

# BUSINESS ECONOMICS I.

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**BEFEKTETÉS A JÖVŐBE**



# **BUSINESS ECONOMICS I.**

**Gabriella Soós**



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## **1. INTRODUCTION**

### **1.1 OBJECTIVES, COMPETENCIES THE CONDITIONS OF COMPLETING THE SUBJECT**

#### **1.1.1 Objective**

The objective of Business Economics subject is to get the student to know the most important tasks of starting and operating enterprises. Business Economics I. includes the basic knowledge, notions, connections belonging to the topic. The student will learn the details of corporate activities studying Business Economics II

In the course of this the students will learn the notion, essentials, the purpose of starting and the operation of the enterprise. They will place the enterprises in the economic system, and attain the effect of enterprises and the factors affecting them in the operation of the economy. They will systematize and list the main types of enterprises. their main attributes, the advantages and disadvantages of the particular types. They will be able to tell the life-cycle elements of the enterprise, the attributes of the particular elements. They will explain the cases and conditions of starting, transforming and terminating enterprises. They will be able to compile the business plan of the enterprise at the start of the enterprise, or to support an investment decision. They can define the role and factors of success in the life of the enterprise. They can explain the basics of entrepreneurial approach, its guiding principles, and the methods of shaping this approach. The students will get to know the life-cycles of enterprises, and the attributes of the particular life-cycles. They will attain the main criteria, functions, tasks of management, and also the importance of knowledge and of the human capital in the life of the enterprise. Finally, they will learn the main points and types, and the role of innovation,

#### **1.1.2 Competencies**

After attaining the subject students will be able to have a good grip of the basic processes of the given enterprise, to make suggestions for the changes in connection with them.

In their professional area, the students will be able to establish an enterprise, organization of their own, to control an organizational unit. The students will sense the current tasks of the life-cycle in connection with the establishment and the operation of the enterprise. They will recognize the areas requiring planning, research and analysis in

proportion to the given life-cycle of the enterprise. They will strive for recognizing the opportunities and abilities necessary to achieve the goals of the enterprise.

Through life-long learning, they can develop themselves, and can build a career. Using their theoretical and methodological knowledge, they can also research resources independently, follow scientific results, reveal and systematize facts, make critical analysis concerning the life, processes and innovation of enterprises, with the help of ICT tools. The students can form an independent standpoint based on an analysis of their own, and also defend it in a debate about getting acquainted with and analyzing the processes of an enterprise, in the course of disclosing and systematizing the wide range of facts and problems. They can use the newly attained knowledge to formulate new conclusions, genuine ideas and solution methods, which concern the organization and processes of the enterprise, or a certain part area of operation. They can formulate strategies to solve problems in connection with managing the enterprise, work out solutions, make decisions. They can make professional summaries, analyses, evaluate processes and results, make presentations, and take part actively in professional debates.

They are open to attain new norms, principles and other knowledge concerning the operation of the enterprise, initiates keeping continuous track of them.

### **1.1.3 Conditions of completing the subject**

Completing Business Economy I is a pre-condition to doing Business Economy II.

To complete the subject the students are supplied with obligatory and recommended literature, which is important to effectively attain the subject, so that the students can successfully apply their knowledge in their work. The video material in the curriculum is strongly connected to the theoretical curriculum, recognizing connections is highly important.

The internet references in the units serve as support with examples for the theoretical material, and also help to memorize them.

The condition of completing the subject is to write a successful test, which is only acceptable if 50% + 1 point is achieved.

## 1.2 THE CONTENT OF THE COURSE (FROM 1 TO 15) (2-13 CORPUS)

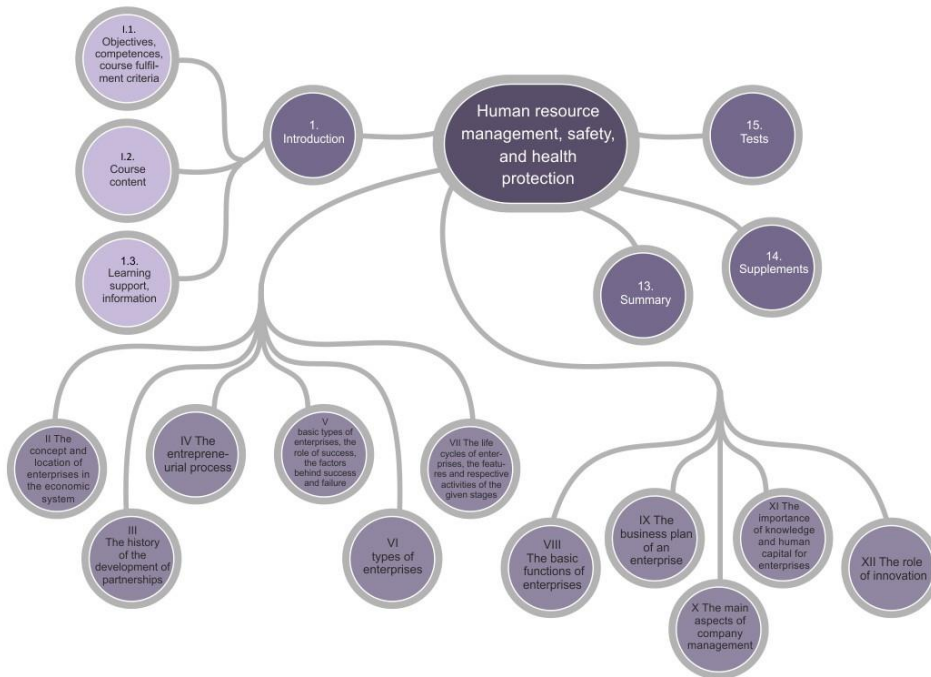


Figure 1: The content of the course

### 1.3 LEARNER ADVICE, INFORMATION

You can read the objective and the build-up of the lesson at the beginning of it. The introduction of the theoretical material comes next. At the end of each lesson we sum up the most important information discussed through the lesson, and with testing questions we help with the preparation for the test. You can test your knowledge with the trial tests belonging to the lessons.

Through the subject you will encounter video materials, animations, which help attain the theoretical material. However, I call your attention that tasks may be connected to them. So when you are learning, pay attention to them just as thoroughly as to texts.

Internet references are attached to the information presented. They demonstrate, complete the studied material, and enhance their understanding and applying it in practice. So we suggest that you find the

articles, studies, reading materials referred to, save them on your computer, so that you can get back to them later.

Using the entries of the lessons you can search for case studies, examples on the internet on your own.

Observe the enterprises of your family, friends or acquaintances, or find well-known enterprises, and examine them to find out how the subject matter you studied work at the selected company.

Should you have any more questions when learning the lessons, find the lecturer of the subject, or use the forum or chat.

We wish you success with learning this subject!

## 2. LESSON: THE NOTION OF ENTERPRISE, ITS PLACE IN THE ECONOMIC SYSTEM

### 2.1 OBJECTIVES AND COMPETENCIES

In this unit the students get to know the basic concepts of enterprises, the motivation and the reasons for establishing enterprises. After learning this unit the students will be able to define the concept and the basic points of enterprises, the purpose of starting and operating them. They can place the enterprises in the economic system.

The students will be able to assess the limiting factors of starting an enterprise in their professional area. They will be aware of people, institutions and groups affected by the enterprise, and will be able to assess their interests. The students will get to know the main risk factors concerning the enterprise and the basics of possible risk management strategies. They can present the role of the SME sector in the economy.

### 2.2 CURRICULUM

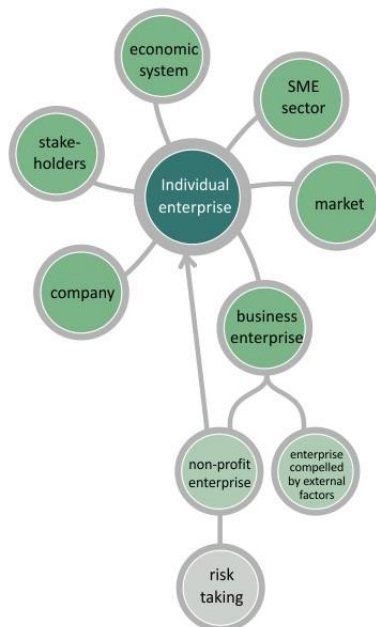


Figure 2: Concept map

### **2.2.1 The reasons for establishing enterprises**

The expression 'enterprise' has become an everyday general notion. It is used often, and with several meanings, however, also in the economic sense the basics of its establishing and operation can be approached differently. As for a start, let's see why, for what reason is an enterprise established. The reasons for establishing one are as follows:

1. The owner(s)/founder(s) – the entrepreneur(s) – own(s) infrastructure, means, financial background, and/or expertise which make it possible to independently carry out an activity, or manufacture a product.
2. They want to make decisions and take responsibility on their own.
3. The entrepreneur has an idea which can be freely realized this way.
4. Enterprises started by force.
5. To make bigger profit (compared to income earned as an employee).
6. To satisfy recognized market demand.

Forced enterprises are the organizations whose operation was started in the shape of an enterprise, because the owners didn't have the possibility to work as employed workers (they were unemployed), so the founders want to make a living as entrepreneurs.

Out of the reasons mentioned above several might motivate people to establish enterprises at the same time.

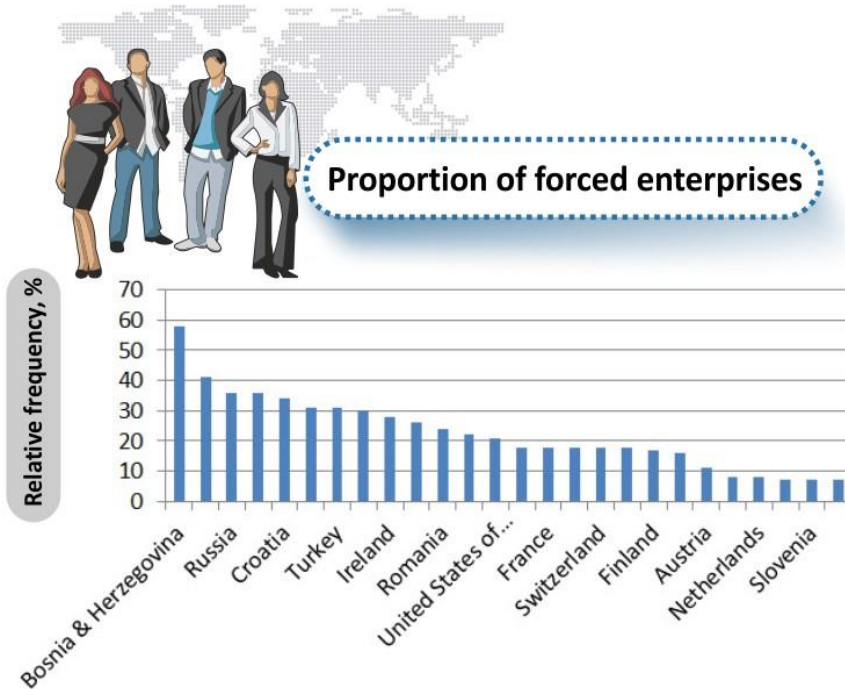


Figure 3: The proportion of forced enterprises in the particular countries<sup>1</sup>

### 2.2.2 The notion of enterprise, or What does an enterprise embark on?

Enterprises in general take up some kind of economic activity to achieve profit, and to satisfy consumer demand.

- ☞ **A business enterprise is a human activity the basic purpose of which, the main point of existence is to satisfy consumer demands and to achieve profit at the same time.**
- ☞ **The company is the organizational frame of busines enterprises: in modern societies a legally circumscribed structure in which the activities to achieve the basic goal are carried out.<sup>2</sup>**

<sup>1</sup> Source: Based on data of Global Entrepreneurship Monitor 2013, edited on our own

<sup>2</sup> Chikán Attila: Business Economics Aula Kiadó Budapest, 2008.

The main attributes of an enterprise are as follows:

- making a profit in the course of the activity
- satisfying relevant consumer demands
- independent decision making in the course of operation (complying with the legal framework)
- risk taking
- influencing the market directly or indirectly, intentionally or unintentionally

It is to be remarked that there is a possibility to establish so called non-profit enterprises, (bubble: the primary aim of non-profit enterprises is not generating profit, but realizing the undertaken activity in the frame of sensible business, - costs are covered by income – and independent of this profit can be made, but it can't be divided between the membrs as dividend.) in which case, originating from the nature of activity (e.g. welfare services) achieving a profit is not a goal (but it's not excluded).

It is important to mention, that more and more often we can hear about so called startup enterprises.

**Startup enterprises are newly established, innovative enterprises having great growth potential, aiming primarily at international markets, and which continuously develop their business model.**

These enterprises continuously develop their organization by applying state-of-the-art management principles to be able to meet the demands for fast growth. Characteristically, they have a patent of their own, and the continuous development of them, and developing new ones is a continuous goal, the condition to remain competitive globally.

### **2.2.3 The place of enterprises in the system of economics**

**Enterprises** are the production units of the economy. They supply resources for production (e.g. machines, real estate, labor force, capital) with the help of which they produce products, services.

In the economic processes enterprises are in strong relationship with **households** consisting of private individuals. Households offer their labor force, abilities, experience to the enterprise, so they supply resources for production. On the other hand, they mean demand for the products of enterprises, because they buy them to satisfy their needs (e.g. food, clothes). Companies which make use of the work done by households give them a salary for this, which creates a base for the



consumption of households. Thus the two spheres shape economic processes in close co-operation.

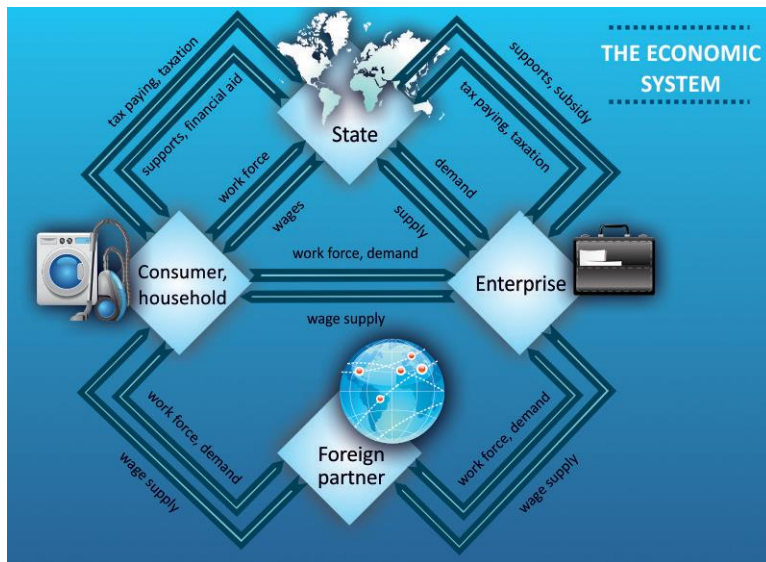


Figure 4.

The **state** is also part of the economic system. In modern market economies the state doesn't control the other players of economy directly, but just indirectly, by legal, financial and other norms (e.g. legal regulations, central bank base rate). It collects taxes from the players of economics, and divides the generated income in the form of subsidies, social aid. The state means demand for the companies because it buys products, services to operate the governmental system, at the same time, it requires labor force from the households and pays for the work done. The 'foreign countries' are interpreted as connected economy, where households can offer their labor force to, and they can receive payment from, and also where they can buy products, services from. The relationship of companies with the foreign countries is similar to the one with domestic players.

The actors of the economic system act driven by their interests. In the case of consumers, satisfying their demand is the aim, and also they have to create the financial and other conditions to achieve it. The goal of enterprises is to operate on the long run and to make a profit needed. The aim of the state is to operate the economy efficiently.

### 2.2.4 The market

The players of the economic system 'meet' in the 'market'. Enterprises offer their products, which the consumers buy here.

☞ **The market is the system of actual and potential sellers and buyers, the main factors of which are demand, supply, price and earnings.**<sup>3</sup>

At the start, or when developing its activity, an enterprise enters a given market. This process is not simple, because a lot of limiting factors have to be considered which cramp the sale of products, providing services, or the beginning of the activity. These factors may be as follows<sup>4</sup>:

1. State ruling
  - a. legal regulations (e.g. regulations concerning particular economic partnerships)
  - b. health regulations (e.g. permission issued by the National Public Health and Medical Officer Service to food shops)
  - c. technological requirements (e.g. regulations of environment pollution)
  - d. patent protection (pl. protected inventions, licenses)
  - e. subsidies, favors granted, restrictions
  - f. customs duties, etc.
2. Size economy
  - a. size of the enterprise: entering a market owned by big size companies (e.g. mobile phone service) is practically impossible
  - b. plant size: how much should be produced so that costs could be compensated for
  - c. market share: how big market share can the company get
3. Product differentiation
  - a. creating a range of products satisfying consumer demand
  - b. differentiating products from those of competitors
4. Limits of capital

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<sup>3</sup> Kopányi Mihály: Microeconomy KJK-Kerszöv Jogi és Üzleti Kiadó Kft. Budapest, 2004. 10. o.

<sup>4</sup> Chikán Attila: based on Business Economics Aula Kiadó Budapest 2003. 89-94. o.

- a. at the start of the enterprise a certain capital has to be provided for the operation, which will only be refunded later
5. The costs of access to the distribution channels
  - a. companies already in the market make it more difficult for new players to enter
  - b. traders have to be convinced that the entering new product is worth taking the risk by traders
6. Channeling into trade often has costs (listing, shelf charge)
7. Other entering obstacles
  - a. lack of experience (e.g. purchasing sources are expensive)
  - b. social requirements, resistance (noisy activity placed in neighborhood)

### 2.2.5 The stakeholders of enterprises<sup>5</sup>

Through the course of achieving its aim, the enterprise gets into connection with different types of organization or individuals, and its activity affects them. We call those people and organizations players of enterprises who the enterprise gets in touch with, and who are affected by the operation of the enterprise.

#### 2.5.5.1. Internal stakeholders

The *internal stakeholders* mean the players directly participating in the activity of the enterprise, and who belong to the organization.

The **owners** invest capital in the operation of the enterprise, hoping to increase their wealth as a result of successful operation. Their risk is that in a case of failure they might even lose their investment. The owners usually intervene in the control of the company by defining strategic principles, aims. The relationship of the owners to the company might change if they are planning to sell it.

