

CBSE
Class XII Business Studies
Abroad Board Paper Set 1 - 2014

Time: 3 hrs

Max. Marks: 90

Note:

- Please check that this question paper contains 12 printed pages.
- Code number given on the right hand side of the question paper should be written on the title page of the answer-book by the candidate.
- Please check that this question paper contains 30 questions.
- **Please write down the Serial Number of the question before attempting it.**
- 15 minutes time has been allotted to read this question paper. The question paper will be distributed at 10.15 a.m. From 10.15 a.m. to 10.30 a.m., the students will read the question paper only and will not write any answer on the answer-book during this period.

General Instructions:

- (i) All questions in both the sections are compulsory.
- (ii) Marks for questions are indicated against each question.
- (iii) Questions No. **1 - 12** are very short-answer questions carrying **1** mark each. They are required to be answered in one sentence each.
- (iv) Questions No. **13 - 18** are short answer questions carrying **3** marks each. Answers to them should normally not exceed **50 - 75** words each.
- (v) Questions No. **19 - 22** are also short answer questions carrying **4** marks each. Answers to them should normally not exceed **150** words each.
- (vi) Question number **23 - 26** are long-answer questions carrying **5** marks each. Answers to them should normally not exceed **150** words each.
- (vii) Question number **27 - 30** are long-answer questions carrying **6** marks each. Answers to them should normally not exceed **200** words each.
- (viii) Answers should be brief and to the point and the above word limits should be adhered to as far as possible.

1. Define 'Financial Management'. **[1]**

2. What is meant by 'Feedback' in the concept of communication? **[1]**

3. How does 'Cost of Debt' affect the capital structure of a company? State. **[1]**

4. Why do employees become lethargic when the organization uses internal sources of recruitment? State. **[1]**

5. Give two characteristics of 'Organizational Climate' that influence the behaviour of individuals and act as a non-financial incentive. [1]
6. 'Maintaining labour relations and union-management relations' is one of the specialised activities performed by Human Resource Management. Mention any two other specialised activities of Human Resource Management. [1]
7. What is meant by 'Management of Operations'? [1]
8. Give the meaning of 'Accountability' as an element of delegation. [1]
9. What is included in 'Technological Environment' of business? State. [1]
10. Give the meaning of 'Procedure' as a type of plan. [1]
11. Define organization as a structure. [1]
12. What is determined by 'Fatigue Study'? [1]
13. Crackers Ltd., a fire-cracker manufacturing company launched some new products on the eve of Diwali in the market, which attracted many buyers. To meet the increased demand the company employed children from nearby villages. Although the products were in great demand, appropriate safety warnings for use were not mentioned on the labels, which led to many accidents.
- Identify and explain the important product related decision that was not taken into consideration by the company.
 - Also state any two values which were violated by the company. [3]
14. How are consumer grievances redressed by the three-tier machinery under Consumer Protection Act, 1986? Explain. [3]
15. Explain any three organizational barriers to effective communication. [3]
16. Explain the following Money Market Instruments: [3]
- Treasury bill
 - Commercial paper
 - Call money
17. State any three points of importance of consumer protection from the point of view of consumers. [3]
18. Kavya is working in a company on permanent basis. As per the job agreement she had to work for 8 hours a day and was free to work overtime. Kavya worked overtime. But

even after working for long hours and putting in her best efforts, no recognition was given to her by her boss. Due to overtime she fell ill and had to take leave from her work. No one showed concern and enquired about her health. She realised that she was fulfilling only some of her needs while some other needs still remained to be fulfilled. [3]

- i. Identify and explain the needs of Kavya discussed in the above para, by quoting the lines.
- ii. Also explain two other needs of Kavya followed by the above needs, which still remained to be satisfied

19. What is meant by the 'Business Environment'? Explain any three features of business environment. [4]

20. Give the meaning of 'Investment' and 'Dividend' decisions of financial management. [4]

21. Mega Ltd. was manufacturing water-heaters. In the first year of its operations, the revenue earned by the company was just sufficient to meet its costs. To increase the revenue, the company analysed the reasons of less revenue. After analysis the company decided [4]

- i. To reduce the labour cost by shifting the manufacturing unit to a backward area where labour was available at a very low rate.
- ii. To start manufacturing solar water-heaters and reduce the production of electric water-heaters slowly.

