiring entrepreneurs, tend to have a number of qualities that help them to identify a good market opportunity. These can include knowledge of the industry, the possible offering for the user, a sense of timing and how to enter the market, and the capacity to deal with changing situations and uncertainties. It is the entrepreneur's task to identify and capitalize on favorable events and take charge of the success equation.

As stated earlier, the Timmons model stimulates the focus on opportunities rather than threats or limitations. It brings an academically tested approach to creating new ventures, at least in concept, written down in a business plan, describing where the fits and gaps are among the three key factors of the model. It must be acknowledged that the model sees the creation of a venture as an evolutionary process. The three critical factors of entrepreneurship in the model (opportunities, team and resources) are therefore not easy to manage separately; changes in one factor have a strong influence on the other factors.

7.3 New Venture Expansion Strategies

7.3.1 Introduction

All successful small business startups eventually face the issue of handling business expansion or growth. Business expansion is a stage of a company's life that is troubled with both opportunities and perils. On the one hand, business growth often carries with it a corresponding increase in financial fortunes for owners and employees alike. In addition, expansion is usually seen as a validation of the entrepreneur's initial business startup idea, and of his or her subsequent efforts to bring that vision to fruition. But business expansion also presents the small business owner with myriad issues that have to be addressed. Growth causes a variety of changes, all of which present different managerial, legal, and financial challenges. Growth means that new employees will be hired who will be looking to the top management of the company for leadership. Growth means that the company's management will become less and less centralized, and this may raise the levels of internal politics, protectionism, and disagreement over what goals and projects the company should pursue. Growth means that market share will expand, calling for new strategies for dealing with larger competitors. Growth also means that additional capital will be required, creating new responsibilities to shareholders, investors, and institutional lenders. Thus, growth brings with it a variety of changes in the company's structure, needs, and objectives. Given these realities the need of the organization to grow must be strengthened by the need to understand that meaningful, long-term objectives. Profitable growth is a by-product of effective management and planning of the three factors indicated.

7.3.2 Methods of Growth

Small businesses can expand their operations by pursuing any number of avenues. The most commonplace methods by which small companies increase their business are incremental in character, i.e., increasing product inventory or services rendered without making wholesale changes to facilities or other operational components. But usually, after some period of time, businesses that have the capacity and desire to grow will find that other options should be studied. Common routes of small business expansion include the following common options:

- Growth through acquisition of another existing business (almost always smaller in size),
- Offering franchise ownership to other entrepreneurs,
- Licensing of intellectual property to third parties, (license for the use of certain innovative models on fee basis may be given to certain companies). This is very common for Software products.
- Establishment of business agreements with distributorships and/or dealerships,
- Pursuing new marketing routes (such as catalogs),
- Joining industry cooperatives to achieve savings in certain common areas of operation, including advertising and purchasing,
- public stock offerings (selling shares to investors and to the general public),
- Employee stock ownership plans (entrepreneurs may give/sell shares to employees as incentive for motivation. Through this process, employee owned companies may be established. This is very common for social enterprises and among Chinese firms.

Of course, none of the above options should be pursued until the business's ownership has laid the necessary groundwork for growth. The growth process begins with an honest assessment of strengths and weaknesses. Given those skills, the organization then identifies the key markets or types of future market opportunities the company is likely to capture. This, of course, raises another set of issues about how to best develop the structures and processes that will further enhance the organization's core capabilities. Once these structures and processes are identified and the long range planning completed, the business has a view of where it will be in three to five years and agreement on key strategies for building future business. One method of growth, namely organic business growth, is explained here.

7.3.3 The Ansoff Matrix – Growth Strategy

What is our business growth strategy in relation to new or existing markets and products?
The Ansoff Matrix is a strategic-planning tool that provides a framework to help executives, senior managers, and marketers devise strategies for future growth. It is named after Russian American Igor Ansoff, who came up with the concept. Ansoff suggested that there were effectively only two approaches to developing a growth strategy; through varying what is sold (product growth) and who it is sold to (market growth).

"When we are in peak, we make a ton of money, as soon as we make a ton of money; we are desperately looking for ways to spend it. And we diversify into areas that, frankly, we don't know how to run very well," thought Bill Ford, great grandson of Henry. Ford's story is neither unique nor new and companies often choose sub-optimal growth paths.

Igor Ansoff created the product/market matrix to illustrate the inherent risks in four generic growth strategies as summarized here below:

1. **Market penetration / consumption –** the firm seeks to achieve growth with existing products in their current market segments, aiming to increase market share. This is a low risk strategy because of the high experience of the entrepreneur with the product and market.
2. **Market development –** the firm seeks growth by pushing its existing products into new market segments. Market development has medium to high risk.
3. **Product development –** the firm develops new products targeted to its existing market segments. This alternative growth strategy is characterized by medium to high risk due to lack of experience about the new product.
4. **Diversification –** the firm grows by developing new products for new markets. This is high risk option as entrepreneurs do not have experience about the product and the market.