The **managers** control the concrete activity of the enterprise according to the owners' guidelines. They make long and short term decisions in the interest of continuous, successful operation. They maintain a close relationship with the company. Their reputation,

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<sup>5</sup> Chikán Attila: Based on Introduction to Business Economics (Aula Kiadó Budapest, 2006.)

prestige, and in a concrete case their salary, too, depends on the success of the company. Their goal is to increase the value of the enterprise, to make as big a profit as possible, to create the conditions for the stable operation on the long run. We have to highlight the social responsibility of managers, too, since the success of the employees also depends on their activity.

The **employees** carry out the different work activities of the enterprise according to the managers' control. The quality of their work significantly influences the final outcome. They can't really influence decision making, so their relationship with the company is not that strong. Their primary aim is to make a calculable income on the long run. They find it also important how interesting the work to be done is, if they have a chance of promotion, and what the quality of their social contacts is like..

As for the income, there is a clash of interests between the employer and the employee. The employee wants to get a bigger salary, this means cost to the employer, who is interested in decreasing it. At the same time, the common interest of the internal players is to maintain the successful operation of the enterprise on the long run.

#### *2.5.5.2. External stakeholders*

*External stakeholders* are those who don't influence the processes of the enterprise directly, but with their decisions they indirectly affect the operation.

The main player for the enterprise is the **consumer**, since with its products, services it tries to satisfy the consumer's demands to the largest possible extent. So the consumers buy the product, if they are satisfied, it will influence their future purchases and they can be made brand loyal. The consumer wants to maximize the usefulness of the product or service when consuming it. The consumers' satisfaction is the measure of value concerning the success of the enterprise.

With the **suppliers**, the situation is just the other way round. There the enterprise buys the product or service from the supplier. So their aim is a long term co-operation with the enterprise, which makes their decision making in the future calculable. For the enterprise, however, it will give a base for same quality production, and the formed relationship helps adapt flexibly to the changing market requirements.

The company competes with **competitors** to gain an identical or similar consumer circle. Thus they share the possibly achievable profit, on the other hand, they force each other to continuously improve by satisfying the consumers' demand better than the other, or to create need.

The **strategic partners** are companies which carry out an activity partly identical, or similar to theirs, so in the case of certain activities co-operation may realize in mutual results, or the relationship is fixed in the long run (e.g. with suppliers, buyers). Strategic co-operations boost the efficiency of the activity of the enterprise, make operation more calculable, so creating and maintaining one is important for all parties.

**State institutions** take part in the regulation of the economy, thus they affect the operation of the enterprise. They determine the restrictions of entering and operating on the market, they collect taxes and other charges, and provide subsidies. Besides, they are involved in handling public tasks (police, public lighting, etc.)

**Local and voluntary civil communities** mean the civil sphere, that is those organizations which are often made at local level, and their purpose is to improve the social, public, environmental, religious, etc. situation. In the course of the company's activity it can support these organizations, so to improve the respect of the enterprise, or its acceptance by the public.

The enterprise is located in a **natural environment**, it makes use of its potentials (e.g. natural resources). Modern business management, however, recognizes that the amount of natural resources is limited, so saving them is also the responsibility of the enterprise. Environmental protection principles are more and more built into the requirements of the consumer, so the enterprise has to pay better and better attention to keeping to these principles.

### 2.2.6 Risk taking of enterprises

The entrepreneur at the start of the enterprise and throughout its operation is continuously forced to take risks. This risk is often caused by uncertainty, that is when making decisions in connection with the enterprise the entrepreneur doesn't have the full range of information, or can't plan securely the processes going on in the enterprise or in its environment.

The main risk factors of the enterprise are as follows:

1. **Financial risk:** to carry out activity the entrepreneurs put in capital advanced, because they expect that by selling the product or service resulting from the activity the invested capital will show a return. Furthermore, the revenues will have to cover the advanced capital in the next production cycle, too
2. **Functional risk:** The entrepreneur manufactures a product or provides service to satisfy consumer demand. But in certain

- cases, (e.g. consumer needs change, the entrepreneur didn't size up market demands properly) it is not successful, so the aim of the enterprise can't be achieved, it'll be unsuccessful
3. **Legal risk:** The legal environment (law system, regulations of institutions, authorities) of the enterprise continuously changes, they are hard to calculate. Already at the start of the enterprise several laws, regulations have to be complied with, and will have to be paid attention to throughout the operation.
  4. **Administrative risk:** To successfully manage the enterprise professional competence on its own is not enough. The operation of the enterprise has to be documented for the stakeholders of the enterprise in a way which complies with the interests (e.g. owner – profit division, tax authority – the extent of taxpaying, employee – salary, etc.).
  5. **Professional risk:** In the course of the activity, they don't only have to meet consumer requirements, but they also have to comply with the professional quality specifications of the given sector, and with the documented or expected norms of it (e.g. making the wine Egri Bikavér).
  6. **Social risk:** The activity of the enterprise has to be carried out in a given social environment, it has to comply with the existing requirements, it has to achieve the support of the close environment in order to successfully operate. (e.g. Running a disco in the neighborhood will trigger resistance among the members of the community.)
  7. **Environmental risk:** Throughout the activity, behavior damaging the environment directly or indirectly will have an adverse effect on the operation (fine, social resistance, negative image).
  8. **Social risk:** The fortune of the employees depends on the success of entrepreneurs. Termination due to fiasco bears a significant risk for employees and their family.
  9. **Psychical risk:** Can the entrepreneur meet the requirements of the continuously changing environment? Can the entrepreneur continuously operate successfully with flexible control?

Throughout the operation of managing the enterprise entrepreneurs have to continuously examine the possible risk factors, and by planning appropriately, they have to prepare for the solution. Of course, not all risks can be anticipated and planned in advance. Most enterprises characteristically only deal with possible risks in an intuitive way, and

planning in connection with this is rare. A common research by Corvinus University and ING Bank shows this. (link: Market and Profit: Company risk management could be a lot more conscious)<sup>6</sup>.

The basic strategies of risk management:

1. **Risk aversion:** planned behavior which eliminates factors causing risk (process, business connection, etc.).
2. **Risk reduction:** strategy aimed at decreasing the extent of the occurred or expected risk or damage, and at decreasing the effect on the enterprise, at keeping it at manageable level.
3. **Risk sharing, shifting:** the enterprise will involve partners in certain activities to manage risks which couldn't be dealt with on their own. So they take and manage risks together.

### 2.2.7 The role of SMEs in the economy

The so called SMEs, and also the microenterprises are significant role players in the economy. 'In 2009 out of the 689,000 enterprises operating in Hungary, 688,000 were qualified as SME.'<sup>7</sup> Most of these enterprises are partnership companies, limited partnerships in particular. 'In 2009 considering all enterprises they produced 56% of the added value, the total of which was more than HUF 7,100 billion.'<sup>8</sup> You can read about the international situation in this study: Global Entrepreneurship Monitor 2013 Global Report.<sup>9</sup>

Based on these data it is obvious that considering the operation of the economy, not just in Hungary, but all over Europe it is important to support, aid the operation of these enterprises. Based on these facts, the European Union has taken measures supporting the SME sector. (: SME sector in Europe).<sup>10</sup>

In harmony with the European regulation principles, *Act XXXIV/2014 about SMEs, and about their support* was born. The law regulates which enterprises are qualified as micro, small or medium-sized ones. This

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<sup>6</sup> 2014. 01. 24. <URL: [<sup>7</sup> The situation of SMEs in the regions Central Statistical Office 2011 September](http://www.piacessprofit.hu/kkv_cegblog/vallalati-kockazatkezes-joval-tudatosabb-is-lehetne/></a>></p></div><div data-bbox=)

<sup>8</sup> The situation of SMEs in the regions Central Statistical Office 2011 September

<sup>9</sup> 2014. 01. 24. URL: <http://www.gemconsortium.org/docs/download/3106>

<sup>10</sup> 2014. 01. 24. URL: [http://ec.europa.eu/enterprise/policies/sme/small-business-act/implementation/index\\_en.htm](http://ec.europa.eu/enterprise/policies/sme/small-business-act/implementation/index_en.htm)

classification is the basis for the regulation of access to support forms coming later. Which enterprises are qualified as SMEs? According to the law, an enterprise is qualified as SME if it has the following characteristics:

*Table 1: Categories of SME organizations*

<b>Index</b>	<b>SME</b>	<b>Small enterprise</b>	<b>Microenterprise</b>
Total number of employed <b>and</b>	<250 people	< 50 people	< 10 people
Yearly net income <b>or</b>	≤€50 million	≤ €10 million	≤ €2 million
Balance sheet total	≤€43 million	≤ €10 million	≤ €2 million

Since these enterprises, considering their size (turnover, number of employees, etc.), are small, less strong financially, so their earnings at disposal to enhance their development is scarce. The development of this sector must be helped by government means.

The government identified the following problems in its SME strategy:<sup>11</sup>

- lack of innovation culture, of material and human preparation characterizes most SMEs;
- the entrepreneurial spirit, the ambition connected to the protection of intangible property are missing;
- entrepreneurial “spin off” processes often get stuck;
- the intersectoral (company-research center) connection system is weak;
- SMEs rarely join into international RDI processes;
- incubation is insufficient;
- risk capital involvement increases slowly;
- missing state innovation management service;
- lack of internationally renowned RDI-managers;
- too few cutting-edge technology small enterprises basing on RDI;

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<sup>11</sup> Hungarian Government Strategy of SMEs 2014-2020



- efficiency of adaptive innovations is bad (e.g. due to shortcomings of RDI infrastructure).

The expected support areas of the SME sector<sup>12</sup>:

**Market development and maintaining the market:** Hungarian SMEs successfully appear at domestic and export markets with their innovative and knowledge-based products. They build out stable supplier relationships, and to an ever growing extent they make use of the advantages provided by networking.

**Differentiated enterprise development:** The actors of the SME sector, suiting their life situation, ambition, and abilities. are granted an aimed support through which more and more of them get on a growth path.

## 2.3 SUMMARY, QUESTIONS

### 2.3.1 Summary

Enterprises are established for some sort of production or service purposes to satisfy consumer demand. The goal of organizing the activity is to gain profit (except for non-profit enterprises). In the system of economics enterprises provide products for the consumers, and also provide possibilities to work, in exchange for the work they pay a salary. They pay taxes to the state and receive subsidies from it.

The exchange of goods is carried out in the market where demand and supply meet, and at the formed prices buying and selling takes place. However, you must consider several limiting factors when planning to enter the market. When launching an enterprise, and also throughout its operation, you must assess the possible risks and work out the possible methods to manage risks.

Throughout its operation the enterprise will get in touch with different people and institutions. The interests of the stakeholders of the enterprise might be different, so the enterprise must recognize these interests, and for the sake of efficient operation must take it into consideration.

A significant segment of enterprises is the SME sector, which takes up a significant role in the economy, but their potentials are limited due to their small size and capital. The support of this sector is a stressed task of the state.

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<sup>12</sup> Magyar Kormány Kis- és középvállalkozások stratégiája 2014-2020

### 2.3.2 Self-testing questions

1. What is a company?
2. What is a business venture?
3. What are the general characteristics of business ventures?
4. Why are forced enterprises established?
5. What's the difference between non-profit and for-profit enterprises?
6. What connection is the enterprise in with different players of the economy?
7. What's the place where the enterprise sells its product to the consumer?
8. Introduce the main limiting factors of entering the market!
9. Who are the internal players of the enterprise? What characterizes them, what are their interests?
10. Who are the external players of the enterprise? What characterizes them and what are their interests?
11. What risks might an enterprise face throughout its operation?
12. What kind of basic risk management strategies do you know of?
13. What does the SME sector mean, and what kind of organizations does include?
14. What's the role of the SME sector in the operation of the economy?
15. What are the main problems of the SME sector?

### 2.3.3 Practice tests

1. The company's number of personnel is 15, its yearly net revenue is HUF 35 million. Can it be qualified as micro small or medium-sized enterprise?

1. no
2. yes, microenterprise
3. yes, small enterprise
4. yes, medium-sized enterprise

(answer: 3. yes, small enterprise)

2. The balance sheet total of the company is HUF 15 billion. Can it be qualified as micro, small or medium-sized enterprise?

1. no
2. yes, microenterprise
3. yes, small enterprise
4. yes, medium-sized enterprise

(answer: 1. no)

3. Make a list of at least 4 purposes why enterprises are established.

(answer: 1. The entrepreneur has the infrastructure, means, financial background and/or expertise which makes it possible to carry out a given activity on its own. 2. Wish to make decisions independently and to take responsibility. 3. The entrepreneur has an idea which can be realized freely this way. 4. Forced enterprises. 5. To make bigger profit (compared to salaries earned as employee).

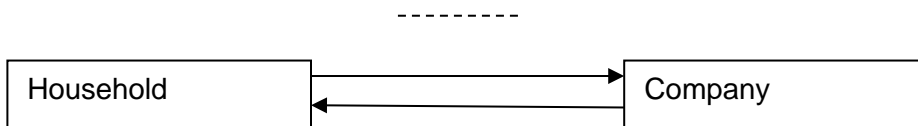
4. Make a list of the common characteristics of enterprises (name 5).

(answer: making profit, satisfy consumer demand, independent decision making, taking risks, influencing the market)

5. Complete the figure by naming the appropriate process!

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answer:  
labor force  
demand



6. Mark how the company can get into connection with the state in the economic system? You can mark more than one.

- a, product supply
- b, utilize subsidies
- c, labor force demand
- d, export
- e, import
- f, taxpaying

answer:  
wage  
supply

(answer: a, b, f)

7. Mark the internal players of the enterprise, choose from the ones below. You can mark more than one.

- a, supplier
- b, consumer
- c, employee
- d, state institutions
- e, natural environment
- f, local civil communities
- g, owner
- h, strategic partners
- i, competitors
- j, managers

(answer: c, g, j)

8. Mark the external players of the enterprise. Choose from the ones below. You can mark more than one.

- a, supplier
- b, consumer
- c, employee
- d, state institutions
- e, natural environment
- f, local civil communities
- g, owner
- h, strategic partners
- i, competitors
- j, managers

(answer: a, b, d, e, f, h, i)

8. Make a list of 3 possible risk management strategies!

(answer: risk aversion, risk reduction, risk sharing or shifting)

### 3. LESSON: HISTORY OF THE FORMATION OF CORPORATE ENTERPRISES

#### 3.1 OBJECTIVES AND COMPETENCIES

The objective of this lesson is to familiarize the students with the formation of enterprises, their historical development, to teach what reasons and processes led to the formation of the current entrepreneurial organization. The students will learn the role of enterprises in the economy.

After learning the lesson, the student will be able to present the history of the formation of enterprises, to explain the reasons of the formation of the current regulations. They will be able to show the current combination of the enterprising sphere, and its contribution to the performance of the economy.

#### 3.2 CURRICULUM

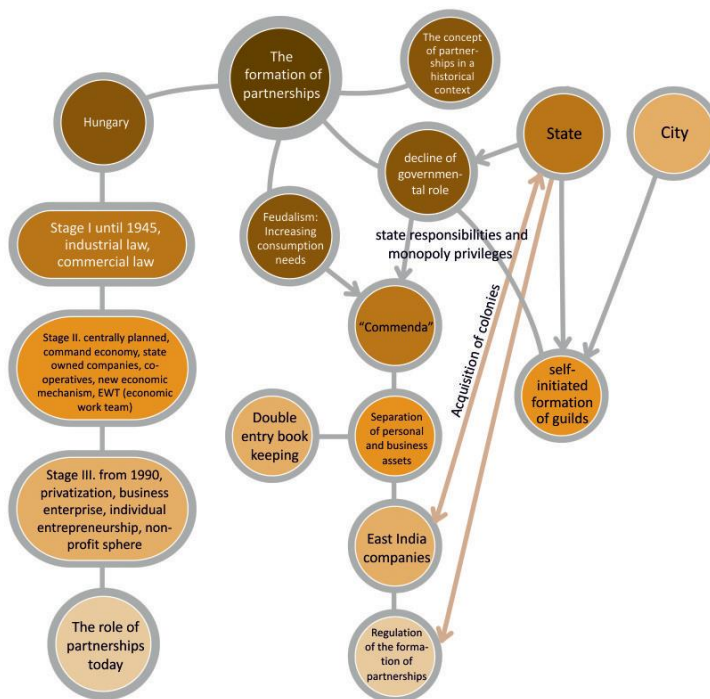


Figure 5: Concept map

Talking about **corporate enterprises** we mean a wide range of enterprises. The notion means more than a big circle of enterprises (it'll be discussed later). By corporate enterprise – in this chapter – we mean all enterprise forms created by several people on their mutual autonomous will, in which the members established the partnership with financial contribution, and the goal of operation is to grow wealth, and the members take the risks of investment together.

### **3.2.1 The evolution of the formation of corporate enterprises<sup>13</sup>**

#### *3.2.1.1. Consequences of the decrease of the state's engagement*

Mentioning corporate enterprises, looking for the most primitive forms of them, we can go back in history as far as the ancient times. At that time state property was determinant, but e.g. certain activities of sea trade were outsourced to guilds. Since one ship carried the goods of several traders, risk was shared.

After the termination of state engagement, the demand for organizing activities in private hands appeared first in sea trade. In the feudal Europe consumer demands kept growing, it meant bigger and bigger volume for producers and traders alike, but the necessary capital couldn't be provided by just a single private individual. Due to the big risk, ship owners (investor, trader, captain, crew) shared the burden and the risk, and divided the profit. The trader most often didn't travel together with the cargo, he sent a 'commissary' instead of himself. The institution of 'commenda' was created from this in the medieval Italy, which was the initial form of limited partnership. The capitalist provided the carrier with ship, money, cargo, but he didn't take part in the journey. The participating parties divided the profit. The capitalist claimed for a bigger profit, the risk extended up to the amount of his invested wealth, often even his name was kept a secret. First this form was applied in the case of Mediterranean trips, then it spread in the case of continental transport as well. These initial corporate enterprise forms were often just made up for one trip, they didn't mean a lasting connection.

In the 14th century due to the increasing demand for capital, families carrying out economic activity more and more were forced to involve exterior capital. Thus the family wealth had to be separated from the

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<sup>13</sup> Kisfaludi András: A társasági jog helye a jogrendszerben (Polgári Jogi Kodifikáció, 2000/2., 36-46. o.) based on article

business wealth. To keep records of this, the initial form of double-entry booking was created.

### 3.2.1.2. *Enterprise forms 'organized from grassroots'*

Guilds formed in the medieval ages meant a different form of corporate enterprise. Whereas the above mentioned trade partnerships were created due to the decreasing state engagement, the guilds were 'grassroots' organizations, they meant most often a common production enterprise which was created upon the voluntary will of members. Primarily, they were organizations created to safeguard the interests of the participants in crafts (the oldest form of this was found about the fishermen in Ravenna). The guilds could monopolize the production of certain goods with his organization (bubble: distributed exclusively).