This will not only help in covering the risks, but also help in meeting other objectives too.

- a. Identify and explain the objectives of management discussed above.
- b. State any two values which the company wanted to communicate to the society.

22. How is training in an organisation beneficial 'for employees'? State by giving any four reasons. [4]

23. State any five features of planning. [5]

24. What is meant by 'Physical Distribution'? Explain its major components. [5]

25. Principles of Taylor and Fayol are mutually complementary. One believed that the management should scientifically select the person and the work assigned should suit his/her physical and intellectual capabilities, while the other suggested that the work can be performed more efficiently if divided into specialised tasks. Identify and explain the principles of Fayol and Taylor referred to in the above para. [5]

26. Differentiate between 'Capital Market' and 'Money Market' on the basis of the following: [5]

- i. Safety
- ii. Expected Return

- iii. Investment outlay
- iv. Participants
- v. Duration

27. Explain any four points which highlight the importance of controlling. [6]

OR

Explain the relationship between planning and controlling.

28. Explain the following functions of marketing: [6]

- i. Marketing Planning
- ii. Product designing and development
- iii. Pricing of products
- iv. Standardisation and Grading

OR

'Though advertising is one of the most frequently used media of promotion of goods and services, yet it attracts lot of objections.' Explain any four such objections.

29. Differentiate between formal and informal organization on the following basis: [6]

- i. Meaning
- ii. Origin
- iii. Authority
- iv. Behaviour
- v. Flow of communication
- vi. Nature

OR

With the help of any four points, explain the importance 'Decentralisation' in an organization.

30. Explain the following as factors affecting the requirements of working capital : [6]

- i. Nature of business
- ii. Scale of operations
- iii. Seasonal factors
- iv. Production cycle

OR

Explain the following as factors affecting the choice of capital structure:

- i. Cash flow position
- ii. Cost of equity
- iii. Flootation cost
- iv. Stock-market conditions

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Answer 1

Financial management refers to the efficient acquisition and distribution of funds of the company.

Answer 2

Feedback means the action performed by the receiver to convey to the sender that the message is received and clearly understood. Only when the sender receives a response does the communication process ends.

Answer 3

Debt is risky where payment of regular interest on debt is a legal obligation of the business. If the firm can manage a borrowed fund at a lower rate of interest, then it will prefer to have more of debt as compared to equity.

Answer 4

Internal sources of recruitment have a tendency to make employees lethargic, because employees are sure of time-bound promotions, hampering the spirit of competition among them.

Answer 5

Two characteristics of 'Organisational Climate' which influence the behaviour of individuals and act as a non-financial incentive:

- i. Autonomy of employee
- ii. Employee recognition

Answer 6

Two other specialised activities performed by Human Resource management:

- i. Recruiting personnel
- ii. Training and development for employees to improve their competence

Answer 7

In every organisation, there is a production process wherein the inputs are converted to the desired product or service. Management is required to ensure that production operations are performed smoothly.

Answer 8

Accountability implies that subordinates will be answerable for the final output of the task to his superior. It cannot be delegated or transferred and is enforced through proper feedback on task completion.

Answer 9

Technological environment includes technological changes and improvements such as new communication facilities. It may also get reflected in factors such as expenditure on R&D and rate of obsolescence.

Answer 10

A procedure is a sequence of steps to carry out different activities. These steps are established well in advance to handle future conditions.

Answer 11

Organisational structure refers to the framework within which managerial and operating tasks are performed. It specifies the relationship between people, work and resources.

Answer 12

Fatigue study determines breaks or intervals which are required during work. It is natural that if a worker works continuously, then fatigue sets in. This leads to reduction in efficiency. Every worker requires regular rest or breaks. According to Taylor, standard break timings must be provided to workers for improving performance.

