1.2C: Types of Organisation: Activity Answers

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1.2 TYPES OF ORGANISATION: ANSWERS TO ACTIVITY C

Read the case study information below and answer the questions that follow.

BANGALORE ENTERPRISE BLOSSOMS

Sonali Singh's enterprise started small, very small. Tending a small flower garden on her family's small holding, she harvested and sold seasonal flowers when they were available in the business district of Bangalore. This sideline earned her family precious but infrequent supplementary income.

In 2005 her luck changed. A 1000 rupee (approximately US$25) microcredit loan and technical assistance from a non-governmental organisation (NGO) enabled her to purchase a range of flower seeds that enabled her to provide different flowers all year round. Over the next few years she gathered and shared these flower seeds with her family and local community. In return, additional plots of community land were given over to the enterprise and small capital investments were made (e.g., the construction of several commercial scale glass houses). In 2007 the Katuri Networks cooperative was formally established by Sonalli and 45 members of the local community.

Surpluses from the cooperative have been retained and reinvested at considerable risk, but their confidence in the growth of 'flower giving' at times of major festivals encouraged others to invest in the cooperative too. The cooperative sold the flowers in India, but their business also became one of the first in India to start exporting flowers on a large scale and has grown at a tremendous rate. Katuri Networks recently bought out a large rose grower in Kenya and the business is now the world's largest cultivator of roses. All of which has been achieved in just ten short years.

*Source: www. **Business**Management**IB**.com*

1.2C: Types of Organisation: Activity Answers

25 marks, 45 minutes

1. **Define the following terms:** **[4 marks]**

   i. **Cooperative**

Firm owned, controlled, and operated by a group of users for their own benefit. Each member contributes equity capital, and shares in the control of the firm on the basis of one-member, one-vote principle (and not in proportion to his or her equity contribution).

   ii. **Micro-finance provider**

An individual or organisation that provides microfinance – a division of financial services that focuses on empowering and providing lower income individuals with the necessary means to become self-sufficient and creditworthy. The loans provided to these individuals are typically small, but may be just enough to bring them into a higher class.

2. **Explain the likely objectives of a non-governmental organisation providing technical assistance and expertise to Indian farmers.** **[5 marks]**

- Some NGOs target education, particularly among women and girls. Educating women in the technical and financial aspects of farming would empower them and their families.
- Many NGOs attempt to reduce poverty in developing nations. Developing farming practices to the point where families can be become self-sufficient farmers and even produce surpluses which can be bartered and traded for additional income would reduce Indian rural poverty.
- Human rights NGOs work to minimise the issues that cause certain groups to become marginalised. Perhaps lower cast rural groups are excluded from seed and produce markets in Indian society. NGOs may be working to break down those barriers and facilitate equal access to capital and technical knowledge for all.
- The goal of some NGOs (including Amnesty International) is promoting human rights, including proper access to justice. Land rights, access to subsidies and legal rights may be part of the technical training provided to farmers.
- NGOs can be dedicated to preserving land, cleaning up environmental hazards or education.
- NGOs might using micro financing to award small business loans to various entrepreneurs to raise out of poverty.
- NGOs might focus on providing better living conditions for people living in poverty. Allowing families to grow more food could go some way to lifting people out of poverty.

3. Evaluate the use of the cooperative legal structure in the case study. [8 marks]

Cooperative are a type of firm that is owned, controlled, and operated by a group of users for their own benefit. Each member contributes equity capital, and shares in the control of the firm on the basis of one-member, one-vote principle (and not in proportion to his or her equity contribution). NB. Whereas partnerships are limited to 20 partners in most countries, cooperatives can have thousands of members.

Common types of cooperative include:

- Financial cooperatives, for example, credit unions are a type of cooperative banking institution that provides banking and lending services to its members.
- Housing cooperatives own real estate, such as condo projects and apartment buildings. Worker's cooperatives are owned and governed by the employees of the business. They operate in all sectors of the economy providing workers with both employment and ownership opportunities.
- Producer cooperatives, for example, retail cooperatives involve small retailers banding together to be more competitive with large retailers by sharing advertising costs and buying as a group for high volume discounts. The cooperative in the case study is a producer cooperative.
- Consumer cooperatives are owned by the people who buy the goods or use the services of the cooperative. Consumer co-ops may sell consumer goods such as food, or provide housing, or electricity. Other co-ops such as community crèches provide childcare services.