At the head of the guilds guildmasters stood. The guildmaster represented the guild in front of the public, and was responsible for the operation of the guild in front of the authorities. The guildmaster's responsibility was to call the guild members together from time to time, when they discussed the businesses of the guild. It was strictly regulated who could become a member, and also the operation was defined by strict professional and moral standards. 'Quality production' was the common interest of the members, since in case of a problem not just a member but the whole guild could be condemned.

Guilds could often get exclusive rights from the state in a particular area, as a function of which state power often intervened in their internal affairs, or the guild's capacities were 'utilized' for state purposes. *'Such a formation was Merchant Adventures, the community of guilds exporting woolen cloth in England, which was granted a legal monopoly with a royal charter in 1564 to export woolen cloth to Germany and the Netherlands. These companies having privileges can be considered one of the prototypes of the companies later.'*<sup>14</sup>

### 3.2.1.3. *Forerunners of shareholding companies*

The first bigger companies mentioned as the forerunners of shareholding companies were made at the beginning of the 1600s to realize trade purposes. With state approval the British East India Company in London was established in 1600, the main purpose of which was tea and spice trade. In 1601 led by Sir James Lancaster the first

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<sup>14</sup> Kisfaludi András: A társasági jog helye a jogrendszerben (Polgári Jogi Kodifikáció, 2000/2., 38. o.)

expedition of the British East India Company started. At the beginning they didn't have constant capital, for the separate trips investors were recruited each time. At the head of it there was the board of directors. The members of the company carried out activity on their own at the beginning, but since the trade privilege in the Asian territory was granted to the company, those who wanted to trade in the area had to become members. After 1692 members were not allowed to trade on their own. Smaller businesses with similar functions were incorporated in the company in 1708, thus it monopolized the market. Besides the board of directors a supervisory board also controlled the company, and they had to give an account of their activity directly to the Parliament. As a consequence of their involvement in the opium trade more and more tension was caused by their operation, so the company was officially terminated in 1857.

The Dutch East India Company was made in Amsterdam in 1602. With its help a significant Dutch colony was formed in Asia. The primary purpose of operation was spice trade. But they couldn't keep up with the British company, so eventually the company was defunct in 1789, its colonies and debts were taken over by the state.

The other means of realizing bigger and bigger trade objectives was the corporate enterprise organized in town. In the 14th-15th centuries those towns which managed trade on their own could involve the public in producing the necessary capital. The participation right of the members was not transferable. Over these companies there always was state supervision, so the state could intervene in the operation, as well. Often in the activity state tasks were dominant.

The creation of corporate enterprises was often a state initiative, or happened with state consent. In the next step the state defines in a normative way under what conditions an enterprise can be established. *'In England a law in 1844 introduced the system that companies could gain their legal entity status by getting registered, and it terminated the requirement that they had had to obtain a decree or act about the foundation of the company from the monarch or the legislation. The system of state permissions to establish enterprises was terminated in France in 1867.'*<sup>15</sup>

Finally the limited company, unlike general partnerships or public limited companies, was not a self-organized form, but was made due to legal initiative. It originates from Denmark, but first it spread in Germany.

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<sup>15</sup> Kisfaludi András: A társasági jog helye a jogrendszerben (Polgári Jogi Kodifikáció, 2000/2., 39. o.)



By the end of the 1800s establishing companies was completely separated from state licensing. The state regulates the framework of establishing and operating companies, but establishing a company and creating the conditions of operation is based on the members' voluntary resolution. At the same time, the regulation of the framework of operation, especially due to enhancing the security of economic connections, is more thorough.

### **3.2.2 The formation of corporate enterprises in Hungary**

In Hungary we divide the development of enterprises into three phases.

The first phase lasts until 1946, the second from 1947 covers the period defined by the socialist regime up until 1989-1990. The third phase has been going on since the change of the regime until today.

#### *3.2.2.1. The first phase (until 1945)*

Compared to the international development, the guilds in Hungary were made on the model of German and Italian guilds, but legally with a unique character. Their primary purpose was to safeguard the interests of the given trade, but sometimes their activity was also used to defend towns or fortresses. A religion centered way of thinking was important for them. The guild followed the private life of members, too, and sometimes they intervened, if it was found necessary.

The **Commercial Law in 1875**<sup>16</sup> names general partnerships, limited partnerships, public limited partnerships and co-operatives. After this you can make a definite difference between civil law (earlier: private law) companies and business (commercial) companies.<sup>17</sup>

*„61. § The following must be considered commercial companies:*

- 1. general partnerships*
- 2. limited partnerships*
- 3. public limited partnerships and*
- 4. co-operatives*

*62. § Occasional partnerships made for common profit or loss concerning one or two commercial deals don't fall under the decisions of the current law about commercial partnerships.*

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<sup>16</sup> Act XXXVII/1875 Trade Law

<sup>17</sup> Szikora Veronika: A polgári jogi társaság szabályozásának főbb csomópontjai Magyarországon Miskolci Jogi Szemle 2. évfolyam (2007) 1. szám 22. o.

*These partnerships, if the partners don't make arrangements otherwise in a contract, the participants contribute to the common partnership in equal measures; without any other agreement they divide the profit or loss per head.*

*In deals made by one of the partners with a third person, this partner is responsible and authorized in that direction. If a deal is made on behalf of the other partners, or if the participants make a contract together or with a common representative, then to/with the third party they together bear the rights and responsibilities.*

*After finishing the common business, the partner who managed the business is accountable to the others. This partner is also obliged to do the wind up.*

**63. §** *Commercial companies can gain rights, take responsibilities, can get rights on properties and other wealth, can get engaged in a lawsuit as plaintiff or defendant in the name of their company.*<sup>18</sup>

The law provides about the foundation of the companies named earlier, the legal relationship between the members, about their responsibilities with third parties, and about the rules terminating the company.

The idea of the limited liability company got to Hungary from Germany via the Austrian legislation in the 1920s. The law about the Limited liability company and about sleeping partnership was made in Hungary in 1930.<sup>19</sup>

**1. §** *The limited liability company (year 1875 XXXVII Act 4 § 1 par.) is a commercial company which is established with equity consisting of shares held determined in advance, and in which the responsibility of the member towards the company extends to providing shares held, and to other non-specified financial contributions stated in the company contract. The member is not responsible for the responsibilities of the company.*

*Limited liability company can be established for any commercial purpose. It must not deal with insurance policies, banking and exchange businesses as a trade, it mustn't take savings deposits, it mustn't issue mortgage bonds or bonds of any kind.*

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<sup>18</sup> 1875. évi XXXVII. törvénycikk Hetedik Czim

<sup>19</sup> 1930. évi V. törvénycikk

*Bonds mustn't be issued about membership rights. The issued bond is invalid and the issuers are together responsible for the possible damage originating from this.*<sup>20</sup>

The law ordains the rights and responsibilities of the members' meeting and of the director, and provides about employing a Supervisory Board and a 'chartered accountant', and also about the volume of equity.

Guilds were terminated in 1872 by law, but instead of them the **Trade Law in 1884** made it obligatory to establish craft unions. Based on this:

*„1. § In the area of the countries of the Hungarian crown all people of age, or who are declared to be one, without distinction to sex, inside the limits of this law, can independently and freely do any crafts, including trade too, anywhere.*

*2. § Minors, after they are 18, with the consent of their father, or their guardian approved by the court of guardians, can practice a trade independently, and thus they become one of age.*

*3. § Legal entities can also practice a trade if they stand a business manager. (41. §)*

*4. § Those who want to practice a trade which does not need a permission, have to report in writing to the competent trade authority, and also to present that to practice the trade independently he meets the requirements in 1-2-3 §; besides if the trade he wants to practice a trade which by its crafts nature can only be acquired after long practice, he has to present the apprentice certificate (§67) and has to prove that after finishing studies he did at least two years of practice in the particular trade; which if happened, the trade authority papers about reporting (except for cases under § 43) can't be refused, and have to be issued by the trade authority in three days, or the person after three days can start practicing the trade. ...*

*... 122. § In towns having local authority and regular council, and in villages where there are at least 100 craftsmen doing trade which needs permission (§4) on request of two thirds of them, after listening to the particular industrial and trade chamber, with the approval of the local authorities, crafts-unions have to be established by the authorities.*<sup>21</sup>

### 3.2.2.2. The second phase (from 1946 to 1989-90)

The period after 1945 was the time of nationalization, private property was not approved. Private companies were nationalized. The players of

<sup>20</sup> 1930. évi V. törvénycikk 1. Fejezet

<sup>21</sup> Act XVII/1884 Industry Law

the company sphere were big state companies, co-operatives and some social organizations having legal entity. The state companies were under direct central rule. A significant part of state companies operated in the heavy industry, while in agriculture the co-operatives were characteristic. Production was carried out according to predetermined long term plans (3-5 years), so successfulness was not defined by market success but by the completion of plans. Act IV in 1959<sup>22</sup> regulates the main point of operation of state companies and co-operatives, but also mentions the Company constituted under civil law, which is a company form that can be made for common activity with strict legal limits. „The members' financial and tangible assets will become their mutual assets, their other contributions will be used together. ... All members are entitled to manage the business.”<sup>23</sup> But this was not considered a basic economic form.

The steps made during the 1968 economy management reform, so called new economic system, started some moves towards market economy elements. Companies remained in state property, but their independence grew. Prices were in part freed from authority ruling. The goal was to improve the market relationship of companies, but creating the socialist market economy met with difficulties, it didn't work in the existing frames. At the same time private small businesses, private smaller industry appeared. Inside the frames of big companies from 1982, in the framework of „the newest economic system” enterprise work teams (EWT) were organized, which after the legal working time could carry out activity for additional income with the tools of the company. They were the forerunners of the companies. Starting from the 1980s the first regulation forms appeared which provided founding for private economic activity.

### 3.2.2.3. *The third phase (from 1990)*

The first 'partnership law' was born in 1988.<sup>24</sup>, „1. § (1) *This act regulates the foundation of economic partnerships, their organization and the operation of their bodies, the members' rights and responsibilities, and the termination of the company. (2) Economic partnerships can gain rights and take responsibilities under the name of their own company,*

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<sup>22</sup> Civil Code

<sup>23</sup> Act IV/1959. 571-574 §

<sup>24</sup> 1988. évi VI. törvény a gazdasági társaságokról

*they can especially purchase property, can make a contract and can start a law suit and can be sued.*<sup>25</sup>

The law about the transformation of economic partnerships was born 1989<sup>26</sup>. The law regulates the new frameworks of processes embodying new organizational demands connected to the change of the regime, and also ordains about the transformation of state companies to become economic partnerships.

The law defines the following partnership forms: general partnership (inside this the EWT), limited partnership, union, joint venture, limited liability company and public limited company.

The law in 2006 about economic partnerships<sup>27</sup> redefines the basic concepts of economic partnerships, determines the common rules for economic partnerships (supreme body, foundation, termination, etc.) and regulates the specific ordains of the particular forms.

Besides this, economic activity could be done in the shape of private enterprises, too, which is regulated in Act CXV./2009.

Today so called non-profit enterprise forms are catching on. At the beginning they were established on government initiative, for public use, to carry out welfare activity. Later on more and more civil organizations separated from the state were set up. Their establishment was defined in the EC (Law about economic companies), but here they don't mean an independent form.

The new Constitution<sup>28</sup> born in 2011 lays the theoretical foundations of the operation of enterprises. Part M) of the Constitution contains this:

'(1) The economy of Hungary is based on work creating value and on the freedom of enterprise.

(2) Hungary provides the conditions of fair business competition. Hungary takes action against the abuse by dominance, and protects the rights of consumers.'

### **3.2.3 The role of corporate enterprises in the operation of the economy today**

According to data by the Central Statistics Office 1,806 thousand economic organizations are registered in Hungary in 2012. Out of this about a million are private ones, another 600 thousand are corporate enterprises. Two thirds of corporate enterprises are limited liability

<sup>25</sup> 1988. évi VI. törvény 1. fejezet 1. §

<sup>26</sup> Act XIII/1989

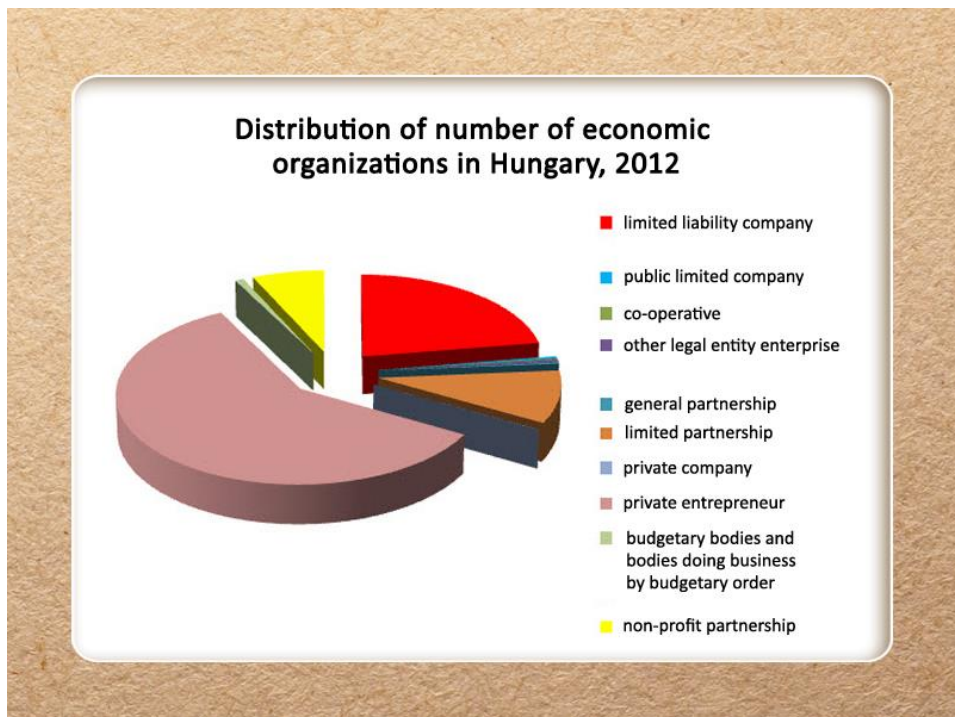
<sup>27</sup> Act IV/2006

<sup>28</sup> The Constitution of Hungary (Apr 25, 2011)

companies. According to CSO, the number of operating companies is 690 thousand. About 30 thousand economic organizations holding foreign interest were registered in 2011.

About three fourths of enterprises operate in the service industry, most characteristically in trade, car repair, or in professional, technical and scientific activity. Bigger organizations operate in the production sector. Enterprises operating in 2011 altogether entered HUF 76 billion in revenues in the books. This index also shows the central role of the capital city: 42% of the revenues were made by enterprises in Budapest, 12% of it was made by enterprises in Pest County. The sales revenue per enterprise in Central Hungary is HUF 153 million, in Northern Hungary it is only HUF 86 million.

„The role enterprises is determinant in producing GDP: In 2011 in Hungary they altogether produced HUF 14,350 billion of added value, six tenths of GDP.”<sup>29</sup>



*Figure 6: Distribution of economic organizations by type<sup>30</sup>*

<sup>29</sup> Regional particularity of enterprises CSO 2013 Oct

There were about 65 thousand economic organizations registered in 2010. Most of them operated in economic development, labor affairs, education and urban development. Their most characteristic forms are non-profit economic companies for public use, societies and foundations<sup>31</sup>.

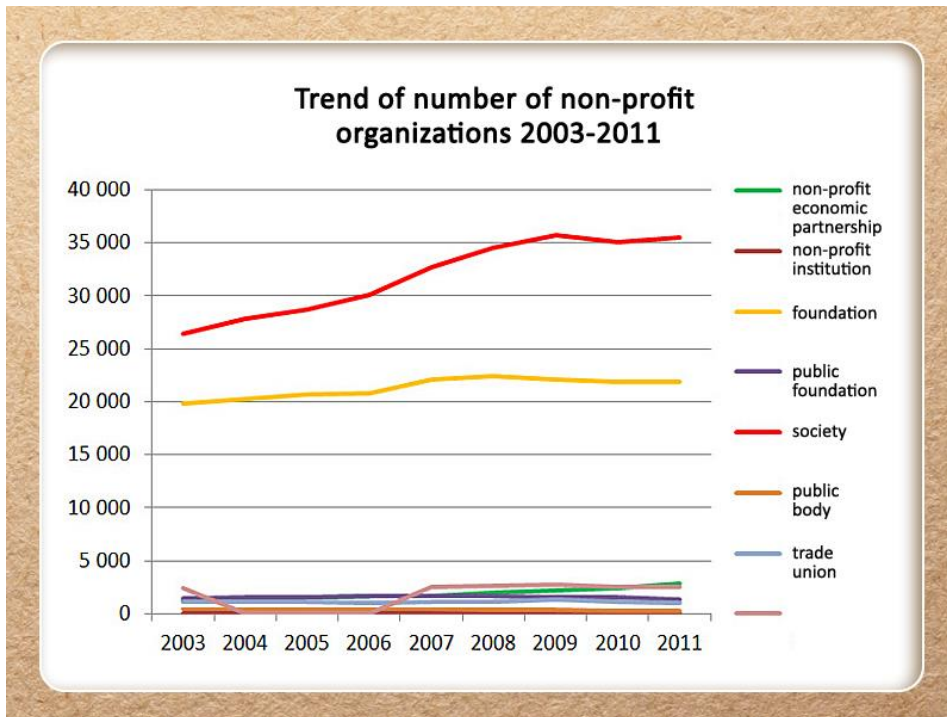


Figure 7: Trend of number of non-profit organizations by form<sup>32</sup>

### 3.3 SUMMARY, QUESTIONS

#### 3.3.1 Summary

The history of corporate enterprises goes back to the ancient times, though their actual formation was characteristic in the Medieval Ages.

<sup>30</sup> Source: KSH 3.2.1.2. The number of registered economic organizations – based on GFO'11

<sup>31</sup> The role of non-profit economic organizations in the Hungarian non-profit sector. Statisztikai tükör VI. évf. 76. szám 1-2. o.