Answer 13

- i. Labelling refers to providing information about the product in the form of a tag and graphic on the package of the product. It describes the product and specifies its components or other useful information such as the caution to be taken while using it and the procedure of use. Here, the company did not provide proper description on the usage of crackers, which may lead to accidents.
- ii. Values which were violated by the company are (a) Employing children, which is against the child labour law, and (b) Not protecting the safety of consumers.

Answer 14

Under the Consumer Protection Act, a three-tier machinery comprising the District Forum, State Commission and National Commission have been formed with the basic objective of consumer redressal.

Brief explanation of the three-tier machinery:

- **District Forum:** It is set up at the district level by the concerned state government. A complaint can be filed in the district forum if the value of goods, including the compensation claimed, is less than Rs 20 lakh.
- **State Commission:** It is set up at the state level by the state government. A complaint can be filed in the district forum if the value of goods, including the compensation claimed, is between Rs 20 lakh and Rs 1 crore.
- **National Commission:** It is set up by the Central Government. A complaint can be filed in the district forum if the value of goods, including the compensation claimed, is more than Rs 1 crore.

Answer 15

- Organisational policy:** If organisational policy controls the free flow of information, then it will become a barrier to communicate effectively.
- Rules and regulations:** Strict rules and regulations will create a barrier for effective communication in an organisation such as delay in action and movement of information.
- Organisational facilities:** In a large-scale operation, free flow of information is possible by facilitating social get-togethers or meetings and placing a complaint box. So, delay in action and movement of information occur only in the absence of such facilities.

Answer 16

- Treasury bills (T-Bills):** A treasury bill is a short-term borrowing instrument of the Government of India. It is a promissory note having a maturity period of less than one year. T-bills are issued by the Reserve Bank of India on behalf of the Central Government.
- Commercial papers:** Commercial papers are short-term unsecured money market instruments. Introduced in India in 1990, they are promissory notes which are negotiable and transferable. They have a maturity period ranging from a minimum of 15 days to a maximum of one year. They are primarily used by large and creditworthy companies for bridge financing.
- Call money:** Call money is a money market instrument which is used by commercial banks for interbank transactions. Commercial banks use call money for meeting their cash reserve requirements. In other words, through call money, commercial banks borrow from each other to fulfil any shortage of funds required to maintain the cash reserve ratio.

Answer 17

Consumer protection means educating consumers about their rights and responsibilities. It also suggests ways to redress their grievances and complaints. Important points of consumer protection from the point of view of consumers:

- i. **Ignorance of consumers:** In India, consumers are unaware about their rights and available reliefs; it becomes important to educate them about the same.
- ii. **Exploitation of consumers:** Sellers are engaged in exploitative and unfair trade practices to increase sales, implying the need for consumer protection.
- iii. **Unorganised consumers:** In India, consumer organisations and NGOs are few and not that powerful, implying the need for protecting consumers.

Answer 18

- i. According to Maslow's Needs Hierarchy Theory, the needs of an individual can be classified into five categories which can be arranged in a hierarchical order as physiological needs, security needs, belongingness needs, esteem needs and actualisation needs. Kavya realised that she was fulfilling only 'physiological needs' and 'security needs'. Physiological needs are the most basic needs in the hierarchy of needs. It comprises needs which are essential for survival and sustenance. For example, need for food, clothing and shelter. In terms of an organisation, the requirement of a basic salary is a physiological need. Security needs is that an individual requires physical and economic security. Kavya has a permanent job which ensures her complete security.
- ii. Two other needs of Kavya (followed by the above needs) which remain to be satisfied are 'belongingness needs' and 'esteem needs'.
 - a. Belongingness needs refers to the social needs of an individual in terms of affection and acceptance.
 - b. Esteem needs comprises elements such as respect, dignity and recognition in the peer group.

Every individual yearns for social acceptance and belongingness and also respects and acknowledgement in the peer group. In this situation, Kavya falls sick and takes leave, but no one showed concern and enquired about her health.

Answer 19

A business environment refers to the aggregate of external conditions, events and resources which are outside the control of a business but interact with it and affect its performance. For example, change in the taste and preferences of consumers, change in government policies, change in political scenario, change in legal polices, all make up the business environment.