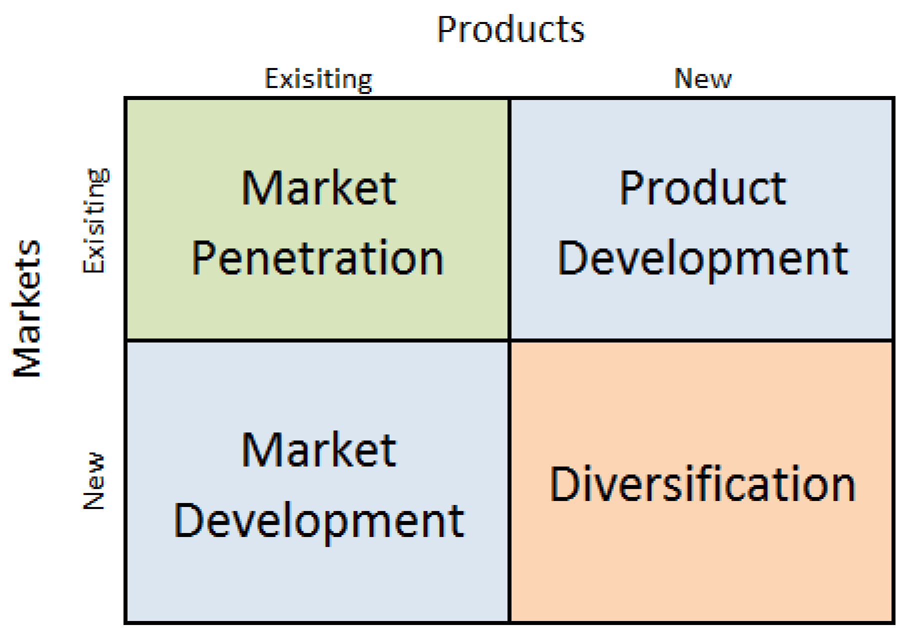


Figure 7.2 Ansoff's Matrix

7.3.3.1 Selecting a Product-Market Growth Strategy

I) Market penetration / consumption:

Market penetration and consumption covers products that are existent in an existing market. In this strategy, there can be further exploitation of the products without necessarily changing the product or the outlook of the product. This will be possible through the use of promotional methods, putting various pricing policies that may attract more customers, or one can make the distribution more extensive.

Market penetration or consumption can also be increased by coming up with various initiatives that will encourage increased usage of the product. A good example is the usage of toothpaste. Research has shown that the toothbrush head influences the amount of toothpaste that one will use. Thus if the head of the toothbrush is bigger it will mean that more toothpaste will be used thus promoting the usage of the toothpaste and eventually leading to more purchase of the toothpaste.

In market penetration / consumption, the risk involved is usually the least since the products are already familiar to the consumers and so is the established market.

II) Market development

In this strategy, the business sells its existing products to new markets. This can be made possible through further market segmentation to aid in identifying a new clientele base. This strategy assumes that the existing markets have been fully exploited thus the need to venture into new markets. There are various approaches to this strategy, which include: new geographical markets, new distribution channels, new product packaging, and different pricing policies.

Going into new geographies could involve launching the product in a completely different market. A good example is Guinness. This beer had originally been made to be sold in countries that have a colder climate, but now it is also being sold in African countries including Ethiopia.

New distribution channels could entail selling the products via e-commerce or mail order. Selling through e-commerce may capture a larger clientele base since we are in a digital era where most people access the Internet often. In new product packaging, it means repacking the product in another method or dimension. That way it may attract a different customer base. In different pricing policies, the business could change its prices so as to attract a different customer base or create a new market segment.

III) Product development

With a product-development growth strategy, a new product is introduced into existing markets. Product development can be from the introduction of a new product in an existing market or it can involve the modification of an existing product. By modifying the product one could change its outlook or presentation, increase the product's performance or quality. By doing so, it can be more appealing to the existing market. A good example is car manufacturers who offer a range of car parts so as to target the car owners in purchasing additional products.

IV) Diversification

This growth strategy involves an organization marketing or selling new products to new markets at the same time. It is the most risky strategy as it involves two unknowns:

- New products are being created and the business does not know the development problems that may occur in the process.
- There is also the fact that there is a new market being targeted, which will bring the problem of having unknown characteristics.

For a business to take a step into diversification, they need to have their facts right regarding what it expects to gain from the strategy and have a clear assessment of the risks involved. There are two types of diversification – related diversification and unrelated diversification.