<sup>32</sup> Source: Non-profit organizations in Hungary, 2011 CSO

Primarily, their first forms were set up to take on some state tasks on state initiative, in areas where state engagement decreased. The first corporate enterprises served to achieve aims in sea trade and in continental commerce. With the increased demand for transport the ever growing need for capital to do commercial activity single families couldn't produce, so the involvement of capitalists started, so did the separation of private and business wealth, and executive and managing roles.

Guilds organized to protect the interests of workers, craftsmen can be considered the ancestors of corporate enterprises. To achieve a common goal, primarily they carried out production activity, under strict rules, guilds were represented by one or more guildmasters.

The first bigger companies (British and Dutch East India Company) were also created in the field of commerce, they had a significant role during the colonization. The capital for the business was first 'recruited' occasionally. Later they made considerable revenues and the profit was divided between the investors. Inhabitants as investors could also be involved in the activities organized by towns. These companies can be considered the ancestor of public limited companies. The limited liability company started from the Netherlands and spread from there.

In the development of enterprises in Hungary we can separate three phases. Before 1945 similarly to other parts of the world the Hungarian sector was formed the same way. After the termination of guilds at the end of the 1800s, the Industrial and Trade Law fixed the first corporate forms.

After 1946 in the framework of the socialist planned economy production was carried out in state companies and co-operatives. In the 1980s inside bigger companies EWTs were made, which can be considered the ancestors of general partnerships.

After the change of the regime state companies and co-operatives were transformed to be economic partnerships.

Today there are about 1.8 million registered economic organizations in Hungary.

Non-profit organizations are catching on. Their characteristic forms are the foundation, society and non-profit economic company.

### **3.3.2 Self-testing questions**

1. What do you call in general a corporate enterprise?
2. When and how were corporate enterprises made as a consequence of decreasing state engagement?
3. Where did 'commenda' develop, and which corporate form is its ancestor of?



4. What was the role of the capitalist in the 'commenda'?
5. As a consequence of what did double bookkeeping develop?
6. What forms of corporate enterprises in the Middle Ages were organized from 'grassroots'?
7. Characterize the operation of guilds from the point of view of corporate form?
8. How and why were the ancestors of public limited companies created? Name at least two of them?
9. How and why did towns organize corporate enterprises?
10. Where and to what extent differently than earlier were limited liability companies formed?
11. Into what phases can you divide the formation of enterprises in Hungarian history?
12. Characterize the development of enterprises in Hungary up to 1945!
13. Characterize the development of enterprises in Hungary between 1946 and the change of the regime!
14. Characterize the development of enterprises in Hungary after the change of the regime!
15. With the help of numerical data, present the role corporate enterprises in the operation of the economy!

### 3.3.3 Practice tests

1. Select from the following statements which is not true for the feudal Europe!

- a, 'commenda' is formed
- b, East India Company is established
- c, due to decreasing state engagement corporate enterprises for commercial purposes are formed
- d, the capitalist claimed big profit, but his name often remained a secret

(answer: b)

2. Match the items on the left with the ones on the right.

1. East India Company	A limited partnership
2. commenda	B limited liability company

3 the Netherlands	C general partnership
4.EWT	D public limited company

(answer: 2A, 1D, 3B, 4C)

3. Put an X to the appropriate period which characterizes the development of corporate enterprises in Hungary.

Statemet	up to 1945	1946-1990	from 1990
The characteristic forms were the state company and the co-operative		X	
Hungarian guilds were made following German and Italian models	X		
The spread of non-profit enterprises			X
EWTs were formed		X	
The regulation of private enterprise			X
The Trade Law names the notion of general partnership.	X		
The „new economic system” allows more independence for the companies.		X	
The Trade Law ordains the foundation of craft unions.	X		
Instead of profit objectives, the aim of the operation of enterprises was completing the plan.		X	

4. Interpret the table below.


TEÁOR'08 (4-3-2-jegy, alág, ág, ipar összesen) 05-63;68-82;85-96	Működő vállalkozások száma (2010. év)		
	A működő vállalkozások száma (db)	Termelési érték (1000 Ft)	Termékek és szolgáltatások összes vásárlása (1000 Ft)
Mindösszesen TEÁOR'08 (4-3-2-jegy, alág, ág, ipar összesen) 05-63;68-82;85-96	656 897	39 656 651 273	56 089 537 954
B+C+D+E Ipar összesen	55 237	23 430 507 715	25 030 455 510
F Építőipar	67 354	2 030 518 873	2 791 003 999
G Kereskedelem, gépjárműjavítás	141 433	4 584 102 515	18 677 173 317
H Szállítás, raktározás	30 731	2 514 459 517	2 717 261 943
I Szálláshely-szolgáltatás, vendéglátás	32 738	556 324 245	578 998 481
J Információ, kommunikáció	34 680	2 014 084 548	1 706 730 500
K Pénzügyi, biztosítási tevékenység			
L Ingatlanügyletek	33 196	914 575 740	1 029 140 628
M Szakmai, tudományos, műszaki tevékenység	113 115	1 686 119 644	1 794 790 475
N Adminisztratív és szolgáltatást támogató tevékenység	39 259	1 025 598 024	1 206 403 668
O Közigazgatás, védelem; kötelező társadalombiztosítás			
P Oktatás	28 262	104 717 635	91 200 645
Q Humán-egészségügyi, szociális ellátás	27 512	297 751 340	164 510 561
R Művészet, szórakoztatás, szabad idő	16 333	353 572 803	159 295 761
S Egyéb szolgáltatás	37 047	144 318 674	142 572 466

33

(Ez a táblázat az Excel fájlok között 03\_03\_K02\_jav.english címen található. Kérem átmásolni.)

5. Mark if the given statement is true (T) or false (F).

1. Non-profit organizations can also make profit. (T)

2. Half of the Hungarian enterprises work in the service industry.

(F)

3. The number of registered economic organizations is about 2 million. (T)

4. It's characteristic for the Hungarian business organizations that they in significant number operate in or around the capital city. (T)

5. Business organizations produce about half of the Hungarian GDP. (F)

6. 10% of the business organizations are non-profit organizations.

(F)

<sup>33</sup> Forrás: KSH Tájékoztatói adatbázis Működő vállalkozások 2010.

7. Out of the non-profit organizations most work in the form of a foundation. (F)

8. The most common economic partnership form is the limited liability company. (T)

## 4. LESSON: THE ASPECTS OF BECOMING AN ENTREPRENEUR

### 4.1 OBJECTIVES AND COMPETENCIES

In the lesson the students will learn the system of those processes on the basis of which the individual gets from the idea arisen to the operation of the enterprise. The objective is that the student will be able to define the main motivations of starting an enterprise. The student can assess the factors influencing the start of the enterprise and plan the process of starting an enterprise.

### 4.2 CURRICULUM

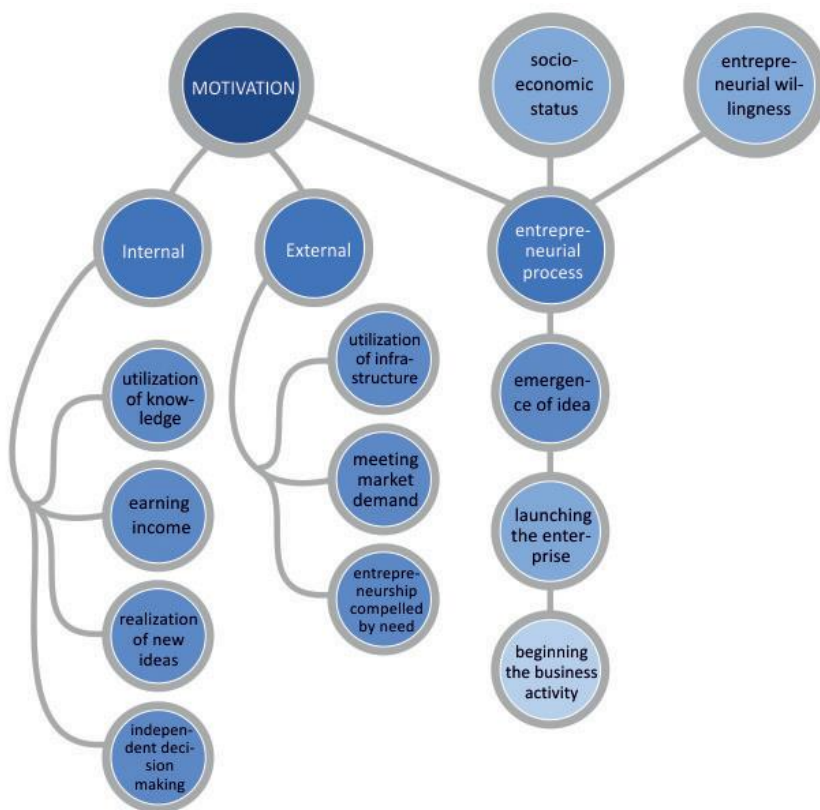


Figure 8: Concept map

#### 4.2.1 The economic, social, welfare background of becoming an entrepreneur

The society of Hungary and of many developed countries is aging. In the Hungary the decrease of population was 4.1/1000 people.<sup>34</sup> Concerning the whole of the population fewer and fewer people have to support a growing proportion of the population. Only 55.8% of the population of 15 to 64 years old were employed in Hungary in 2011.<sup>35</sup> It, has several reasons. On the one hand it is the factors influencing the workforce supply (e.g. health condition, higher expectation compared to possibilities), on the other the demand for work (not enough jobs, *structural problems* in the labor force market, etc.)

What's more, migration problems also influence the situation of the labor market (both immigration and emigration). The objective of government measures is creating jobs, and also supporting people to become entrepreneurs. An important effort is also, with different means in different countries, that professionals trained in vocational education and higher education, should use their knowledge where the education took place, and migration should decrease, especially when jobs with workforce shortage are concerned (e.g. doctors).

The other reason for the difference between demand for work and work supply is the change in qualification. More and more people take part in secondary and higher education, they learn languages, and obtain knowledge and competencies which encourage them to start independent activity. Considering the number students learning popular and less popular trades the divide is continuously growing. The value of trades with the shortage of workers is raised, though it takes a long time, thus higher and higher salary can be obtained as a result of doing activity in these areas.

The life cycle of education is prolonged. Students try to stay in the educational system longer, so starting to work and building a career comes later and later. As a result the time of having a family is put off too, according to several studies not just in Hungary but also in a significant part of Europe.

The classic male-female role has also been rearranged, women take their share of the work and career building, just like men. In spite of similar qualification, skills and career opportunities, women are still underpaid. (In Germany e.g. on the average, women make 23% less,

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<sup>34</sup> Forrás: KSH

<sup>35</sup> Forrás: KSH

than men<sup>36</sup>) Obtaining higher income is a motivation for starting an enterprise.

One type of obtaining extra income can be the combination of being an employee and an entrepreneur at the same time. It happens if someone is employed by a company but he also works part-time as a private entrepreneur. One reason for this is really making extra income, but the other is that you can do an activity which you can't do at the company.

#### 4.2.2 The main motives of becoming an entrepreneur

What is motivation? The word originates from the Latin 'movere' expression, the meaning of which is move.

📖 **Motivation is internal and external encouraging power which stimulates the individual to do a given activity. In our case we are looking for stimulating powers which motivate the individual to start a private enterprise.**



*Figure 9: The motivations of becoming an entrepreneur*

<sup>36</sup> Selma Stern : Lohnunterschied Warum verdienen Frauen weniger als Männer? Die Zeit 2012/25. (2014. 01. 29. <http://www.zeit.de/2012/25/Analyse-Frauen> )

Starting an enterprise can have internal and external motivation.

#### *4.2.2.1. Internal motivation*

The internal motivation originates from the individual's inner characteristics, will, character, attitude. This motivation can be:

##### **1. Obtaining income**

Obtaining income as motivation may show up in different ways. A frequent reason is that the employee is not satisfied with the salary at the workplace, so he starts an enterprise either as a main job, or as a part-time job, hoping to gain a higher salary. In the case of this motivation objective, the entrepreneur plans and considers primarily based on the achievable profit objective.

##### **2. Utilization of existing knowledge**

In this case the individual feels that he has a knowledge (e.g. building false nails), ability (e.g. journalism), or competency (e.g. expert), which in the given situation is not, or not well enough utilized. The purpose of starting an enterprise is the utilization of knowledge, the use of professionalism in the most complete way.

##### **3. Demand for making decisions and taking responsibility independently**

As an employed person the employee is forced to accept his/her superiors' decisions, and carry out the activity based on it, many times no one is interested if he agrees or not. Disagreement causes internal tensions, which the employee can either manage, or not, depending on the individual for a longer or shorter period. Reaching the tolerance limit, the person has to choose, either he solves the problem, or quits. Those who think in a given decision making situation they could manage the activity causing tension better, to prove this (to themselves or to others) start a private enterprise. The main aim is achieving and declaring success.

##### **4. The realization of a new idea, innovation**

This motivation appears when the individual has a new idea for a product or service, maybe for some business method, which wasn't present in the market before, or at least not in a market available for the individual. An enterprise can be established for the utilization of patented innovation having significant novelty.



A good example for this is the *glass fiber reinforced concrete*. ([Link: Multi failed with glass fiber reinforced concrete](#))<sup>37</sup> ([English link: Seeing through concrete](#))<sup>38</sup>.

When realizing a new idea, the main aim is to make the product and to introduce it to the market. Of course, it's worth thinking about patenting.

#### 4.2.2.2. *External motivation*

The external motivation is a stimulating power coming from the environment, and is independent of the individual's character. Some for example:

### 5. Utilization of existing infrastructure

An enterprise idea is often born starting off with a property the individual has (garage – non-stop shop), or an instrument (lorry – moving furniture), which the person would like to utilize. Since they mean a basis for the start, due to their existence less capital is needed, so often a given enterprise develops from this.

### 6. Satisfying recognized market demand

The entrepreneur establishes a company because he thinks he recognized some consumer demand which doesn't have a solution, or just scarcely, in the relevant region, and which could be satisfied with his/her product or service. The aim is to succeed in the given market. At the link below you can read about a toy shop.

([link: The toy shop that doubles its revenues every year](#))<sup>39</sup>.

([English link: Why Steve Case is Betting Millions on Lolly Wolly Doodle](#))<sup>40</sup>.

### 7. Forced enterprise

The most frequent reason for starting a forced enterprise is that the employee lost his/her job, and/or can't find a suitable one for a long time.

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<sup>37</sup> 2014. 01.31. <http://www.pannonnovum.hu/hirek/az-innovacio-vilagabol/beletort-a-multi-bicskaja-a-magyar-uvegbetonba>

<sup>38</sup> 2014. 01.31. <http://hungarian-success-stories.com/2013/03/10/seeing-through-concrete/>

<sup>39</sup> 2014. 01. 31.

[http://hvg.hu/enesacegem/20140129\\_Az\\_uzlet\\_amely\\_evente\\_megduplazza\\_a\\_bevet](http://hvg.hu/enesacegem/20140129_Az_uzlet_amely_evente_megduplazza_a_bevet) )

<sup>40</sup> 2014. 01.31. <http://www.entrepreneur.com/article/227089> )

So, to make income he wants to carry out manufacturing or service activity. The aim is financing himself/herself.

Forced enterprises can become successful a, too. Read about it here. ([link: Chokome](#))<sup>41</sup>.

Of course, the government also tries to handle the problem of forced enterprises. You can read about it as an example at the following link in The Morning Star. ([link: Labor We'll End Bogus Self-employment](#))<sup>42</sup>

The above mentioned motivations can occur separately, or mixed with each other. The more aims point at the direction of the enterprise, the sooner the entrepreneur makes a decision about starting a company.

### 4.2.3 Entrepreneurial willingness

On behalf of the European Union a survey<sup>43</sup> was carried out in 2004 about entrepreneurial willingness, in which 21 thousand people worldwide were asked about the attitude connected with becoming entrepreneurs. It turns out, that while Europeans prefer being employed, in the USA self-employment is preferred. 61% of the Americans said they would go for self-employment, whereas 51% of the Europeans (EU-15) would like to be employed. In Europe the biggest number of people opting for employed status can be found in Finland, self-employment is preferred best in Portugal.

A bigger proportion (51%) of men would opt for being self-employed, as opposed to 39% of women. The younger age-group takes up starting an enterprise with more pleasure, especially those still in education are susceptible. Inhabitants of bigger towns choose starting an enterprise in bigger proportion, as opposed to those living in the country. Employment status is preferred because it means calculable income, as opposed to the uncertain income of entrepreneurs which can be planned with difficulty. It is evaluated as more secure from different points of view, like social security. Starting an enterprise due to independent decision making is primarily important for Americans. To make a stable income as an employee, is primarily important for citizens of less prospering economies, whereas the stability of work with lower unemployment rate it is not really an argument.

In Hungary the proportion of those willing to become entrepreneurs to achieve higher income was significant: 43%.

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<sup>41</sup> 2014. 01. 31. <http://www.chocome.hu/chocome/?menu=cegtortenet>

<sup>42</sup> 2014. 01.31. [http://www.morningstaronline.co.uk/a-3222-Labour-Well-end-bogus-self-employment#.UukrL\\_tpqXs](http://www.morningstaronline.co.uk/a-3222-Labour-Well-end-bogus-self-employment#.UukrL_tpqXs)


<sup>43</sup> Entrepreneurship Flash Eurobarometer European Commission 2004

The wish to own a business of their own is more characteristic with men, and is also stronger with the young generation. Just 34% of the Hungarians would like to become entrepreneurs in the next 5 years, with this the country is in the middle of the field in the EU-25.

It is interesting though, that 59% of responders said, they had never even thought of becoming an entrepreneur (in Hungary it is 57%).

Though it is difficult to think over in advance, but entrepreneurial willingness is also influenced by sizing up how long they can operate in a given industry, area, region. According to CSO data, the *one year survival rate* of enterprises (**bubble**: proportion of enterprises still operating in the first year after the start) is 79% in northern Hungary<sup>44</sup>. This means that 21% of the newly established enterprises are terminated in the first year. The two year survival rate is 60% in the same area, whereas the three year one is 50%. That is, in the 3rd year after starting only half of the enterprises „survive”<sup>45</sup>

#### 4.2.4 The process of becoming an entrepreneur

 **The process of becoming an entrepreneur includes all the activities of the entrepreneur from the idea arising to the operation of the enterprise.**

The process consists of the following steps:

##### 4.2.4.1. *The idea arises*

The process of enterprising starts when the **idea of the enterprise arises**. It might be the consequence of either internal or external *motivation effect*, which we discussed in *chapter 4.2.2. (reference)* At this stage the individual evaluates if the idea triggered by the motivation effect is relevant, if it is worth dealing with in detail at all. If the individual thinks that this possibility is feasible, then further **consideration factors** will be taken into account. The individual will assess if he has the necessary *skills*, qualifications, competencies, or can get them in an acceptable way (e.g. course). The individual will also examine the different *environmental elements* (e.g. social), if the activity can be fit into the given environmental conditions (e.g. compost plant in a resort area, luxury hotel, slum, etc.).