Features of business environment:

- i. **Interrelated:** Different forces acting in a business environment are closely related to each other. For example, an increase in the income of consumers increases the demand for consumer durables (e.g. television or refrigerator).

- ii. **Ever changing:** The business environment is dynamic and ever changing. For example, consumer tastes and preferences, technology, government rules and policies change continuously.
- iii. **Complex:** The business environment is the aggregate of different interrelated and dynamic forces. Thus, it becomes difficult and complex to understand. For example, all political, social, economic, technological and legal matters affect the performance of an organisation simultaneously. While it may be easy to understand the individual affects of these forces, their cumulative effect is quite difficult to understand.

Answer 20

- (i) **Investment decisions:** A firm must decide where to invest the funds such that it can earn maximum returns. Such decisions are known as investment decisions. These decisions are taken for both long term and short term. (a) Long-term investment decisions affect a firm's long-term earning capacity and profitability. They are also known as capital budgeting decisions. For example, the decision to purchase a new machine or land. (b) Short-term investment decisions, also known as working capital decisions, affect the day-to-day business operations. For example, decisions related to cash or bill receivables.
- (ii) **Dividend decisions:** Dividend decisions involve decisions regarding how the company would distribute its profit or surplus. It can either distribute it to equity shareholders in the form of dividends or keep it in the form of retained earnings. Dividend decisions aim at maximising the wealth of shareholders while at the same time considering the requirements of retained earnings for the company.

Answer 21

- a. The objective of the management referred in the paragraph is 'organisational objective'. One of the important organisational objectives is to survive and exist in a competitive market for a long period. This becomes feasible only if the total income earned by an organisation should be able to cover the various costs incurred in its operation. Also it must grow and expand their activities.
- b. Two values conveyed by the organisation in this situation:
 - i. Providing employment in backward areas of the society
 - ii. Using environment-friendly methods of production

Answer 22

Training refers to enhancing the skills and abilities necessary for a specific job. In other words, it attempts at improving the aptitude and knowledge of employees according to the requirements of the specific job.

Benefits to the Employee

- i. **Better Career Opportunities:** Training helps in improving the knowledge of the employee which in turn helps in improving his career prospects.
- ii. **Earn More:** By helping individuals to improve their knowledge and skills, training improves the earning prospects of employees.
- iii. **Less Accident Prone:** With proper training, employees become more efficient in handling complex machines. This helps in reducing the chances of an accident.
- iv. **Self-confidence:** By increasing the knowledge, skills and aptitude of employees, training helps in boosting self-confidence, which in turn helps in improving job satisfaction.

Answer 23

Planning implies to a state in advance where to go and in which direction to move to achieve a target. Being a continuous process which helps in reducing the risk of uncertainty, planning provides the rationale for undertaking policies in the direction of achieving goals. It is based on anticipating the future course of action and deciding the best course of action.

Features of planning:

- i. **Focus on objectives:** Planning starts when an objective is set. A proper planning method gives a boost to a well-organised and goal-oriented management. Plans ensure that the desired objective is attained economically and quickly. Managers must make sure that plans made are purposeful, specific, realistic and clear and should adhere to the company's strategies, procedures and policies. For example, if a sales target is to be achieved, then plans must align with this objective.
- ii. **Acts as a stepping stone:** A goal is achieved through planning, organising, staffing, directing and controlling. Planning thus serves as the stepping stone for all other functions of an organisation. The remaining functions are conducted within the framework of the plans drawn, i.e. the other functions are interrelated and interdependent on planning. Thus, planning acts as the primary function for all organisations.
- iii. **Pervasiveness:** Planning must be done at all levels of management and in all departments of the organisation. However, its scope differs along the various dimensions of business levels. For example, top-level managers have to chalk out policies regarding overall management, whereas middle-level managers plan the authority to be assigned to subordinates or departmental planning. On the other hand, lower level managers have to perform day-to-day operational planning and make out small targets.
- iv. **Continuity:** After an objective or goal is achieved, the plan drawn for it does not cease to exist but goes on to become a never-ending strategy because of the dynamic nature of the business environment. It is a continuous process—after or within the plan period, a need arises for the formulation or modification of another

plan, keeping in view the new objectives and circumstances. It is a continuous process all along the life of a business enterprise.