In related diversification, the business remains in the same industry in which it is currently operating. For example, a cake manufacturer diversifies into fresh-juice manufacturing. This diversification is within the food industry.

In unrelated diversification, there are usually no previous industry relations or market experiences. One can diversify from a food industry into the personal-care industry. A good example of the unrelated diversification is Richard Branson. He took advantage of the Virgin brand and diversified into various fields such as entertainment, air and rail travel, foods, etc. Sir Branson has more than 400 companies.

7.3.4 Expansion Issues

Whatever method a company chooses to utilize to expand—and whatever guiding strategy it chooses to employ its owners will likely face a combination of potentially frustrating issues as they try to grow their business in a smooth and productive manner. *Growth* means understanding, adjusting to, and managing a whole new set of challenges in essence, a very different business.

IX) Growing Too Fast

This is a common disease that strikes ambitious and talented entrepreneurs who have built a flourishing business that meets a strong demand for a specific set of goods and/or services. Success is wonderful, of course, but rapid growth can sometimes overwhelm the ill-prepared business owner. Companies growing at hyper-speed sometimes pay a steep price for their success. According to management experts, controlling fast-track growth and the problems that come with it can be one of the most frightening tasks an entrepreneur will face. This problem most often strikes on the operational end of a business. Demand for a product will outpace production capacity, for example. Effective research and long range planning can do a lot to relieve the problems often associated with rapid business expansion.

X) Recordkeeping and Other Infrastructure Needs

It is essential for small businesses that are undergoing expansion to establish or update systems for monitoring cash flow, tracking inventories and deliveries, managing finances, tracking human resources information, and myriad other aspects of the rapidly expanding business operation. In addition, growing enterprises often have to invest in more sophisticated communication systems in order to provide adequate support to various business operations.

XI) Expansion Capital

Small businesses experiencing growth often require additional financing. Finding expansion capital can be a frustrating experience for the ill-prepared entrepreneur, but for those who plan ahead, it can be far less painful. Businesses should revise their business plan on an annual basis and update marketing strategies accordingly so that you are equipped to secure financing under the most advantageous terms possible.

XII) Personnel Issues

Growing companies will almost always have to hire new personnel to meet the demands associated with new production, new marketing campaigns, new recordkeeping and administrative requirements, etc. Careful hiring practices are always essential, but they are even more so when a business is engaged in a sensitive period of expansion.

Business expansion also brings with it increased opportunities for staff members who were a part of the business in its early days. The entrepreneur who recognizes these opportunities and delegates responsibilities appropriately can go far toward satisfying the desires of employees who want to grow in both personal and professional capacities. But, small business owners also need to recognize that business growth often triggers the departure of workers who are either unable or unwilling to adjust to the changing business environment. Indeed, some employees prefer the more relaxed, family-type atmosphere that is prevalent at many small business establishments to the more business-like environment that often accompanies periods of growth. Entrepreneurs who pursue a course of ambitious expansion may find that some of their most valuable and well-liked employees decide to instead take a different path with their lives.

XIII) Customer Service

Good customer service is often a significant factor in small business success, but ironically it is also one of the first things that tends to fall by the roadside when business growth takes on a hectic flavor. When the workload increases tremendously, there's a feeling of being overwhelmed. And sometimes you have a hard time getting back to clients in a timely fashion. So the very customer service that caused your growth in the first place becomes difficult to sustain. Under such scenarios, businesses not only have greater difficulty retaining existing clients, but also become less effective at securing new business. A key to minimizing such developments is to maintain adequate staffing levels to ensure that customers receive the attention and service they demand (and deserve).

XIV) Disagreements among Ownership

On many occasions, ownership arrangements that functioned fairly effectively during the early stages of a company's life can become increasingly problematic as business issues become more complex and divergent philosophies emerge. For example, one or more of the cofounders are unable to keep pace with the level of sophistication or business wisdom that the company now requires. Such a cofounder is no longer making a significant contribution to the business and in essence has become 'obsolete.' It's even harder when the obsolete partner is a close friend or family member. In this case, you need to ask: Will the obsolete cofounder's ego allow for a position of diminished responsibility? Can our overhead continue to keep him or her on staff?" Another common scenario that unfolds during times of business growth is that the owners realize that they have profoundly different visions of the company's future direction. One founder may want to devote resources to exploring new marketing niches, while the other may be convinced that consolidation of the company's presence in existing markets is the way to go. In such instances, the departure of one or more partners may be necessary to establish a unified direction for the growing company.