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<sup>44</sup> 2010. évi adat

<sup>45</sup> KSH 1.2.4. Vállalkozások demográfiája és struktúrája (2000–2011)

It is important to assess if there is **consumer demand**, or if it can be created for the planned activity, if the product or service can be sold in a volume which generates profit for the enterprise.

If the idea seems feasible on the given conditions, then you'll have to start assessing the concrete factors necessary for realization. They are the necessary **resources** for starting and doing the activity (e.g. real estate, means, machines, human resources, capital, natural resources, etc.).

At the start of the enterprise the future entrepreneur must consider several costs which are not optional but 'obligatory'. While in the case of real estate or a machine he can decide what kind of thing he wants to buy at what price and quality, the fees of establishing a company can't be influenced. To establish a company you need a corporate contract (or founding document, constitution), and registration can only be made by a lawyer (or public notary). Together with this, certain activities can only be carried out with the permission of authorities, which also have to be calculated with as for their **demand for time and costs**.

When assessing the necessary resources, the future entrepreneur compares the resources necessary for the activity with the existing ones. He defines what means beyond the existing ones have to be found, and if it is feasible. It also has to be considered if the cost of finding the necessary resources will be refunded as the result of the activity.

#### *4.2.4.2. Starting the enterprise*

If based on the preparatory phases the entrepreneur finds the possibility favorable, concrete steps can be made to actually start the enterprise.

Starting an enterprise starts with the concrete **assessment of consumer demands**. It can be done with secondary (already existing) statistics statements, with a survey of our own (questionnaire).

The **necessary resources** for the start of the enterprise have to be obtained, and put at disposal. We mean property necessary for the activity (e.g. plant or office building), instruments, machines (e.g. lorry, turner's lathe), staff (joiner, driver, cleaner, accountant) and capital (e.g. to buy basic material). About the resources of the enterprise you will learn later.

An important step for carrying out an activity is **strategic planning**. In the course of it we determine the main objectives of establishing an enterprise, the activities and instruments necessary to achieve the aims. The main parts of the strategic plan are: Executive summary, Introduction of the enterprise, Trade analysis, Products, services, activities, Human

resources plan, Marketing plan, Financial plan, Risk assessment, Social commitments, environment protection.

The main point of planning is not that you have to concretely determine each step in advance which you can't turn aside from, since the environmental conditions keep changing continuously, and the enterprise has to adapt to this. The aim of planning is the assessment of fundamentals, potentials and risks, which have to be followed with attention, and in case of deviation from the plan, intervention is needed.

Planning is followed by **obtaining** the necessary **permissions**. Certain activities can only be done if you have the permission of the particular authorities, as ordered by law. E. g. running a food shop you need the permission of NPHMOS (National Public Health and Medical Officer Service), or to do activity which produces waste-water you need the permission of the National Inspectorate for Environment, Nature and Water.

The next step is **company foundation**. The conditions for this are defined in IV./2006 Act about economic partnerships, Civil Law (V./2013 Law about Civil Code), and CXV./2009 Law about private entrepreneurs and private companies. The establishment needs different conditions in the case of starting individual or corporate enterprises. We will discuss this later in detail when talking about particular corporate types (reference: 8. Lesson: Types of enterprises).

The condition for starting the activity is the **registration of the company**, that is corporate enterprises have to be registered at the registry court, private enterprises have to be registered at the local government document office. After getting registered the activity can be started.

Check out the following web page:  
<https://ugyintezes.magyarorszag.hu>

#### *4.2.4.3. Beginning the activity*

To begin the activity you have set up the **organization system** which can manage all the processes of the enterprise. Here, beyond the basic activity, you must think of additional tasks, too (e.g. when opening a pizzeria besides employing a baker, you need an accountant, a cleaner, too). Besides employing the staff having the suitable skills, the condition of efficient operation is creating the well-defined responsibility and authority circles. You have to determine who can carry out certain activities, who can instruct whom, who is reports to whom. Authorities run into each other, destroyed responsibilities will damage the efficiency of operation.

The other important condition of successfulness is to **determine and co-ordinate part activities**. So that our pizzeria could serve the guest with hot pizza in 20 minutes, you must have the basic material of the appropriate quality at disposal at the necessary time in the necessary amount, you must have the professional who makes it, there must be an working oven, you must have plates to serve the pizza on, etc. These part activities, individually and together, must be planned carefully and precisely.

When the enterprise started operation, or even before it, you must let the possible consumer circle know. Learning Marketing, you will learn about the instruments with the help of which you let the consumer know about your enterprise about the available products, services, prices and the conditions of using them. Efficient **promotion** contributes to the success of the enterprise.

After starting the activity, you have to assess the long term opportunities. It is important to define the reasonable goals, which the entrepreneur wants to achieve through the operation. An aim can be continuous growth, transformation (e.g. from private enterprise into business partnership), extension of the scope of activity, or sales at a higher value, and also withdrawal. It can also happen that a company is only established for a particular reason (so called **project company**), and after achieving the objective the company is terminated (e.g. the construction of M4 metro line).

To encourage the processes above, several initiatives, strategies were born in Hungary and in the European Union, as well. Also the supporting system for it was made and is continuously shaping. You can read about the principles, objectives and instruments at the link below:

**link:** [Green Paper Entrepreneurship in Europe](#)<sup>46</sup>

### 4.3 SUMMARY, QUESTIONS

#### 4.3.1 Summary

The entrepreneurial sector is a very important area of every economic system. Not only because of its function generating income, but its influence on work supply, product offer is also essential. Several environmental elements influence enterprises. The interaction with social, economic, political and other elements is a determinant factor.

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<sup>46</sup> 2014. 01. 31.

[http://eur-lex.europa.eu/LexUriServ/site/en/com/2003/com2003\\_0027en01.pdf](http://eur-lex.europa.eu/LexUriServ/site/en/com/2003/com2003_0027en01.pdf)

The establishment of enterprises can be motivated by internal and external factors, or their combination. At the same time, significant differences can be observed considering entrepreneurial willingness between different communities, which can be attributed to different reasons. The motivation to start an enterprise is still low in Hungary, the bigger part of the active population still opt for a secure income of employment. The main motivation to start an enterprise in Hungary is to gain bigger income.

The process of becoming an entrepreneur is complex, it lasts from the idea arising to the operation of the enterprise. The emerging of the idea is followed by starting the enterprise, finally the entrepreneur's continuous task is the operation.

#### **4.3.2 Self-testing questions**

1. What are the current economic and social challenges which influence starting an enterprise?
2. What does the notion of motivation mean?
3. What internal motivation factors do you know concerning the start of an enterprise?
4. What external motivation factors do you know concerning the start of an enterprise?
5. What does entrepreneurial willingness mean, and what are its criteria?
6. How is entrepreneurial willingness shaping in Hungary?
7. What does the process of becoming an entrepreneur mean?
8. What stages does the process of becoming an entrepreneur consist of? Characterize the different stages.

#### **4.3.3 Practice tests**

1. Choose the environmental factors which currently don't have an effect on starting an enterprise.
  - a, the life-cycle of education is prolonged
  - b, male-female roles are rearranged
  - c, migration problems
  - d, armament programs
  - e, the decrease of the number of the active population

(answer: d)

2. Mark which factor is not of internal motivation character.

- a, utilization of existing infrastructure
- b, demand for independent decision making
- c, making income
- d, utilization of knowledge

(answer: a)

3. Mark which factor is not of external motivation character.

- a, satisfying market demand
- b, force
- c, utilization of existing infrastructure
- d, realization of new innovation

(answer: d)

4. Mark which statement is true (T), or false (F)

- a, Entrepreneurial willingness in Hungary is high. (F)
- b, Women prefer being employed to being entrepreneurs. (T)
- c, At least half of the population of Hungary don't even think of becoming an entrepreneur. (T)
- d, Half of the Hungarian enterprises don't survive longer than 3 years. (T)
- e, The process of becoming an entrepreneur lasts from the idea arising until the termination of the enterprise. (F)

5. Introduce the 3 steps of becoming an entrepreneur.

- 1. ....
- 2. ....
- 3. ....

(answer: 1. idea arising, 2. starting the enterprise, 3. operating the enterprise)

6. What factors have to be considered when the idea of an enterprise arises? Name at least 5 with one word.

- 1. ....
- 2. ....
- 3. ....
- 4. ....



5. ....

(answer: demand for time, demand for cost, skills, environment, consumer demand, resources)

7. Introduce the steps of starting an enterprise.

1. ....
2. ....
3. ....
4. ....
5. ....
6. ....

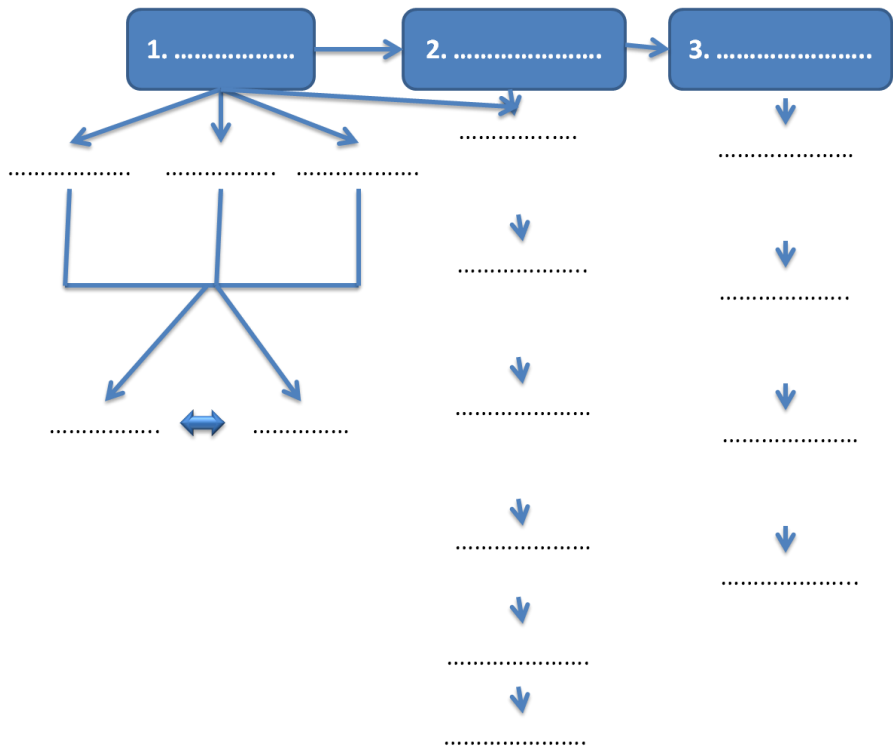
(megoldás: assessment of consumer demand, obtaining resources, planning, permissions, establishing the company, registration of the company)

8. Which statement does not characterize a project company?

- a, it can't divide the profit between the members
- b, it is set up for realizing a given objective
- c, after completing the task, the enterprise is terminated
- d, achieving long term profit is not an objective

(answer: a)

9. Introduce the steps of becoming an entrepreneur. Fill in the figure below.



## 5. LESSON: THE BASIC TYPES OF ENTERPRISES AND THE ROLE OF SUCCESS, THE FACTORS OF SUCCESS AND FAILURE

### 5.1 OBJECTIVES AND COMPETENCIES

In the lesson the student will learn the basic types of enterprises. He can categorize and characterize the particular enterprises based on business experience and entrepreneurial readiness. He can define the essence of business success. He can determine the basic factors and grades of business success. He knows the main categories of measuring success. He knows the meaning and the main features of critical success factor.

### 5.2 CURRICULUM

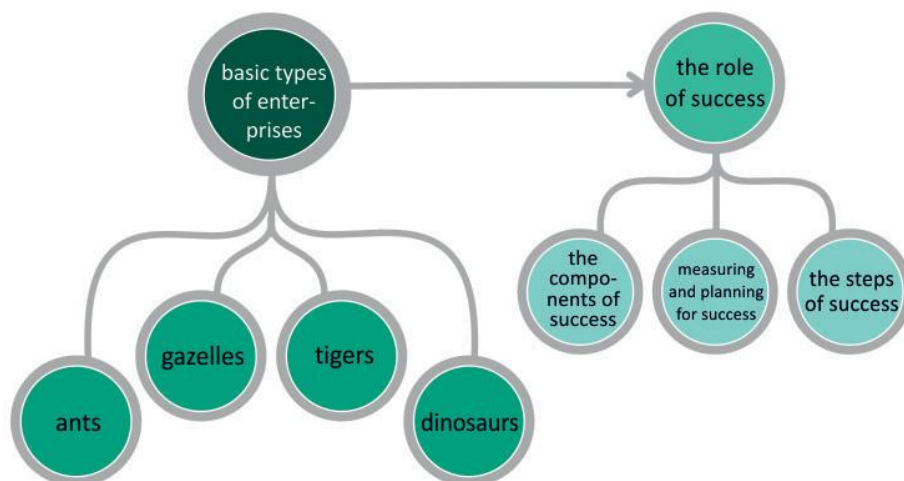


Figure 10: Concept map

#### 5.2.1 The basic types of enterprises<sup>47</sup>

Enterprises, their market character, behavior, attitude considered, can be put into four main groups. We categorize the four main groups with

<sup>47</sup> Vecsenyi János: Vállalkozás az ötlettől az újrakezdésig Aula Kiadó Budapest, 2003. 2. fejezet alapján 53-77. o. alapján

the help of a matrix, the two dimensions of which are business and operation experience, and entrepreneurial and changing readiness.

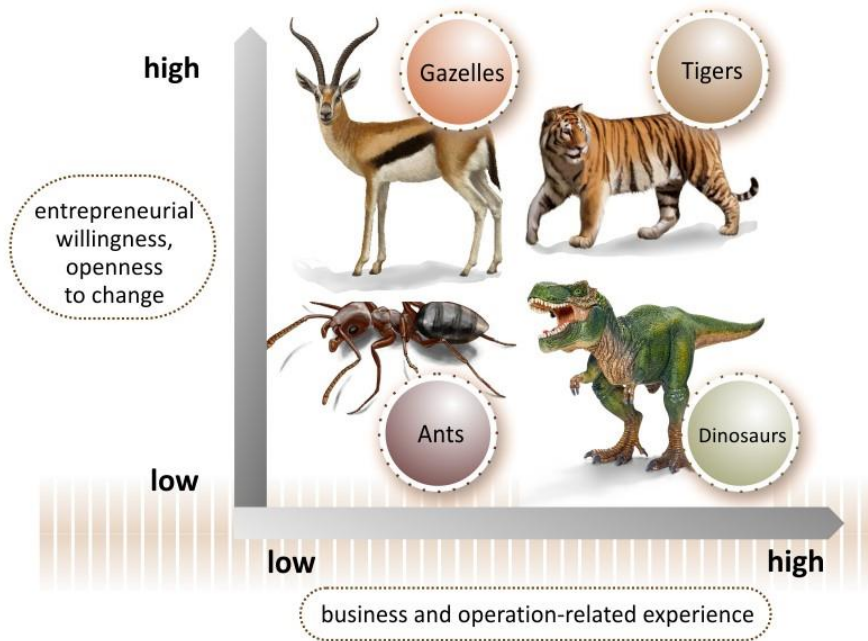


Figure 11: The basic types of entrepreneurs:

**Entrepreneurial readiness** shows the flexibility adapting to the changing environment, in a broader sense, it refers to innovation skills, the utilization of new opportunities, the level of innovative approach. Business experience refer to the past of the company, what professional and **business experience** they have for the stable operation of the enterprise, what knowledge they can 'mobilize' in a decision making situation.

The features of the different types:

#### 5.2.1.1. Ants (self-employed small enterprises)

Typically, micro and small enterprises belong to this category. Generally, they are characterized by low business experience and little entrepreneurial readiness. Many forced enterprises belong into this group. The name suggests, that they work hard, they do the usual and tried processes. The aim of the operation is to preserve the current situation (size, activity, income). Coming from this, they take few risks.

Their characteristic strategy is survival. For this they even change activity circle, so by the profile it's hard to typify these organizations. In the usually small organization the owner-manager performs several tasks and responsibilities. Work share is not planned, it shapes spontaneously. The characteristic corporate forms are the private enterprise, the limited partnership and the limited liability company. Management itself is also intuitive, usually not planned. Business decisions are always determined by the current conditions.

In the case of these organizations the economies of scale can be a important problem, so they usually calculate growth. When they achieve growth, the organization shapes spontaneously. They can survive beside the big organizations with similar profile, if they satisfy special demand, or make use of the small size (personal relationship with buyers, flexible adaptation to market conditions).

In the financial area maintaining *liquidity* (bubble: continuous solvency) is the main aim. They don't have innovation activity, or just at minimum level, and it is limited to improving products or services. Their market strategy is characterized by keeping their share, or increasing it on a small scale. Their objective can be becoming a gazelle-organization..

E.g. shoe repair small entrepreneur, non-stop garage shop

#### 5.2.1.2. Gazelles (*dynamically developing enterprises*)

The gazelle type of enterprises have little experience but grow fast. Since they have big goals, if they are not careful enough, their operation can be endangered. Characteristically, they show up in quickly developing industries (e.g. IT), but they are present in the traditional sectors too. The executives are usually prepared managers, with suitable managing skills and business experience.

They perform their activity according to a definite business plan. As for their products are concerned, they strive for high quality and often for special offer. Their sales strategy is characterized by the opening to international markets. Characteristically, they finance their operation from their own resources. They rather utilize other financial means (credit, risk capital) to realize bigger investments.

In the course of their development either they transform to be tiger organization, or disappear from the market. With their growth, the organization also shapes. Beside the one-person executive, managers control certain part areas. Characteristically, they operate in the form of limited partnerships, limited liability companies, or public limited companies.

Many gazelle enterprises face the problem of overrushing development. Then, among others, liquidity problems might crop up. Sometimes the development of the organizational system, or management style doesn't follow the increase of turnover. The marketing activity necessary for the continuous development requires significant resources. Big scale expansion can't be financed merely from profit, so most of the time the need to involve external capital makes them more vulnerable. As a consequence, the ownership structure may be rearranged.

E.g. software developing company (e.g. Google or Facebook started the same way) [link](#): You can read about the establishment of Facebook in the article in The Guardian)<sup>48</sup>.