- v. **Choice making:** After coming up with all possible alternatives and its outcomes, managers need to evaluate them. This evaluation is based on the utility and consequences of the options and the performance study of various actions. Various factors will be weighed against each other as they must assess the pros and cons of each alternative.

Answer 24

Physical distribution is the transfer of products from the place of production to the place where they are finally consumed. Components of physical distribution:

- i. **Processing of Order:** Processing of order implies the activities which occur between the placement of order and the final delivery to the consumer. It comprises steps such as placement of order, intimation of order to the manufacturer and delivery of goods. The system of distribution should be such that the processing of order is speedy. Speedy processing with sufficient accuracy leads to greater customer satisfaction.
- ii. **Transportation of Products:** Transportation of products implies physical transfer of goods from the place of manufacturing to the place of actual consumption.
- iii. **Warehousing:** Warehousing implies storing the goods before they are finally sold to consumers. Storing of goods at the warehouse enables ready availability of goods at different locations as and when required. However, warehousing involves costs as well. Thus, the benefits of warehousing must be weighed against the costs involved so as to maintain a balance according to the requirement.
- iv. **Maintenance of Inventory:** Maintaining inventories enables timely supply of products as and when required. Similar to warehousing, maintenance of inventory also involves a cost.

Answer 25

Two principles which are mentioned in the paragraph:

- i. **Development of each and every person to his or her greatest efficiency and prosperity:**

According to Taylor, the overall efficiency and productivity in an organisation depends on the competency of individual employees. Accordingly, to improve the overall productivity and efficiency, the working capabilities of employees must be improved. If the efficiency of workers improves, then they will be able to increase their contribution to the organisation's development. They should initiate new ways and incentives to develop their competitiveness. They should

be assigned work according to their mental/physical qualities. For this, they must be given proper training and education.

ii. **Division of work:**

Work should be divided into small parts to ensure that execution occurs competently. A particular unit of work is assigned to an individual based on ability because he or she may not be comfortable to execute the entire process. So, when an individual works continuously on a particular task, he will become specialised in that task. Therefore, he will become an expert in the routine work assigned by the superior.

Answer 26

Basis	Capital Market	Money Market
(i) Safety	Securities traded are risky with regard to both return and principle repayment.	Securities traded are safe as securities are traded for short duration and the issuers are financially sound.
(ii) Expected return	Offer higher possibility of gain as securities are for a longer period.	As securities have a shorter maturity period, the expected return is lower.
(iii) Investment outlay	Low-value securities, i.e. securities of values Rs 10 and Rs 100.	High-value securities, i.e. the minimum amount of call loan is Rs 10 crore.
(iv) Participants	Financial institutions, commercial banks, corporates, foreign investors and public.	RBI, commercial banks, financial institutions and financial companies.
(v) Duration	Long-term and medium-term securities with a maturity period of more than a year.	Instruments have a maturity period of maximum one year.

Answer 27

Controlling refers to making sure that various activities and tasks in an organisation are performed according to predefined goals and objectives.

Points highlighting the importance of controlling in an organisation:

- i. **Achieving goals:** Controlling ensures that various activities are carried out correctly according to plans. It ensures that deviations if any are identified and appropriate corrective action is taken.
- ii. **Reviewing standards:** An effective control system ensures that the standards are set accurately. As the business environment changes, it ensures that the standards are reviewed so as to adapt to the changes taking place.
- iii. **Enables efficiency in resource utilisation:** An effective control system ensures that there is minimum wastage of resources. In other words, it ensures that the resources are used optimally and in the most efficient manner.

- iv. **Better motivation:** With controlling, employees know what is expected from them and how their performance would be evaluated. This clarity motivates employees to perform better.