Advantages:

- Easy to form
- No obstruction for membership
- Limited liability
- Service motive (e.g., members are working for the good of the cooperative and not already wealthy shareholders)
- Democratic management
- Stability and continuity
- Economic operations (e.g., economies of scale –purchasing economies may be achieved)
- Surplus shared by the members

Disadvantages:

- As cooperatives are formed to provide a service to their members rather than a return on investment, it may be difficult to attract potential members/shareholders whose primary interest is a financial return.
- There is a usually a limited distribution of surplus (profits) to members/shareholders and some cooperatives may prohibit the distribution of any surplus to members/shareholders.

- Even though some shareholders may have a greater involvement or investment than others, they still only get one vote.
- Active and direct involvement of members/shareholders in the cooperative.
- Requires continuous cooperative education programs for members.
- Management may be inefficient as many cooperatives are managed by their non-specialist members. Further, strategic decisions may require the vote of a membership quorum.

The cooperative legal structure has worked very well in establishing Katuri Networks from its humble origins into the thriving business that is today. This is largely because the workers and owners of the firm have such a vested interest into working hard and making it succeed. The workers in the cooperative share in the financial success of the cooperative. An argument could be made for changing the legal structure, but this would be dependent on the objectives of KN and how large its growth ambitions are. A private limited company may offer a more familiar face to the business on which financiers could better evaluate the business. And, if rapid growth was to be financed, then a public limited company structure would enable significant capital to be raised in a share flotation.

However, KN is currently working well as a cooperative, and cooperatives can be large and profitable if good management is in place and following a good business plan.

4. Explain the nature of the for profit social enterprises mentioned in the case study – micro-finance providers and cooperatives. [8 marks]

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Ownership and Control: Each member contributes equity capital, and shares in the control of the firm on the basis of one-member, one-vote principle (and not in proportion to his or her equity contribution).

Management: The cooperative is managed by its members.

Capital: Each member contributes equity capital, owns shares in the organisation and is paid dividends out of profits in addition to their usual remuneration

Sources of Finance: Equity capital from cooperative members, retained profits and long-term bank loans.

Legal status: A cooperative is a legal entity owned and democratically controlled by its members. Cooperatives may take the form of companies limited by shares or by guarantee, partnerships or unincorporated associations.

Liability of owners: The liability of the owners is dependent on the form of organisation: limited liability companies, partnerships or unincorporated associations.

Microfinance is defined as financial services for poor and low-income clients, especially microcredit, offered by different types of service providers. In practice, the term is often used more narrowly to refer to loans and other services from providers that identify themselves as 'microfinance institutions' (MFIs). These institutions commonly tend to use new methods developed over the last 30 years to deliver very small loans to unsalaried borrowers, taking little or no collateral. These methods include group lending and liability, pre-loan savings requirements, gradually increasing loan sizes, and an implicit guarantee of ready access to future loans if present loans are repaid fully and promptly.

More broadly, microfinance refers to a movement that envisions a world in which low-income households have permanent access to a range of high quality and affordable financial services offered by a range of retail providers to finance income-producing activities, build assets, stabilise consumption, and protect against risks. These services include savings, credit, insurance, remittances, and payments, and others.

How do borrowers use microcredit loans? Many microcredit borrowers have microenterprises – unsalaried, informal income-generating activities. However, microloans may not predominantly be used to start or finance microenterprises. Scattered research suggests that only half or less of loan proceeds are used for business purposes. The remainder supports a wide range of household cash management needs, including stabilising consumption and spreading out large, lumpy cash needs like education fees, medical expenses, or lifecycle events such as weddings and funerals.

Most MFIs started as not-for-profit organisations like NGOs (non-governmental organizations), credit unions and other financial cooperatives, and state-owned development and postal savings banks. An increasing number of MFIs are now organized as for-profit entities, often because it is a requirement to obtaining a license from banking authorities to offer savings

services. For-profit MFIs may be organised as non-bank financial institutions (NBFIs), commercial banks that specialise in microfinance, or microfinance departments of full-service banks.