#### *5.2.1.3. Tigers (dynamic enterprising big companies)*

These organizations have significant business experience and entrepreneurial skills, and look back on at least 15 years history. Many of them were made out of former state companies. So, the market, the activity and the organization were all given. But with the new form they could preserve their dynamism. The tigers who weren't state companies before, belonged to the gazelle type.

They often create an international organization system by outsourcing certain branches into independent divisions. Mother companies belong to the dinosaurs, affiliates belong to the tiger category.

Their strategy is continuous expansion, the search for newer and newer business opportunities. With time, they can become dinosaurs. Their characteristic business form is the division, or matrix structure, they usually operate as public limited companies with international organization system. The management of the company is complex, the number one executive surrounds himself with a significant manager organization, where the individual branches are controlled by experienced and dynamic managers. Continuous learning characterizes the organizational structure. They try to adapt continuously the organizational system to the changing conditions.

The growing size might mean the danger of losing flexibility. Since they have to keep on going energetically, they easily change the tired labor force new dynamic professionals, which is also characteristic in the case of products.

Willingness for innovation is significant, this is the basic condition of survival and of dynamic development. The emphasis is on satisfying

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<sup>48</sup> <http://www.theguardian.com/technology/2007/jul/25/media.newmedia>

demands, but also on creating need. Their marketing activity is significant. The difficulties of financing are the circulation of funds over the borders, and the management of funds properly, and also the financing of expansion.

E.g. Coca Cola, Microsoft

5.2.1.4. *Dinosaurs (traditional big companies)*

Traditional big companies with significant history belong to this group. They don't already show significant growth, they might start to decrease. In the given market their role is significant. The organizational system doesn't develop any more, operation is directed by routine based on significant hierarchy. On the long run, with this conditioning they can't remain on their feet. The chance of staying alive is changing. A frequent strategy is in this case to reorganize, withdraw branches, introduce new branches, open to new markets, perhaps to change owners. The product and activity offer is rather diversified, which is often unmanageable.

The corporate form almost exclusively is the public limited company, with strong centralized management. The company is managed by professionals having great professional knowledge and expertise, in a rather bureaucratic system. Due to this the organization is inflexible, the decision making process is slow. Due to the autocratic management style initiative gradually loses edge. They don't really pay attention to the quality of the product. Innovation willingness is smaller and smaller.

E.g. MAL Co. Ltd..

You can see the features of the four types in the table below.<sup>49</sup>

Feature	Ants	Gazelles	Tigers	Dinosaurs
	minimum growth („small is beautiful“)	fast growth	continuous growth and adaptation to changes, hunt for business opportunities	minimum growth, management conditioning to preserve size of organization and base view
	unstructured, with few levels	usually unstructured, but tending to	organized in divisions entrepreneurial	by branches and hierarchic

<sup>49</sup> Forrás: Vecsenyi János: Vállalkozás az ötlettől az újrakezdésig Aula Kiadó Budapest 2003. 76. o.

owner manager („no one does it if you don't")	become structured shaping up management knowledge, enterprising managers	business/economic units enterprising managers supporting enterprise	mostly professionals by professional area, market oriented without business and managerial qualification centralized
owner controls directly	shaping up management/supervising systems, charismatic	semi-autonomous control	
informal, individual		positive team approach	autocratic
usually depends on owner	team spirit: „we are the champions"	enterprising and attacking-hunting	deformed and destroying, workers devotion is little („little money, little football", „as long as we are paid little, we work little")
usually depends on owner	team spirit: „we are the champions"	enterprising and attacking-hunting	

*Figure 12: Basic entrepreneur types*

For the success of the operation of the types above different strategies are applied. These strategies might be successful, or less successful, but all organization focus on achieving aims, on success. But what is success?



## 5.2.2 The role of success in the life of enterprises

„We consider entrepreneur a person who thinks an opportunity is something others find a problem, or shortcomings.<sup>50</sup>”

### 5.2.2.1. Basic factors of entrepreneurial success

What do we consider success? There are several definitions for this but in entrepreneurial sense success means achieving enterprising aims. Almost all enterprises' main aim is making profit, but besides this an aim can be growth, transformation, organizational development, overtaking competitors, and a lot more. Individual goals are always defined by the company management. But there factors which are important in each company's case to achieve individual aims, for success.

These factors are as follows:

1. **Human management:** it means the staff building the organization. The workers of the organization must be managed appropriately. You have to shape up responsibility and authority areas. You have to organize the sphere of activities and how they are connected to operate efficiently. The effective manager controls the organization by giving personalized instruction to each colleague so that the best result could be achieved from the different conditions.
2. **Aim-strategy:** the aim is what the people work for together. We determine the aims in vain, the world changes fast. The key to success is the adaptive adjustment to the changing conditions. If it's missing, it leads to unsuccessfulness in the market competition on the long run.
3. **Process organization:** activities carried out by people to achieve aims. The change of strategy appears in daily activities. Production has to be adjusted to changes, if consumer demand changes. The aim is to satisfy consumer demands in the most efficient way, to organize parts of the process considering the whole of it the most efficient way.
4. **Resources:** workplace, furnishing, capital. The conditions at disposal, the obtained assets, instruments, and the existing or obtainable capital define to what extent the above mentioned process can be created or shaped. Without sufficient capital or instruments enterprising activity can't be started. It is important that you must be

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<sup>50</sup> Forrás: Vecsenyi János: Vállalkozás az ötlettől az újrakezdésig Aula Kiadó Budapest 2003. 26. o.

able to purchase as much basic material for the production that is enough to manufacture the final product, and by selling it you will have the sufficient capital for the next production cycle.

5. **Consumers:** they are the buyers who spend their money to buy the company's products, services. The most important success factor is the buyer. The buyers' satisfaction is the key to survival. If the buyers' needs were appropriately satisfied by the product or service, the company will get their money in the future too. Important: they must get what they want, and not just necessarily what they want to buy. For this, you need to know their demands, try to influence their choice and achieve their satisfaction.

#### *5.2.2.2. The grades of entrepreneurial success<sup>51</sup>*

Entrepreneurial success is interpreted at several levels. These factors mean a certain development process, so their order is determinant.

1. **Professional success** (Could we make it?): The entrepreneurs appear in the market with a new product. The product wins the recognition of competitors.
2. **Sales success** (Could we sell it?): With the new product we could boost revenues, the consumers get to know it, they buy it.
3. **Economic success** (Could we make a profit?): By selling the product we gain revenues, and profit is generated.
4. **Social success** (Did the society accept it?): If the product of the company is acceptable for the society, the company can operate steadily. Important: the product must be useful for the society.
5. **Personal, creative success** (Did I do what I wanted?): It is about the satisfaction of the entrepreneur in connection with the achievement.

#### *5.2.2.3. Measuring and planning success*

Success is usually interpreted as an abstract notion. Individual success is often a feeling ('I did it quite well'). At the same time it is also important that it has to be quantified somehow, so that the road to success could be planned.

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<sup>51</sup> Forrás: Vecsenyi János: Vállalkozás az ötlettől az újrakezdésig Aula Kiadó Budapest 2003. 26-27. o.

To measure success we get data from the books of the enterprise (accounting-financial register). The indexes of measuring success can be, e.g.:

1. Number of new buyers per year (head/year).
2. Number of lost/preserved buyers (head/year).
3. Employment of highly qualified labor force (head/year).
4. Successful introduction of new product: number of sales (unit), revenues (HUF, \$, etc.)
5. Successfully popularized programs: revenues (HUF, \$, etc.)
6. Good financing indexes: e.g. working capital, profit rate, total debt, etc.
7. Strong supply background (connections, character of power relations, bargaining power).
8. Strong sales network (number of connections, character of power relations, bargaining power).
9. Meeting quality requirements (consumer opinion, complaints, repair under guarantee).
10. Appropriate product positioning: the product was made, sold, advertised for those whose demands it satisfies best.
11. Low cost level (type of cost, fixed and changing costs, RCSP-structure (bubble: revenues-cost-security-profit).
12. Change of market structure (shaping of market proportions in time, %).

Above this several other factors have to be examined and planned for successful operation, but the circle of them have to be determined by the management, based on the strategy.

From the success factors the so called **Critical Success Factor (CSF<sup>52</sup>)** emerges. Those 3-5 factors belong to this category without which the processes, systems of the enterprise can't work efficiently. These factors affect the current situation and aims to be achieved. The definition of these factors is done with the method of business analysis. The planning of these factors is a key area of strategy. For the planning they fix CSFs in a matrix in one dimension, the critical business processes belonging to them in the other. Based on this, they determine the

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<sup>52</sup> It was created by John F. Rockart (C. V. Bullen, J. F. Rockart: A Primer of Critical Success Factors, 1981.)

connection between certain factors and the processes belonging to them. From this you can see, how many factors affect one process, or the other way round, how many processes are affected by one factor.

Success is a subjective factor, but with the help of certain indexes it can be made objective. It is important to observe, however, that success must be interpreted on the long run to found and sustain the stable and successful operation of the company.

At the end of the lesson watch a report with a successful company manager.

### **5.3 SUMMARY, QUESTIONS**

#### **5.3.1 Summary**

Enterprises can be grouped in different ways. According to one method we examine the companies based on two dimensions. One dimension is business experience, the other is entrepreneurial readiness, which means adjustment to the changing environmental conditions. Based on this we can distinguish four basic types: ants, gazelles, tigers, dinosaurs. Ants and gazelles have little business experience. The growth of ants is not significant, but gazelles have a significant growth potential. Typically, smaller organizations belong to this category. Bigger companies are tigers or dinosaurs, which operate on significant business experience. Tigers are strong enterprises, usually having an international organization, still showing significant growth. Dinosaurs want to keep their given size, significant growth can't be expected from them. These organizations significantly differ from each other, as for management style, character of managers, organizational build-up, market strategy, and the willingness for innovation are concerned.

Success means achieving the entrepreneurial aims. Success is difficult to interpret objectively, but the basic factors which are indispensable for every enterprise to achieve success can be defined. We know different levels of achieving success, which can be realized, built on one another. To measure success we discussed a few indexes.

#### **5.3.2 Self-testing questions**

1. By which two dimensions can the basic types of enterprises be categorized?
2. Which four basic types of enterprises do you know?
3. What characterizes 'ants'? Tell an example.
4. What characterizes 'gazelles'? Tell an example.

5. What characterizes 'tigers'? Tell an example.
6. What characterizes 'dinosaurs'? Tell an example.
7. What do we consider success in the case of the operation of an enterprise?
8. Define the basic factors of entrepreneurial success.
9. What grades of entrepreneurial success do you know of?
10. What indexes can use to measure success?
11. What does CSF man? How do we define it?

**5.3.3 Practice tests**

1. Introduce the basic types of enterprises. Complete the table.

.....	.....
.....	.....

.....

(answer: 10 figure)

2. Which type of organization do the features characterize?  
 ..... (answer: gazelles)

Fast growth, slightly structured organization, shaping-up enterprising managers, charismatic management style, good team spirit inside the organization.

3. Match the features with the appropriate type of enterprise.

- A) semi-autonomous control
- B) owner manager

- C) autocratic manager
  - D) destructive organizational culture
  - E) hunt for business opportunities
  - F) forming control
  - G) team spirit
  - H) informal, individual control
1. ants
  2. gazelles
  3. tigers
  4. dinosaurs

answer: 1. B) H), 2. F) G), 3. A) E), 4. C) D)

#### 4. True and False questions

1. Entrepreneurial readiness refers to the past of the company, what business and professional experience the enterprise has for stable operation, what knowledge they can 'mobilize' in decision making situation. (F)
2. Ants have a significant growth potential. (F)
3. Gazelles characteristically are present in quickly developing industries (T)
4. Tigers are characterized by divisional, or matrix structure. (T)
5. The most innovative form is the dinosaur type organization. (F)
6. Facebook is a typically dinosaur organization. (F)
8. The organizational culture of tigers is characterized by continuous learning. (T)
9. Many 'ants' enterprises face the problem of overchasing growth. (F)
10. Many of the tiger companies were separated from or were set up from state companies. (T)

#### 5. Name the 5 general basic factors of entrepreneurial success.

(answer: Human management, objective-strategy, process organization, resources, consumers)

#### 6. Name at least 5 indexes with which success can be measured.

(answer: Number of new buyers per year. Number of lost/preserved buyers, Employment of highly qualified labor force, Successful introduction of new product: number of sales, revenues,

Successfully popularized programs: revenues, Good financing indexes: e.g. working capital, profit rate, total debt, Strong supply background, Strong sales network, Meeting quality requirements, Appropriate product positioning, Low cost level, Change of market structure)

7. What factors are used in the analysis when defining CSFs with the help of a matrix?

(answer: critical success factors, critical business processes)

8. According to József Farkas, executive of Sanatmetal Kft., what is the secret of success?

## **6. LESSON: TYPES OF ENTERPRISES**

### **6.1 OBJECTIVES AND COMPETENCIES**

In the curriculum the students learn about the possible types of enterprises, and their main features. After studying the lesson, the students will be able to compare the features of private and corporate enterprises, to argue for and against one or another form. They will know the notion and types of business partnerships defined by the economic law. Based on the main features (founding capital, responsibility, founding document, supreme body, etc.), they will be able to compare the different types of business partnerships.

The students know other forms of enterprises, and can characterize each type briefly.

The students can systematize the basic features of the learnt types of enterprises, and can sum up the advantages and disadvantages of the particular types.



## 6.2 CURRICULUM

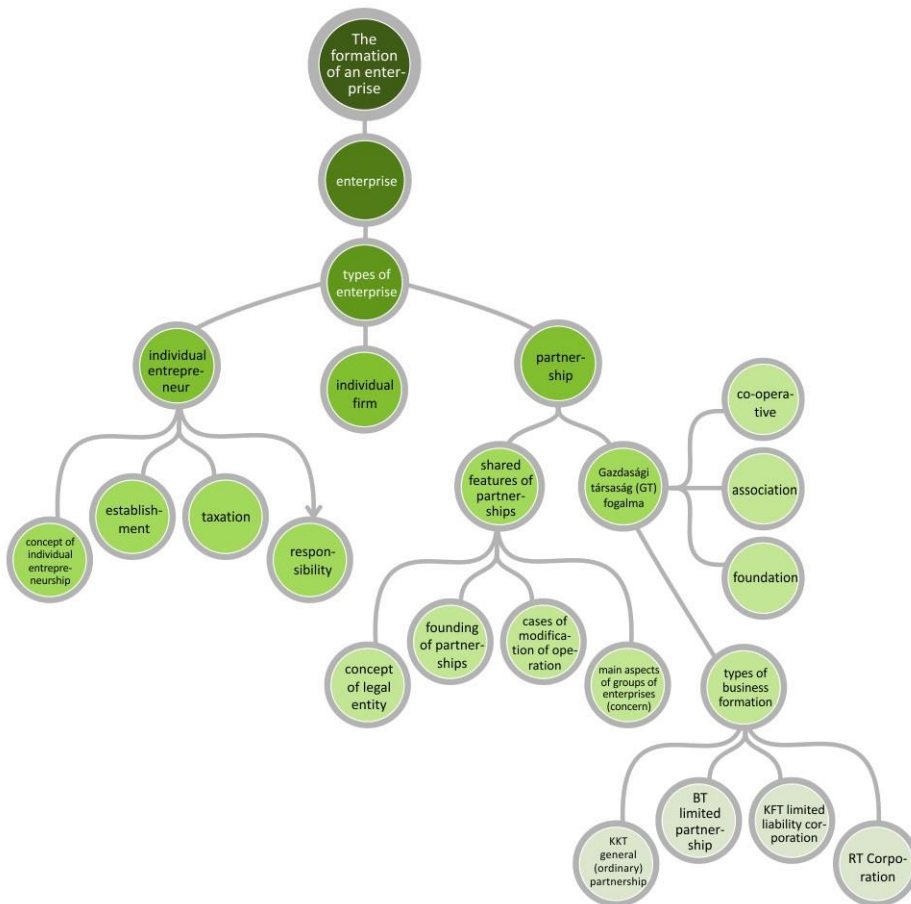


Figure 13: Concept map

### 6.2.1 The birth of an enterprise

When the idea is born in someone's head to start an enterprise it usually takes a long time to actually starting it. This period is the time for preparation. During this time several decisions have to be made. You have to decide about the following:

1. What activity do you want to do in the enterprise?
2. What consumer demand do you want to satisfy with the activity?

3. What property, instruments, stocks, labor force do you need to realize the activity?
4. Out of the resources, which one do you have, which ones have to be obtained?
5. In total how big capital do you need to start production?
6. For the starting capital how much is at disposal, and how much has to be financed from other sources?
7. How do you have to finance the missing capital? (involve a partner, taking a loan, risk capital, etc.)
8. How big responsibility does the entrepreneur take?

After answering the questions above, the first decision has to be made: shall we carry out the activity as a private or as a corporate enterprise?

#### *6.2.1.1. Private enterprise vs corporate enterprise*

In Hungary business activities directed at gaining income or wealth, or which results in them is considered entrepreneurial activity.<sup>53</sup>



*Figure 14: Company forms*

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<sup>53</sup> 1996. évi LXXXI. törvény a társasági adóról és az osztalékadóról

If you decide to have an independent enterprise, you have to decide what form you want to start it in. You can start operation on your own, or with involving partners. As a private entrepreneur you do the activity yourself, but besides you can also employ staff. In this case you are taxed by the rules of personal income tax, you show the result of your enterprise in your personal income tax return.

If the future entrepreneurs think, they will need to involve partners, it's worth starting a corporate enterprise. In this case, with at least two people voluntarily joining forces, after getting registered by the registry court, the activity can be started. Taxation is done separately from private wealth, according to the rules of corporate tax law.

Whether you start the enterprise in private or corporate form, depends on several factors, out of which the most important ones are:

- what kind of activity you want to do (commerce, service, production, etc.)
- if the entrepreneur has all the necessary competencies to do the activity,
- if the entrepreneur has enough capital to start the activity,
- if the entrepreneur can or wants to take responsibility independently for the activity or its result,
- expectably what result can be produced in the different phases of operation ( e.g. in one economic year).

### **6.2.2 The founding and features of private enterprises**

„In the area of Hungary natural persons can do economic activity carried out by taking their own economic risk, to gain profit and wealth, as private entrepreneurs”<sup>54</sup>.