OR

Controlling is closely related to planning. A good control system requires set standards for evaluation. These standards are provided by the plans defined by the organisation. In other words, plans serve as the base for controlling.

Controlling is essential for effective implementation of plans. It is essential to keep a close watch on the plans, identify any deviations and take appropriate corrective actions. Without proper controlling, planning would be futile.

In a similar manner, planning forms the base for controlling. Without planning, there would be nothing to control. Controlling is done only when there are predetermined standards for evaluation.

While planning involves intellectual thinking, decision making and deciding a course of action, controlling ensures that plans take the required course of action.

Both concepts of planning and controlling are interlinked as they are forward looking and backward looking. Planning is a process wherein it is decided what is to be done and accordingly deciding the required course of action. In other words, planning involves deciding the goals and objectives which are to be achieved and deciding the actions through which they are to be achieved. In this way, planning helps in predicting future actions; thus, it can be said to be looking ahead.

As against planning, the controlling function involves assessing and evaluating past performance against pre-defined standards. As controlling assesses past performance, it can be said to be backward looking.

However, it must be remembered that planning decides the goals and actions for the future, but these decisions are taken on the basis of experience and previous controlling actions. Thus, planning involves looking back as well.

In a similar manner, controlling not only involves assessing past performance but also decides the corrective actions to be taken (in the future) and forms the base for plans. Thus, the controlling function looks forward as well.

Answer 28

Functions of marketing:

- i. **Market planning:** Creating a market plan to achieve marketing goals and objectives of the organisation. Market research is conducted to analyse the preferences of customers to formulate a suitable plan.
- ii. **Product designing and development:** With the help of designing, customers are able to identify the product. It can also be used for promoting the product. It can be used for attracting customers towards product purchase. Proper packaging also helps in

- protecting the product from spoilage and breakage.
- iii. **Standardising and grading:** It enables grading of the product in various categories. For instance, different features of the product are specified on the label. For example, a brand of ice cream comes in different flavours.
 - iv. **Pricing of the product:** Price refers to the amount of money which is paid by a consumer to obtain a product. Price is the most important factor determining the demand of a product. Demand for a product shares a negative relation with its price. Marketers must suitably decide a price by properly analysing the various related factors such as target customers, pricing range of competitors and goals of the firm. The price which is set must be at par with the value offered by the product. In addition, the firm must offer suitable discounts, offers or incentive schemes.

OR

There are different views with regard to expenditure on advertising. On one hand, it is considered a social waste as it adds to the cost of production, weakens social values and adds to consumer needs and desires. On the other hand, it is beneficial as it helps in enhancing the sales of the product of the firm.

Points objecting advertisement:

- i. **Higher Cost:** Expenses on advertisement add to the cost of the product and the firm, and these are then passed on as additional cost to consumers in the form of higher prices. However, advertising helps in attracting consumers to the product. Accordingly, the demand for the product increases. To cater to the increased demand, production increases. An increase in production in turn lowers the per unit cost of production.
- ii. **Creates Confusion:** Advertisements of a large number of similar products often confuse consumers. In contrast, advertisements help in increasing the knowledge of consumers with regard to the availability of different products in the market. In this way, it increases their choice and helps them in making an informed decision with regard to product purchase.
- iii. **Promotes Inferior Goods:** Advertisements induce consumers to purchase the product. Even inferior goods can be advertised, and their demand be induced. However, it is said that quality is only a relative product. Advertisements provide knowledge with regard to all kinds of products. Whether to purchase the product or not is up to consumers themselves.
- iv. **Objectionable Advertisements:** Sometimes, advertisements can be objectionable in the sense that they undermine social values. For instance, in certain advertisements, women are shown in an objectionable manner. Sometimes, the language, images and content of the advertisement may not appeal to society at large.