XV) Family Issues

Embarking on a strategy of aggressive business expansion typically entails an extensive sacrifice of time and often of money on the part of the owner (or owners). But as many growing companies especially those founded by younger entrepreneurs, are established at a time when all of the cofounders are either unmarried or in the early stages of a marriage. As the size of the company grows, so does the size of the cofounder’s family. Cofounders with young children may feel pressure to spend more time at home, but their absence will significantly cut their ability to make a continuous, valuable contribution to the company's growth. Entrepreneurs thinking a strategy of business growth, then, need to decide whether they are willing to make the sacrifices that such initiatives often require.

XVI) Transformation of Company Culture

As companies grow, entrepreneurs often find it increasingly difficult for them to keep the business grounded on the bedrock values that were instituted in its early days. Owners are ultimately the people that are most responsible for communicating those values to employees. But as staff size increases, markets grow, and deadlines proliferate, that responsibility gradually falls by the edge and the company culture becomes one that is far different from the one that was in place and enjoyed just a few short years ago. Entrepreneurs need to make sure that they stay attentive to their obligations and role in shaping company culture.

XVII) Changing Role of Owner At The Initial State

You have few employees; you're doing lots of things yourself. But when a company experiences its first real surge of growth, it's time for you to change what you do. You need to become a CEO—that is, the leader, the strategic thinker, and the planner—and to delegate day-to-day operations to others. Moreover, as businesses grow in size they often encounter problems that increasingly require the experience and knowledge of outside people. Entrepreneurs guiding growing businesses have to be willing to solicit the expertise of accounting and legal experts where necessary, and they have to recognize their shortcomings in other areas that assume increased importance with business expansion.

7.3.5 Choosing not to Grow

Small business owners choose not to expand their operations even though they have ample opportunity to do so. For many small business people, the greatest satisfactions in owning a business, which often include working closely with customers and employees, inevitably diminish as the business grows and the owner's role changes. Many entrepreneurs would rather limit growth than give up those satisfactions. Other successful small business owners, meanwhile, simply prefer to avoid the headaches that inevitably occur with increases in staff size, etc. And many small business owners choose to maintain their operations at a certain level because it enables them to devote time to family and other interests that would otherwise be allocated to expansion efforts.

7.4 Business Ethics and Social Responsibility

Learning Objectives

- Define and discuss the three main theories of corporate social responsibility (CSR).
- Explain why CSR ultimately benefits both companies and their stakeholders.

7.4.1 Introduction

Business organizations, as established by their entrepreneurs, are expected to do their businesses in a sustainable and ethical manner. For this there are certain theories that we should understand.

These theories have been evolving through time as business practices mature and grow as well as societal and government influence increase.

7.4.2 Three Approaches to Corporate Responsibility

According to the traditional view of the corporation, it exists primarily to make profits supported by stockholder theory. From this money-centered perspective, insofar as business ethics are important, they apply to moral dilemmas arising as the struggle for profit proceeds. These dilemmas include: “What obligations do organizations have to ensure that individuals seeking employment or promotion are treated fairly?” “How should conflicts of interest be handled?” and “What kind of advertising strategy should be pursued?” “What pricing strategy should be pursued?”

While these dilemmas continue to be important throughout the economic world, when businesses are conceived as holding a wide range of economic and civic responsibilities as part of their daily operation, the field of business ethics expands correspondingly. Now there are large sets of issues that need to be confronted and managed outside of and independent of the struggle for money. Broadly, there are three theoretical approaches to these new responsibilities:

1. Corporate social responsibility (CSR)
2. The triple bottom line
3. Stakeholder theory

Corporate Social Responsibility (CSR)

The title corporate social responsibility has two meanings. First, it’s a general name for any theory of the corporation that emphasizes both the responsibility to make money and the responsibility to interact ethically with the surrounding community. Second, corporate social responsibility is also a specific conception of that responsibility to profit while playing a role in broader questions of community welfare. For its definition, CRS is a philosophy in which the company’s expected actions include not only producing a reliable product, charging a fair price with fair profit margins, and paying a fair wage to employees, but also caring for the environment and acting on other social concerns.

As a specific theory of the way corporations interact with the surrounding community and larger world, corporate social responsibility (CSR) is composed of four obligations:

1. **The economic responsibility to make money**. Required by simple economics, this obligation is the business version of the human survival instinct (to live we have to eat). Companies that don't make profits are in a modern market economy doomed to perish. Of course there are special cases. Nonprofit organizations make money (from their own activities as well as through donations and grants), but pour it back into their work. Also, public/private hybrids can operate without turning a profit. In some cities, trash collection is handled by this kind of organization, one that keeps the streets clean without (at least theoretically) making anyone rich. For the vast majority of operations, however, there have to be profits. Without them, there's no business and no business ethics.
2. **The legal responsibility** to adhere to rules and regulations. Like the previous, this responsibility is not controversial. What proponents of CSR argue, however, is that this obligation must be understood as a proactive duty. That is, laws aren't boundaries that enterprises skirt and cross over if the penalty is low; instead, responsible organizations accept the rules as a social good and make good faith efforts to obey not just the letter but also the spirit of the limits. In concrete terms, this is the difference between the driver who stays under the speed limit because he can't afford a traffic ticket, and one who obeys because society as a whole is served when we all agree to respect the signs and stoplights and limits.
3. **The ethical responsibility** to do what's right even when not required by the letter or spirit of the law. This is the theory's keystone obligation, and it depends on a coherent corporate culture that views the business itself as a citizen in society, with the kind of obligations that citizenship normally entails. When someone is racing their Porsche along a country road on a freezing winter's night and encounters another driver stopped on the roadside with a flat, there's a social obligation to do something, though not a legal one. The same logic can work in the corporate world. Many industrial plants produce, as an unavoidable part of their fabricating process, poisonous waste. Think of a plant producing toxin in the manufacturing process. The law governing toxic waste disposal may be ambiguous, but even if the companies are not legally required to enclose their poisons in double-encased, leak-proof barrels, isn't that the right thing to do so as to ensure that the contamination will be safely contained? True, it might not be the right thing to do in terms of pure profits, but from a perspective that values everyone's welfare as being valuable, the measure could be recommendable.

4. **The philanthropic responsibility** to contribute to society's projects even when they're independent of the particular business. A lawyer driving home from work may spot the local children gathered around an impoverished area stand and sense an obligation to buy food to contribute to the neighborhood project. Similarly, a law firm may volunteer access to their offices for an afternoon every year so some local schoolchildren may take a field trip to discover what lawyers do all day. An industrial chemical company may take the lead in rehabilitating an empty lot into a park. None of these acts arise as obligations extending from the day-to-day operations of the business involved. They're not like the responsibility a chemical firm has for safe disposal of its waste. Instead, these public acts of generosity represent a view that businesses, like everyone in the world, have some obligation to support the general welfare in ways determined by the needs of the surrounding community.

The Triple Bottom Line

The triple bottom line is a form of corporate social responsibility dictating that corporate leaders formulate bottom-line results not only in economic terms (costs versus revenue) but also in terms of company effects in the social realm, and with respect to the environment. There are two keys to this idea. First, the three columns of responsibility must be kept separate, with results reported independently for each. Second, in all three of these areas, the company should obtain sustainable results.

The notion of sustainability is very specific. At the intersection of ethics and economics, sustainability means the long-term maintenance of balance. As elaborated by here below how the balance is defined and achieved economically, socially, and environmentally:

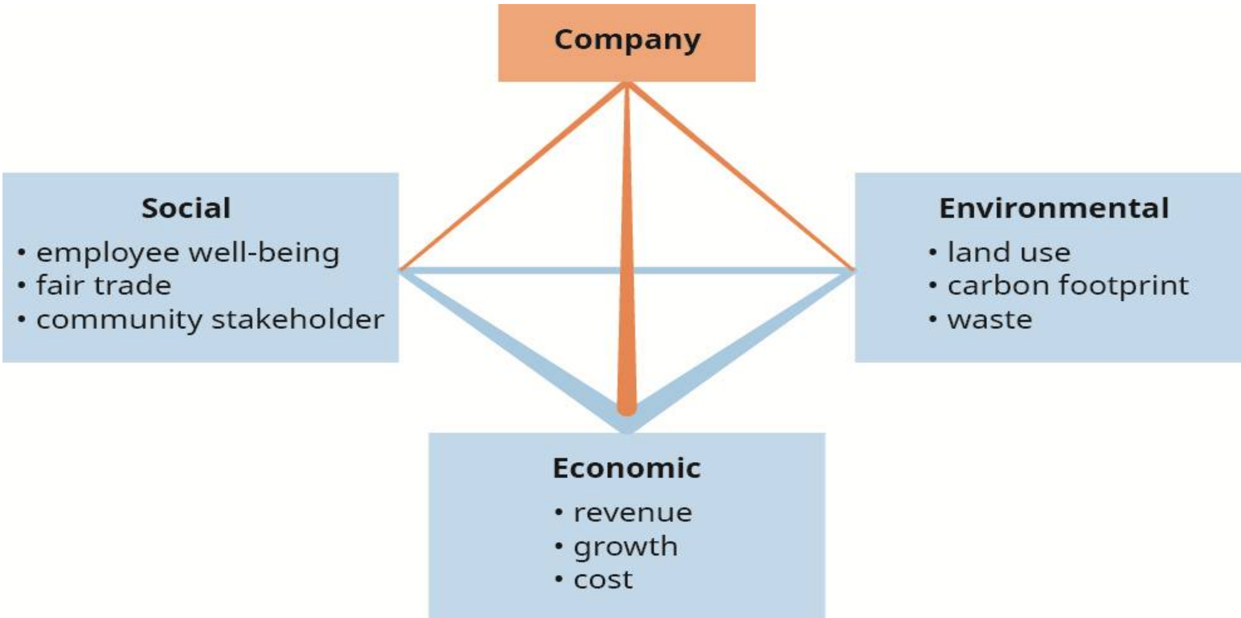


Figure 7.3 Triple bottom lines

- **Economic sustainability** values long-term financial solidity over more volatile, short-term profits, no matter how high. According to the triple-bottom-line model, corporations have a responsibility to create business plans allowing stable and prolonged action. That bias in favor of duration should make companies hesitant about investing in things like dot-coms. While it's true that speculative ventures may lead to windfalls, they may also lead to collapse. Silicon Valley, California, for example, is full of small, start-up companies. A few will convert into the next Google, Apple, and Microsoft. What gets left out, however, of the newspaper reports hailing the accomplishments of a Steve Jobs or a Bill Gates are all those other people who never made it—all those who invested family savings in a project that ended up bankrupt. Sustainability as a virtue means valuing business plans that may not lead to quick riches but that also avoid disastrous losses.
- **Social sustainability** values balance in people's lives and the way we live. A world in which a few Fortune 500 executives are moving down millions a year, while millions of people elsewhere in the world are living on pennies a day can't go on forever. As the imbalances grow, as the rich get richer and the poor get both poorer and more numerous, the chances that society itself will collapse in anger and revolution increase. The threat of governmental overthrow from below sounds remote almost absurd for powerful nations such as to Americans who are accustomed to a solid middle class and minimal resentment of the wealthy. In world history, however, such revolutions are quite common. That doesn't mean

revolution is coming to our time's developed nations. It may indicate, however, that for a business to be stable over the long term, opportunities and subsequently wealth need to be spread out to cover as many people as possible.

The **fair trade movement** fits this ethical imperative to shared opportunity and wealth. Developed and refined as an idea in Europe in the 1960s, organizations promoting fair trade ask businesses—especially large producers in the richest countries to guarantee that suppliers in impoverished nations receive reasonable payment for their goods and services even when the raw economic laws of supply and demand don't require it. An array of ethical arguments may be arranged to support fair trade, but on the front of sustainability, the lead argument is that peace and order in the world depend on the world's resources being divided up in ways that limit greed, resentment, and anger. For instance, there is a fair trade practice for specialty coffee from Ethiopian farmers to markets of developed nations. Ethiopian coffee farmers, through specialty coffee as certified, get more than 30% than the prices of normal coffee.

Social sustainability doesn't end with dollars; it also requires human respect. All work, the logic of stability dictates, contains dignity, and no workers deserve to be treated like machines or as expendable tools on a production line. In today's capitalism, many see—and the perception is especially strong in Europe a world in which dignity has been stripped away from a large number of trades and professions.

Finally, social sustainability requires that corporations as citizens in a specific community of people maintain a healthy relationship with those people. Corporations should not affect the health of community negatively.

- **Environmental sustainability** begins from the affirmation that natural resources—especially the oil fueling engines, the clean air we breathe, and the water we drink—are limited. If those things deteriorate significantly, our children won't be able to enjoy the same quality of life most of us experience. Conservation of resources, therefore, becomes tremendously important, as does the development of new sources of energy that may substitute those we're currently using.

Further, the case of an industrial chemical company pouring toxins into the ground that erupt years later with horrific consequences evidences this: not only are resources finite, but our earth is limited in its ability to naturally regenerate clean air and water from the pipes and runoff of our industries. There are, clearly, good faith debates that thoughtful people can have about where those limits are. For example, have we released greenhouse gases into the air so heavily that the earth's temperature is rising? No one knows for sure, but it's certain that somewhere there's a limit; at some point carbon-burning pollution will do to the planet: make the place unlivable. Sustainability, finally, on this environmental front means actions must be taken to facilitate our natural world's renewal. Recycling or cleaning up contamination that already exists is important here, as is limiting the pollution emitted from factories, cars, and consumer products in the first place. All these are actions that corporations must support, not because they're legally required to do so, but because the preservation of a livable planet is a direct obligation within the triple-bottom-line model of business responsibility.

Together, these three notions of sustainability economic, social, and environmental guide businesses toward actions fitted to the conception of the corporation as a participating citizen in the community and not just as a money machine.

One deep difference between corporate social responsibility and the triple bottom line is cultural. The first is more American, the second European. Americans, accustomed to economic progress, tend to be more comfortable with, and optimistic about, change. Collectively, Americans want business to transform the world, and ethical thinking is there (hopefully) to help the transformations maximize improvement across society. Europeans, accustomed to general economic decline with respect to the United States, view change much less favorably. Their inclination is to slow development down, and to keep things the same as far as possible. This outlook is naturally suited to sustainability as a guiding value.