Private entrepreneurs can be:

- natural persons,
- Hungarian citizens
- who are fit to act,
- who are not under penalty,
- who are not a member with unlimited liability of a private company or business partnership,

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<sup>54</sup> 2009. évi CXV. törvény az egyéni vállalkozóról és az egyéni cégről

- who fill in the registry form without mistakes, and send it in electronically, hand it in personally into any document office.

You can start private enterprise activity after performing registration. The registration of private entrepreneurs is done by the Central Office of Administrative and Electronic Municipal Services. You can get registered electronically via the so called Citizen Portal, or in person at the responsible Document Office.

In the registration you must have the following data:

- surname and last name, surname and last name at birth, mother's surname and last name, place and date of birth, address, notification address, citizenship of person to be registered,
- the main activity and other activities to be done,
- address of headquarters, or if necessary, of company seat(s), and of branch establishment(s).

Registration is free. Unlike earlier, now it is not compulsory to have an entrepreneurial identification card to run the enterprise. The certificate issued after registration is enough. If you do want to have a card you can claim one on the registry form, by paying a fee (HUF 10,000 in 2013).

If the entrepreneurs want to do an activity which needs the permission of authorities, they can't start the activity before they get it. (e.g. NPHMOS)

Private entrepreneurs calculate and report the result of their activity according to the appropriate rules of accounting and of personal income tax about each economic year after closing it until Feb 25. The return can be handed in electronically.

If any piece of registered data of the enterprise changes, or the entrepreneurs stop or terminate operation, it has to be reported to the registry authorities, but this can only be done electronically.

The private entrepreneur has unlimited responsibility for the activity.<sup>55</sup>

### **6.2.3 The common features of corporate enterprises<sup>56</sup>**

For the introduction of corporate enterprises first let's see what the notion of 'legal entity' means. The private entrepreneur in the previous

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<sup>55</sup> It's worth checking out the webpage referred to earlier  
<https://ugyintezes.magyarorszag.hu>

<sup>56</sup> Based on Act V/2013 about the Civil Code

lession is a natural person, who has certain rights from birth, e.g. he can take obligations in his own name and on his own responsibility, he can make a contract, etc. He will have these rights until his death, except his ability to act has to be limited or excluded (e.g. abnormal mental state).

Legal entity is a right given by the state, which is created on claim. In this case, an organization has rights and wealth, separated from the founders, and can take responsibilities and make a contract on behalf of the organization.

To establish a corporate enterprise you need a corporate contract (or charter, or constitution). The contract must include the following:

- name of the enterprise;
- its headquarters;
- aim or main activity of the enterprise;
- name, address or headquarters of founders;
- volume of issued capital;
- financial contributions executed to the enterprise, their volume, and the way and time of putting it at disposal;
- particulars of the first executive of the enterprise;
- period of operation of enterprise (if not indicated otherwise, for indefinite time).

If there is a Supervisory Board and/or an accountant with the enterprise, they have to be named in the charter.

**It's obligatory to set up a Supervisory Board**, if the number of full-time employees of the enterprise exceeds 200 people on yearly average. The Supervisory Board consists of three people.

The enterprise is established when getting registered by the Registry Court, and it's published in 'Magyar Közlöny' (Hungarian Gazette).

The Civil Code orders about the supreme decision making body of the enterprise. According to the main rule, it has to assemble at least. Besides, the supreme body brings resolutions concerning important strategic decisions.

The activity of the company is controlled by the management, its task is to make decisions, which don't belong to the supreme body's authority, about the operations of the company.

The operation of the organization can change in the following ways:

- **transformation:** the type of enterprise changes (e.g. from Llc. it will be a plc.), then the legal predecessor is terminated, its rights and responsibilities are executed by the legal successor
- **merger:** two or more companies merge into one organization, new enterprise is established (in the case of take-over the company taken over is terminated)
- **separation:** spin-off (the legal entity is terminated, its wealth goes to the other legal entities as to legal successors) or opt-out ( the legal entity remains, part of its wealth goes to the legal entity created by opting out, as to legal successor)
- **termination without legal successor** (e.g. after the expiry of the determined time in the charter, number of members decreased, there were no new members, etc.)

⊖ **Corporate group: Recognized corporate group, obliged to make yearly consolidated financial statement, co-operation based on common business policy determined in the control contract made by at least one ruling member and at least three members ruled by the ruling member. In the corporate group public limited company, limited liability company, union and co-operative can take part as members.**

#### 6.2.4 Types of corporate enterprises

You can get to know the main types of corporate enterprises on the basis of the new Civil Code (Act V./2013 Law about the Civil Code) valid from Mach 15, 2014.

⊖ **Business organization: Business organizations are enterprises to carry out professional common economic activity, which are established with the financial contribution of the members, which have legal entity, and in which the members share the profit and take the losses together. The profit of the company is divided according to each member's volume of financial contribution, and the losses have to be taken in the same proportion. A business organization can be established in the form of general partnership, limited partnership, limited liability company, or public limited company.**

An important rule is that natural person at the same time can be a member with unlimited responsibility in one business organization. General partnership, limited partnership and private company can't be the member with unlimited responsibility of a business organization.

#### 6.2.4.1. *General partnership*

By making a partnership contract to establish a General partnership (gp.) the members of the partnership take responsibility for executing financial contribution for the partnership for economic activity, and accept **unlimited and joint** responsibility for the responsibilities of the partnership, which are not covered by the partnership's wealth.

Its main body is the members' assembly. A general partnership can be transformed to be a limited partnership, a limited partnership can be transformed to be a general partnership without applying the rule about the transformation of business organizations, by modifying the partnership contract. For this partnership form the law doesn't order about the volume of the smallest necessary capital for the start.

#### 6.2.4.2. *Limited partnership*

Entering into a contract to establish a limited partnership (LP) the members take responsibility for executing financial contribution for the partnership's economic activity, and at least one member (general partner) accepts the responsibilities, not covered by the partnership wealth, of the partnership together with other general partners, until at least another member (limited partner) isn't responsible for the partnership's responsibilities.

Its main body is the members' assembly. For this partnership form the law doesn't order about the volume of the smallest necessary capital to start.

Its founding document is the partnership contract.

#### 6.2.4.3. *Limited liability company*

The limited liability company is a business organization which is established with equity capital consisting of capital contribution of a predetermined volume, and the members' responsibility extends to providing shares held to the company, and to other financial contributions as defined in the partnership contract. The member doesn't have to take responsibility for the responsibilities of the company.

Capital contribution is the member's financial contribution. The shares held of the members can be of different volume; the value of the particular capital contribution can't be less than HUF 100,000. Each member can have one capital contribution. The law orders that limited liability companies must have not less than HUF 3 million of starting capital (**issued capital**).

Its main body is the members' assembly. The management of the company is done by one or more managers.

Its founding document is the partnership contract.

Limited liability company can also be set up in a one-man form.

#### *6.2.4.4. Public limited company*

The public limited company is a business organization which operates with an initial capital consisting of a predetermined number and volume of shares, and the shareholders' responsibility for the public limited company is to execute the nominal or issue value of the shares for the company. The shareholder doesn't have to take responsibility for the responsibilities of the plc.

Its founding document is the charter (with a one-man company it's the articles of association).

The plc. can be publicly traded, if the shares are introduced to the stock exchange, or can be closely held, if the shares are not introduced to the stock exchange.

The total of the nominal value of all the shares is the **share capital of the plc.** The share capital of the closely held plc. can't be less than **HUF 5 million.** The share capital of the publicly traded plc. can't be less than **HUF 20 million.**

The **share** embodies the rights to be practiced in the plc. It's a marketable registered security with nominal value.

Shares that the plc. can issue:

- **The Common stock** is share which doesn't belong to the preferred, employee, interest bearing, redeemable or other, named in the charter, share type. The total nominal value of shares issued by the plc. must always exceed half of the initial capital of the plc.
- **Preferred share:** unlike other shares, provides a certain advantage for the shareholder. It can provide preferred dividend, preferred vote, option to purchase, etc.
- **Employee share:** can be issued for full-time or part-time employees of the plc. for free, or at reduced price, lower than the nominal value.
- **Interest-bearing share:** up to the maximum of 10% of the initial capital shares can be issued to entitle the holder for interest to a previously determined extent.
- **Redeemable share:** up to the maximum of 20% of the initial capital shares can be issued, the plc. has the right to purchase the shares, the shareholder has the right to sell or buy.



The main body of the plc. is the **general assembly**. The plc. is managed by the **executive board**. The executive board consists of three natural persons.

A public limited company can be established in a one-man form, too.

#### *6.2.4.5. Co-operative*

The co-operative is an organization established with capital consisting of the members' financial contribution; it is a legal entity operating on the principles of open membership and changing capital, carrying out an activity directed at satisfying the economic and social needs of the members; in which the members' responsibility extends to providing financial contribution for the co-operative and to personally participating as determined in the charter. The member is not responsible for the responsibilities of the co-operative. The activity of the co-operative can consist of sales, purchase, production and service. Members can't be recruited by public call.

The establishing document of the co-operative is the charter. Its main body is the assembly. The management of the co-operative is done by a directorate of three.

In the course of management and supervision of the co-operative, members are entitled to equal rights, independent of the financial contribution they provide.

#### *6.2.4.6. Association*

The association is a legal entity having registered members, established to continuously realize the members' common, lasting aim determined in the charter. It can't be established for economic purposes, but it can carry out an economic activity in direct connection with the realization of the aim of the association.

It can use the wealth of the association according to the aims of the association, it can't divide up the wealth between the members, and it can't provide profit for the members.

It can be established with a charter. The members, beyond paying their membership fee, are not responsible for the debts of the association with their own wealth. Its main decision making body is the assembly, which assembles at least once a year. The responsibilities of the assembly are, among others: modifying the charter; making decisions about termination, merger and separation; electing leading officials, their recall, and stating their compensation; accepting the yearly report; accepting the yearly budget; practicing employer rights over the leading official; etc.

The management of the association is done by the manager of the association, or by the presidency. Leading officials of the association are the manager or the members of the presidency. The presidency consists of three members. The presidency itself elects the president from its own members.

It is the management's assignment to do the daily tasks of the association; to make decisions about affairs in the responsibility of the management; to make reports and to submit it to the assembly; to make the yearly budget and to submit it to the assembly; to manage the wealth of the association; etc.

#### 6.2.4.7. *Foundation*

The foundation is a legal entity established by the founder to continuously realize the lasting aim of the foundation as determined in the charter. Foundation can't be established for economic activity.

Its founding document is the charter. The managing body of it is the Board of Trustees, consisting of three persons. The members of the Board of Trustees are the leading officials of the foundation. The founder can appoint a curator as a one-man managing body.

### 6.2.5 Individual company

The establishment and operation of the individual company is regulated by Act CXV./2009 (Law about private entrepreneurs and private companies). According to the law:

The individual company is an entity having no legal personality, is established by a natural person registered as private entrepreneur, which is created by getting registered in the business register. The individual company is of legal capacity, on behalf of the company can acquire rights and take responsibilities, so especially it can obtain property, enter into contract, can sue and can be sued.

The individual company is established by one person. For the foundation a charter is needed. The individual company is created by getting it registered at the registry court.

The smallest capital for the foundation of an individual company is not fixed, but if the issued capital of the individual company does not exceed HUF 200,000, then it can only be financial contribution, otherwise it can consist of financial contribution and *contribution in kind*. (bubble: contribution in kind for the issued capital, e.g. machine or lorry).

The individual company is liable for the responsibilities of the individual company with its wealth. If the wealth of the individual

company doesn't cover the claim, the member is unlimitedly liable with his own wealth.

### 6.3 SUMMARY, QUESTIONS

#### 6.3.1 Summary

At the start of enterprises the future entrepreneur must consider several factors following the idea arising. Based on capabilities and plans, one has to decide if they want to start the activity alone, as a private entrepreneur or as an individual company, or together with others as a corporate enterprise.

Below, we'll sum up the main features of the particular enterprising forms.

*Table 2: The main features of particular enterprise types 1*

<b>Form of enterprise</b>	<b>Private enterprise</b>	<b>Individual company</b>	<b>Association</b>	<b>Co-operative</b>	<b>Foundation</b>
<b>Foundation</b>	Registry in document office	Registration at Court of Registry	Registration at Court of Registry	Registration at Court of Registry	Registration at Court of Registry
<b>Deed of company formation</b>	-	Articles of association	Charter	Charter	Articles of association
<b>Minimum initial capital</b>	-	- (if under HUF 200,000 it can only be financial contribution)	-	-	-
<b>Responsibility of members</b>	unlimited	unlimited	limited	limited	limited
<b>Main body</b>	-	-	assembly	assembly	Board of Trustees
<b>Taxation form</b>	personal income tax	corporate tax	corporate tax	corporate tax	corporate tax

*Table 2: The main features of particular enterprise types 2*

<b>Form of enterprise</b>	<b>gp.</b>	<b>lp.</b>	<b>Ltd.</b>	<b>plc.</b>
<b>Foundation</b>	Registration at Court of Registry	Registration at Court of Registry	Registration at Court of Registry	Registration at Court of Registry
<b>Deed of company formation</b>	partnership contract	partnership contract	partnership contract	Articles of Association (one-man plc.: charter)
<b>Minimum initial capital</b>	-	-	HUF 3 million	closed plc.. HUF 5 million plc. HUF 20 million
<b>Responsibility of members</b>	unlimited	General partner: unlimited Limited partner: limited	limited	limited
<b>Main body</b>	member' assembly	members' assembly	meeting of partners	general assembly
<b>Taxation form</b>	corporate tax	corporate tax	corporate tax	corporate tax

### **6.3.2 Self-testing questions**

1. Considering the number of owners which two basic forms can you start an enterprise in?
2. What forms of corporate enterprise do you know of?
3. Describe the notion of business partnership.
4. What business partnership types do you know of?
5. How can you establish a private enterprise? What do you need for it?
6. How can you establish a corporate enterprise? What do you need for it?
7. Why do we call the individual company an intermediate form?
8. What characterizes the particular business partnerships according to the way of establishing, type of deed of company formation, responsibility of members, initial minimum capital and the main body?

9. When is it obligatory to elect a supervisory board?
10. Besides business partnerships, what other forms of corporate enterprises do you know of? What characterizes them according to the way of establishing, type of deed of company formation, members' responsibility, initial minimum capital and the main body?

### 6.3.3 Practice tests

1. Match the features with the forms of enterprises. One feature can only match one form.

1) Private enterprise	a) HUF 5 million is needed for establishment
2) Individual company	b) unlimited partner has unlimited responsibility
3) Limited liability company	c) created with equity capital consisting of capital contributions
4) Limited partnership	d) members have unlimited responsibility and typically take part in the activity of the company
5) General partnership	e) intermediate form between private and corporate enterprise
6) Public limited company	f) taxed according to personal income tax

(answer: a-6, b-4, c-3, d-5, e-2, f-1)

2. Fill in the table below.

Form of enterprise	gp.	lp.	Ltd.	plc.
Foundation				
Deed of company formation				
Minimum initial capital				
Responsibility of members				

(answer: see: Table 4: The main features of particular enterprise types 2.)

3. Fill in the table.

Form of enterprise	Private enterprise	Individual company	Association	Co-operative	Foundation
Foundation					
Deed of company formation					
Minimum initial capital					
Responsibility of members					
Main body					
Taxation form					

(answer: see. Table 3: The main features of particular enterprise types 1

4. Match the types of shares with their features. One feature can only belong to one type of shares.

1) common share	a) Up to the maximum of 20% of the initial capital they can order to issue shares, based on which considering the share the plc. has the right of purchase
2) preferred share	b) it can be issued up to the maximum of 10% of the initial capital
3) employee share	c) against other types of shares, it gives determined advantage to the shareholder
4) interest-bearing share	d) its nominal value must exceed half of the initial capital of the plc.
5) redeemable share	e) it can be issued free, or at a discount price, lower than the nominal value

(answer: a-5, b-4, c-2, d-1, e-3)

5. There is a mistake in the notions below (one mistake in each notion). Find and correct them.

Notion	Mistake	Correctly
In the area of Hungary <b>legal</b> persons can do regular economic activity – <b>business like</b> - carried out by taking their own economic risk, to gain profit and wealth, as private entrepreneurs	„legal”	„natural”
It's obligatory to set up a Supervisory Board, if the number of full-time employees of the enterprise exceeds <b>100</b> people on yearly average. The Supervisory Board consists of three people.	„100”	„200”
Business organizations are enterprises to carry out professional common economic activity, which are established with the financial contribution of the members, which have legal entity, and in which the members share the profit and the losses are taken <b>by the manager</b> .	„by the manager”	„by them together”
The members of the general partnership in the <b>charter</b> take responsibility for executing financial contribution for the partnership, and accept <b>unlimited and joint</b> responsibility for the responsibilities of the partnership, which are not covered by the partnership's wealth.	„charter”	„partnership contract”
The initial capital of a plc. can't be less than HUF <b>5 million</b> .	„5 million”	„20 million”

6. Name the company forms for the start of which initial capital is needed. Write in the minimum volume of it.

Company form	Minimum capital requirement
Limited liability company (or Ltd.)	HUF 3 million
publicly traded public limited company	HUF 20 million
closely held public limited company	HUF 5 million

7. Name the enterprise forms in which at least one member has unlimited responsibility.

(answer: private enterprise, individual company, general partnership, limited partnership)

8. Out of the ones below **who cannot become** a private entrepreneur? (Several answers are possible.)

- legal entity,
- Hungarian citizen,
- unfit to act,
- is not under penalty,
- individual company or unlimited member of business partnership,
- fills in the registration form without mistakes, and submits it electronically, or submits it in person in any document office.



## 7. LESSON: THE LIFE-CYCLE OF ENTERPRISES, ATTRIBUTES AND TASKS OF THE PARTICULAR STAGES

### 7.1 OBJECTIVES AND COMPETENCIES

In this lesson we learn the characteristic life of an enterprise, different theories modeling the determining cycles of growth, and the frequent problems of the particular stages. After learning the lesson, students will be able to define the current state of development of the given enterprise, the essential factors of observation, and their effect on the growth of the enterprise. They can highlight the problems of the given stage, can word suggestions for the solution, for their elimination.