Answer 29

Basis for Difference	Formal Organisation	Informal Organisation
Meaning	Organisational structure designed by the management to accomplish a particular task. It specifies the boundaries of authority and responsibility, and there is systematic coordination to achieve organisational goals.	Interaction among people at work gives rise to a network of social relationships among employees. It emerges from within the formal organisation when people interact beyond their officially defined roles.
Origin	Originates from the rules and policies of management.	Originates from social interactions among employees.
Authority	Based on profile and managerial positions, i.e. flow from top to bottom.	Based on personal qualities of employees, i.e. flows from all directions.
Behaviour	Complete control on the behaviour of employees as it is decided by managers.	No control on the behaviour of employees as managers will not interfere with the behaviour of employees unless it results in a negative impact on the organisation.
Duration	More stable and hence exists till the survival of the organisation.	Not stable as employees can frequently change the social group.
Nature	Completely rigid.	More flexible.

OR

Decentralisation refers to the delegation of authority and power to the lower level in the hierarchy. It is optional in the sense that it is up to the organisation to decide how much authority and power it wishes to delegate to the lower levels. Points explaining why an organisation would choose to be decentralised:

- i. **Initiative:** Decentralisation provides managers the freedom and authority to take their own decisions. In this way, it gives them opportunities to take initiatives. This helps managers to develop self-confidence.
- ii. **Managerial Competence:** Decentralisation provides personnel the opportunity to gain new experience and develop their skills. This helps in improving their competence. In this way, it helps in the development of future managers who can take greater responsibilities.

- iii. **Control:** With decentralisation, the performance of various departments can be evaluated better. The contribution of each department towards the overall objectives can be easily analysed.
- iv. **Active Decision Making:** Decentralisation enables decision making at the nearest point of action. This ensures quick decision making.
- v. **Growth:** With decentralisation, the responsibility is passed on to the lower levels in the hierarchy. This motivates them to work to their best, improving their competence and efficiency. Accordingly, overall performance and growth of the organisation are enhanced.
- vi. **Reduced Workload of Top Managers:** With decentralisation, a part of the responsibility of top-level managers is passed on to the lower management. Accordingly, top managers can focus on other priority areas, while lower managers handle the routine work.

Answer 30

Working capital refers to current assets which help in day-to-day business operations.

- i. **Nature of business:** A company which deals in trading or services will require low working capital because it manages a small operating cycle and absence of processing. On the other hand, a company managing a large operating cycle will require high working capital as the conversion of raw materials into finished product before the end of sale transaction.
Manufacturing organisations ⇒ High working capital
Trading/Service organisations ⇒ Low working capital
- ii. **Scale of operations:** A company which is operating in a large-scale of operations will require larger fixed assets in the form of plants, land and building.
Larger organisation ⇒ Higher investment in fixed assets
Small organisation ⇒ Lower investment in fixed assets
- iii. **Seasonal factors:** A company selling seasonal products will require high working capital to meet higher sales, higher production, higher stock and more debtors. While a company selling goods throughout the season will require constant working capital which is low working capital spread throughout the season.
Peak season ⇒ High working capital
Lean season ⇒ Low working capital
- iv. **Production cycle:** A longer production cycle will require high working capital as it will take more time to convert raw material to finished products. On the other hand, a small production cycle will require less working capital.
Long production cycle ⇒ High working capital
Small production cycle ⇒ Low working capital

OR

Capital structure is the proportion of debt and equity used for financing business operations.

- i. **Cash flow position:** The cash flow position should match with the obligation of making payments because a company which fails to make payments will face insolvency. So, a company employs more debt securities in its capital structure if it is sure of generating enough cash inflow. On the other hand, if there is less cash, then a company should use more equity in its capital structure.

Strong cash flow position ⇒ More debt

Weak cash flow position ⇒ More equity

- ii. **Cost of equity:** In terms of dividend payments, higher the cost of equity, lower is its proportion in total capital.

Use of debt increases ⇒ Financial risk increases ⇒ Expectation of rate of return increases ⇒ Difficult to opt for equity ⇒ Equity cost increases

- iii. **Flotation cost:** Costs involved in raising funds from various sources will affect the selection of the capital structure by a company.

Higher flotation cost involved in raising funds from a particular source ⇒

Lower proportion of that source in capital structure

- iv. **Stock-market conditions:** It is easy to opt for equity during a boom and difficult to opt for equity during a recession.