Stakeholder Theory

Stakeholder theory, which has been described by Edward Freeman and others, is the mirror image of corporate social responsibility. Instead of starting with a business and looking out into the world to see what ethical obligations are there, stakeholder theory starts in the world. It lists and describes those individuals and groups who will be affected by (or affect) the company's actions and asks, "What are their legitimate claims on the business?" "What rights do they have with respect to the company's actions?" and "What kind of responsibilities and obligations can they justifiably impose on a particular business?" In a single sentence, stakeholder theory affirms that those whose lives are touched by a corporation hold a right and obligation to participate in directing it.

As a simple example, when a factory produces industrial waste, a CSR perspective attaches a responsibility directly to factory owners to dispose of the waste safely. By contrast, a stakeholder theorist begins with those living in the surrounding community who may find their environment poisoned, and begins to talk about business ethics by insisting that they have a right to clean air and water. Therefore, they're stakeholders in the company and their voices must contribute to corporate decisions. It's true that they may own no stock, but they have a moral claim to participate in the decision-making process. This is a very important point. At least in theoretical form, those affected by a company's actions actually become something like shareholders and owners. Because they're touched by a company's actions, they have a right to participate in managing it.

Who are the stakeholders surrounding companies? The answer depends on the particular business, but the list can be quite extensive. If the enterprise produces chemicals for industrial use and is located in a small town, the stakeholders and their interests in parentheses include:

- Company owners, whether a private individual or shareholders, (reasonable profit)
- Company workers (reasonable salaries that enable them to live decent lives),
- Customers and potential customers of the company (quality products at fair prices),
- Suppliers and potential suppliers to the company (fair prices for their inputs),
- Everyone living in the town who may be affected by contamination from workplace operations,
- Creditors whose money or loaned goods are mixed into the company's actions,
- Government entities involved in regulation and taxation (fair tax),
- Local businesses that cater to company employees (restaurants where workers have lunch, grocery stores where employee families shop, and similar),
- Other companies in the same line of work competing for market share (fair competition for competitiveness of the industry),

The outer limits of stake-holding are blurry. In an abstract sense, it's probably true that everyone in the world counts as a stakeholder of any serious factory insofar as we all breathe the same air and because the global economy is so tightly linked that decisions taken in a boardroom in a small town on the East Coast can end up costing someone in India her job and the effects keep rippling out from there.

In practical terms, however, a strict stakeholder theory—one insistently bestowing the power to make ethical claims on anyone affected by a company's action—would be inoperable. There'd be no end to simply figuring out whose rights needed to be accounted for. Realistically, the stakeholders surrounding a business should be defined as those tangibly affected by the company's action. There ought to be an unbroken line that you can follow from a corporate decision to an individual's life.

Once a discrete set of stakeholders surrounding an enterprise has been located, **stakeholder ethics may begin**. The purpose of the firm, underneath this theory, is to maximize profit on a collective bottom line, with profit defined not as money but as human welfare. The collective bottom line is the summed effect of a company's actions on all stakeholders. Company managers, that means, are primarily charged not with representing the interests of shareholders (the owners of the company) but with the more social task of coordinating the interests of all stakeholders, balancing them in the case of conflict and maximizing the sum of benefits over the medium and long term. Corporate directors, in other words, spend part of the day just as directors always have: explaining to board members and shareholders how it is that the current plans will boost profits. They spend other parts of the day, however, talking with other stakeholders about their interests: they ask for input from local environmentalists about how pollution could be limited, they seek advice from consumers about how product safety could be improved and so on. At every turn, stakeholders are treated (to some extent) like shareholders, as people whose interests need to be served and whose voices carry real force.

In many cases transparency is an important value for those promoting stakeholder ethics. The reasoning is simple: if you're going to let every stakeholder actively participate in a corporation's decision making, then those stakeholders need to have a good idea about what's going on. The theory demands that all those who may be affected know what's being dumped, what the risks are to people and the environment, and what the costs are of taking the steps necessary to dispose of the chemical runoff more permanently and safely.

7.4.3 Business Ethics Principles

There are certain universal ethical principles that managers of enterprises must adhere to. Ethical values, translated into active language establishing standards or rules describing the kind of behavior an ethical person should and should not engage in, are ethical principles. The following list of principles incorporates the characteristics and values that most people associate with ethical behavior.

1. **Honesty**. Ethical executives are honest and truthful in all their dealings and they do not deliberately mislead or deceive others by misrepresentations, overstatements, partial truths, selective omissions, or any other means.
2. **Integrity**. Ethical executives demonstrate personal integrity and the courage of their convictions by doing what they think is right even when there is great pressure to do otherwise; they are principled, honorable and upright; they will fight for their beliefs. They will not sacrifice principle for suitability, be hypocritical, or unscrupulous.
3. **Promise-Keeping & Trustworthiness**. Ethical executives are worthy of trust. They are candid and forthcoming in supplying relevant information and correcting misapprehensions of fact, and they make every reasonable effort to fulfill the letter and spirit of their promises and commitments. They do not interpret agreements in an unreasonably technical or legalistic manner in order to rationalize non-compliance or create justifications for escaping their commitments.
4. **Loyalty**. Ethical executives are worthy of trust, demonstrate fidelity and loyalty to persons and institutions by friendship in adversity, support and devotion to duty; they do not use or disclose information learned in confidence for personal advantage. They safeguard the ability to make independent professional judgments by scrupulously avoiding undue influences and conflicts of interest. They are loyal to their companies and colleagues and if they decide to accept other employment, they provide reasonable notice, respect the proprietary information of their former employer, and refuse to engage in any activities that take undue advantage of their previous positions.
5. **Fairness**. Ethical executives are fair and just in all dealings; they do not exercise power arbitrarily, and do not use overreaching nor offensive means to gain or maintain any advantage nor take undue advantage of another's mistakes or difficulties. Fair persons manifest a commitment to justice, the equal treatment of individuals, tolerance for and acceptance of diversity, they are open-minded; they are willing to admit they are wrong and, where appropriate, change their positions and beliefs.

6. **Concern for Others**. Ethical executives are caring, compassionate, benevolent and kind; they like the **Golden Rule**, help those in needs, and seek to accomplish their business objectives in a manner that causes the least harm and the greatest positive good.
7. **Respect for Others.** Ethical executives demonstrate respect for the human dignity, autonomy, privacy, rights, and interests of all those who have a stake in their decisions; they are courteous and treat all people with equal respect and dignity regardless of sex, race or national origin.
8. **Law Abiding**. Ethical executives abide by laws, rules and regulations relating to their business activities.
9. **Commitment to Excellence**. Ethical executives pursue excellence in performing their duties, are well informed and prepared, and constantly endeavor to increase their proficiency in all areas of responsibility.
10. **Leadership**. Ethical executives are conscious of the responsibilities and opportunities of their position of leadership and seek to be positive ethical role models by their own conduct and by helping to create an environment in which principled reasoning and ethical decision making are highly prized.
11. **Reputation and Morale**. Ethical executives seek to protect and build the company's good reputation and the morale of its employees by engaging in no conduct that might undermine respect and by taking whatever actions are necessary to correct or prevent inappropriate conduct of others.
12. **Accountability.** Ethical executives acknowledge and accept personal accountability for the ethical quality of their decisions and omissions to themselves, their colleagues, their companies, and their communities.

7.5 Summary

1. Entrepreneurs must be able to manage controllable factors and understand the external and uncontrollable variables. The external environment is the source of opportunities. Problems in societies are opportunities for business.
2. There are many methods of growth, the internal growth strategy may be simple to implement in Ethiopia. But, there are limited government regulations for other methods such as acquisition and merger.

3. The Ansoff matrix gives managers a framework for surveying all the initiatives the business has under way – how many are being pursued in each realm and how much investment is going to each type, and also allows managers to understand the risks and thus probability of success of each initiative.
4. Entrepreneurs must be able to understand the obstacles for growth.
5. Corporations may have obligations that go beyond generating profits and include the larger society.
6. Corporate social responsibility as a specific theory affirms that corporations are entities with economic, legal, ethical, and philanthropic obligations.
7. Corporations responsible for a triple bottom line seek sustainability in the economic, social, and environmental realms.
8. Corporate ethics built on stakeholder theory seek to involve all those affected by the organization in its decision-making process. Ethical principles are guides for decision making in business.

7.6 Review Questions

1. Conduct interview with business owner such as Café or Restaurant around your locality. What are the challenges for growth of his/her business?
2. For corporate advocates of the specific CSR theory, what are the responsibilities the corporation holds, and how are conflicts between those responsibilities managed?
3. Create a hypothetical situation in which philanthropy would not be required of a corporation by CSR theory.
4. What does sustainability mean within each of the three columns of the theory of the triple bottom line?
5. How does the fair trade movement fit together with the triple-bottom-line theory of corporate responsibility?
6. Who are the stakeholders in stakeholder ethics?
7. What does it mean for a corporate director to “balance stakeholder interests”?
8. What basic elements do CSR, the triple bottom line, and stakeholder theory have in common?
9. What do you want to say about the ethical practices of business around your community? Why?

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