### 7.2 CURRICULUM

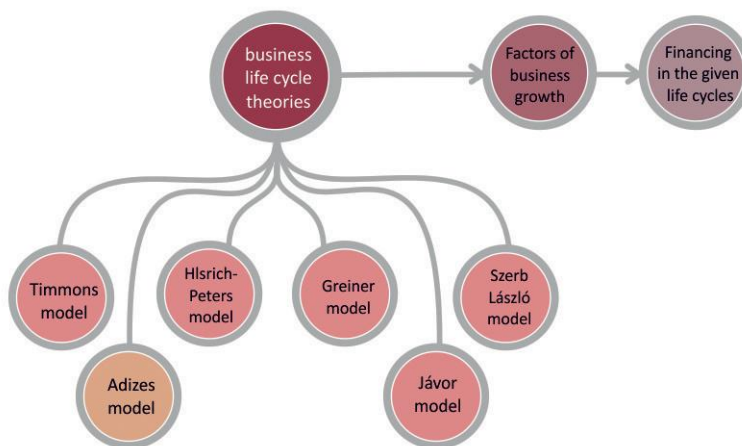


Figure 15: Concept map

#### 7.2.1 Corporate life-cycle theories

Enterprises, beginning from the idea arising, to the termination of activity go through a long process and several development stages. Modeling of life stages appeared in other fields of economic science, too. You can see product life-cycles in marketing, industry branch life-cycle model in strategic planning, different cycle theories in macroeconomics.

In business economics **life cycle** refers to how the attributes change from the foundation of the enterprise to its termination. The first life-cycle models appeared from the 1960s, after this several theories were born,

most researchers divided the life-cycle of enterprises into 4-5 cycles. We are going to learn about some in this chapter.

7.2.1.1. *The Timmons model*

Jeffrey A. Timmons<sup>57</sup> grouped enterprises according to time ('age'), revenues, and number of staff. Based on this, he divides the life of enterprises into 5 stages. Based on his typology, enterprises are characterized by:

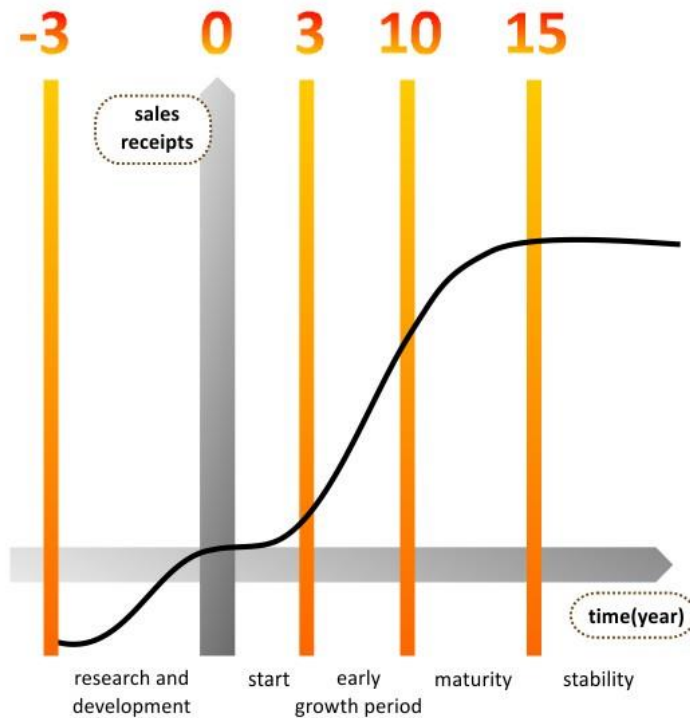


Figure 16: *Timmons life-cycle model*

**Stage 1: Research and development stage:** 1-3 years prior to the establishment of the enterprise. At this stage the enterprise doesn't exist

<sup>57</sup> He explained his theory in his book *New venture creations* published in 1977, then his book *New Venture Creation: Entrepreneurship in the 1990s* was published in 1990. (Irwin, Homewood), His book published in 2003: J.A. Timmons – S. Spinelli: *New venture creation Entrepreneurship for the 21st Century* McGraw-Hill. International Edition, 2003.

actually, the future founders are researching the helping and interfering factors of the feasibility of realizing the idea. This stage doesn't really mean real risk, since here we can't talk about the operation of the enterprise. Timmons says this is the most risky stage, it puts an exhausting burden on the management, and requires a lot of energy.

**Stage 1: „Start-up” – Starting phase:** *the first 3 years after establishment.* At this stage enterprises start operation. They establish the enterprise, start manufacturing or servicing, look for sales opportunities for the products, and start marketing activity.

**Stage 3: High-growth stage – Early growth phase:** 4th-10th years of the operation of the enterprise. In this period, turnover grows increasingly, the organization, operation, capacity of the company has to be adjusted to this growth level. Timmons says this stage brings decision making difficulties for the founders, success depends on their attitude. The condition of growth is how they can distribute responsibilities and authorities.

**Stage 4: Maturity – Maturity phase:** *11th-15th year of the operation of the enterprise.* At this stage the pace of growth decreases, turnover reaches its maximum. Timmons says, the primary aim is to sustain profitably.

**Stage 5: Stabilizing phase:** *the operation of the company after the 15th year.* At this stage the company is managed by the usual mechanisms. Turnover is stable, sustainable.

Timmons thinks, to enter into the following stage management decision is needed. The interesting thing of the model is that it doesn't calculate with the decline and termination of the enterprise, though we saw earlier, that only half the enterprises sustain for 3 years (or at least in Hungary it is so).

#### 7.2.1.2. Hisrich-Peters model

The creators of another model were Robert Hisrich and Michael Peters<sup>58</sup> who further developed the Timmons theory. They divided up the processes of the first, research and development stage. They summed up their company growth theory like this:

**1. Idea phase:** collecting the ideas of new products, services, the basic selection of ideas goes on at this stage. The new ideas have to be selected by sustainability.

**2. Product vision phase:** at this stage a preliminary business plan is made concerning the product to be realized.

<sup>58</sup> R. Hisrich, M. Peters, D. Shepherd: Entrepreneurship McGraw-Hill Irwin; 9 edition 2012

**3. Product development phase:** the prototype of the product is made at this stage.

**4. Pilot production phase:** At this stage small scale production starts, the operational test is done.

**5. Preliminary product trial phase:** at this stage they test the expectable acceptance of the product in the test market.

Then come the phases similar to product life-cycle known from marketing:

**6. Introduction**

**7. Growth**

**8. Maturity**

**9. Decline**

Except for the last stage, they can be compared to the Timmons model. At the stage of decline the enterprise can't maintain the earlier sales turnover, the number of buyers, the volume of the goods sold, decreases to a greater or lesser extent. At this stage two basic solutions are applicable: with significant innovation the declining process can again be boosted, or in the lack of it, the generation of further losses can be avoided by terminating the enterprise.

#### 7.2.1.3. László Szerb model<sup>59</sup>

László Szerb made up his model based on the 1993 work of Mount – Zinger – Forsyth 1993<sup>60</sup>.

**1. Beginning:** usually the first year of the enterprise.

**2. Start:** the first to third year of the enterprise.

**3. Early growth:** this stage is characterized by the increase of demand, revenues, profit. All this requires the company to rethink and change strategy.

**4) Expansion:** intensifying competition, rivalry is characteristic. Due to increasing demand for money, the modification of marketing strategy and the rethinking of financing growth come to the foreground.

**5) Maturity**

**6) Innovation or decline.**

Szerb calls Stages 1-2 *introduction*, and Stages 3-5 are called *growth*.

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<sup>59</sup> Zsupanekné Palányi Ildikó (2007): A vállalati növekedés a vállalati életciklus-modellek tükrében. Budapesti Gazdasági Főiskola, Magyar Tudomány Napja munkája alapján

<sup>60</sup> Mount: Organizing for Development in the Small Business (Long Range Planning) 1993. 113. o.)

#### 7.2.1.4. Adizes model<sup>61</sup>

According to Ichak Adizes 1992 model the development of enterprises is similar to the life of humans. The two chains of the bell curve illustrated in the co-ordinate system are time past and the vitality of the organization. Adizes divides the life of the enterprise into two basic stages: the periods of growth and aging, which are connected by stabilization.

Adizes says, company growth can be described with the two important factors in interaction with each other, flexibility and maneuverability. A young organization is easily convertible and flexible, like a baby, but it is less maneuverable, and its future is not calculable. As time passes, an older organization is more and more easy to maneuver, but it obviously loses flexibility. Growth and aging don't depend on size or time, *the measure of growth is if an organization can beat bigger, difficult problems on its way*. Aging, however, is interpreted as a process of decline, when the organization can't overcome difficulties.

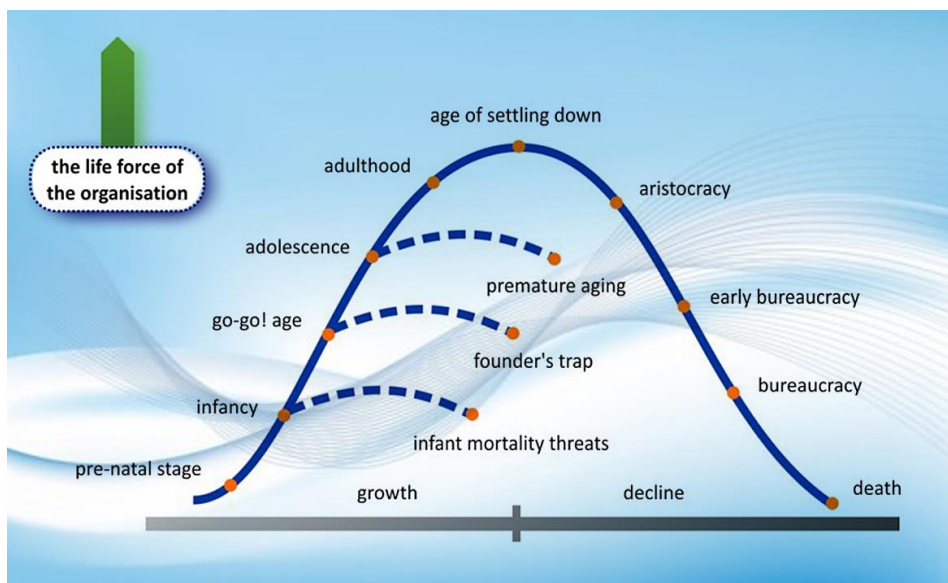
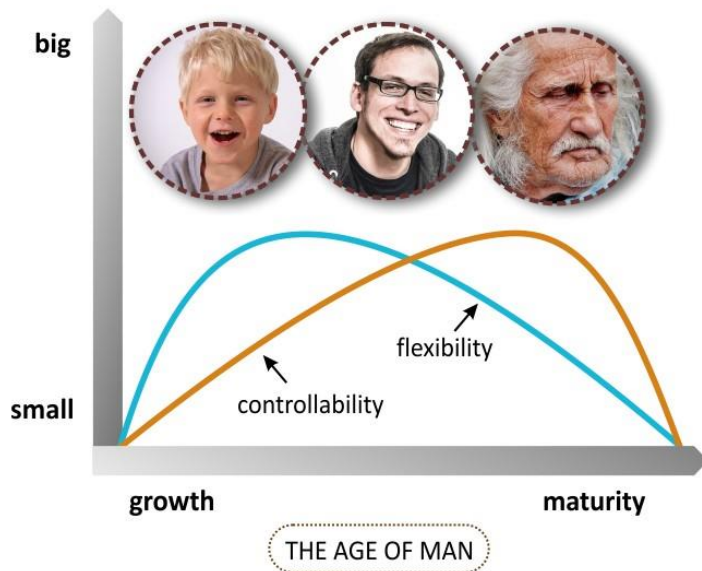


Figure 17: Adizes model

<sup>61</sup> Zsupanekné Palányi Ildikó (2007): A vállalati növekedés a vállalati életciklus-modellek tükrében. Budapesti Gazdasági Főiskola, Magyar Tudomány Napja munkája alapján

The character of growth, according to Adizes, depends on maneuverability and flexibility. Maneuverability is smaller at young age, the „old” organization can be maneuvered more easily. Flexibility works the other way round. A younger enterprise is more flexible than an old organization.

This connection is shown in the figure below:



*Figure 18: Connection between maneuverability and flexibility in the Adizes model*

Adizes in his model names the aims of the particular life stages characterizing the enterprise best:

- **courting**: satisfying needs
- infancy: cash
- stage of youthful mobility: sales and market share
- adolescence: profit
- **the prime of life**: sales and profit
- **stage of stability**: preserving status quo

- aristocracy: ROI<sup>62</sup>
- **death**: miracles

Adizes' model served as base for several further theories, many researchers used it as a basis for their own research.

#### 7.2.1.5. Greiner model<sup>63</sup>

Greiner approached growth from the business management side. In his model he describes the life of companies as the alternating changes of evolution and revolution periods. In the evolution period company growth is continuous, undisturbed, whereas in the revolution period the management has to tackle obstacles, which disturb the pace of growth. Growth depends on how the organization can manage the emerged problems. He highlighted 5 key factors in the operation of the model:

**The age of the company:** here he agrees with Adizes, a young organization is flexible, an aging one has rather perpetuated behavior patterns, thus it needs sizable ('revolutionary') changes to get ahead.

- **Company size:** as the size of the company grows, management, co-ordination between the participants becomes more and more difficult.
- **Evolution stages:** problems of the evolutionary growth periods can be solved with tested, routine methods.
- **Revolution stages:** in every revolutionary period the organization has to tackle a new problem, the management has to adapt to this, they can't rely on earlier, tested methods.
- **The pace of growth in the sector:** beyond the own potentials of the company, also the pace of growth of the sector will influence the length and frequency of evolutionary and revolutionary periods of the enterprise. In a fast-growing sector also the enterprises belonging to it have to react to the challenges fast.

Greiner, based on this, set up his model in a two-dimensional system of co-ordinates, on one axis of which there is the age of the company, on the other there is its size. He divided the development of the enterprise into 5 stages:

<sup>62</sup> buborék: ROI index (Return of Investment): index used to calculate return on investment. It shows what proportion of the taxed profit (%) the „capital stock immobilized long-term” makes attainable.  $ROI = \text{taxed profit} / \text{immobilized capital stock}$ .

<sup>63</sup> Zsupanekné Palányi Ildikó (2007): A vállalati növekedés a vállalati életciklus-modellek tükrében. Budapesti Gazdasági Főiskola, Magyar Tudomány Napja munkája alapján

1. **Creativity:** in the initial stage they shape the organization based on market demand, and the organization (due to its size) can quickly adapt to these demands. Communication inside the organization is accidental and informal. In this period the management don't consider profit management important. As a consequence, a problem defined by Greiner characteristic for this stage, emerges: management style crisis. The condition of getting further ahead is making a professional management.
2. **Management:** They start to shape up the organizational system consciously, spheres of activity, hierarchical responsibility and authority spheres are created. Division of labor develops. With the division of authority spheres a new problem crops up, clashes between management levels, the autonomy crises. If the organizations can manage the decentralization of management, they an step on to the next level.
3. **Delegating:** With growing size, the load of the management also grows. They have less and less insight into the direct processes, they get information from their subordinates' reports, instead of 'manual control' they shape out automatisms, and personally they rather focus on strategy. Crisis comes when the company top management loses direct control over part areas and they try to get it back. This is the supervision crisis.
4. **Co-ordination:** To solve the supervision crisis the top management appoints managers into the system, whose task is to keep contact with the part areas, so to help control. They improve the organization by taking certain functions under central control, but they keep operational control in part areas. The system of the organization becomes more and more difficult and inflexible, the lack of trust between the management levels further intensifies the institutionalization of processes, the next crisis to come is the bureaucracy crisis.
5. **Co-operation:** By creating the knowledge management system, they use more and more effective methods to solve the emerging interpersonal problems. The significance of team work, team building comes into the foreground. Instead of using the routine incentives, they use new ones (e.g. incentive trips) In this period Greiner mentions the continuity crisis, routine processes rule the operation, the difficult organizational system is more and more inflexible, it reacts slower and slower to the emerging challenges.



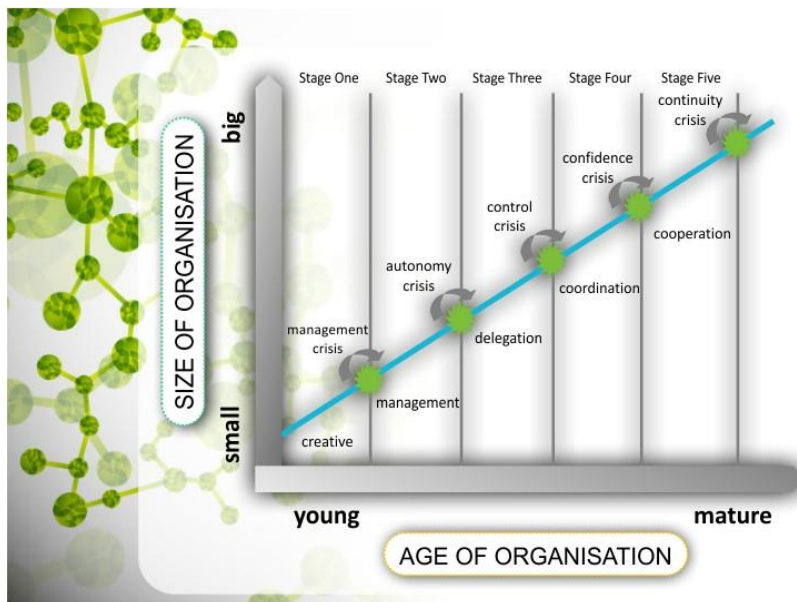


Figure 19: Greiner's growth model

#### 7.2.1.6. Jávor's model<sup>64</sup>

Among the Hungarian researchers, besides Szerb, we want to highlight István Jávor's 1993 model. He examines enterprises from the point of view of organizational psychology, he introduces the organizational problems of growth. He divides the life-cycle introduced earlier into 12 stages. The decisions made in transitional periods, just like with Greiner, are critical ones. Since based on the decisions made, the enterprises can have very much different life, he calls his model the ideal life.

1. Preparatory stage: business idea, the examination of availability of resources.
2. Establishment: decision about the organization, the initial profile, work share.
3. Market acquisition: formation of business connections on input and output side.

<sup>64</sup> Zsupanekné Palányi Ildikó (2007): A vállalati növekedés a vállalati életciklus-modellek tükrében. Budapesti Gazdasági Főiskola, Magyar Tudomány Napja munkája alapján

4. Slow growth: first stabilization stage, first opportunity to accumulate.
5. Preparation for great headway: the great headway is realized by the sudden increase of sales, or through sources advanced. In this period the increase of profit is the main company aim.
6. Accumulation: the stage of rapid development, the organization, staff number, turnover, profit grow, but after a time the organization starts to muddle.
7. Crisis phenomena: financial problems, trouble in organizational value system, which lead to ownership crisis. Power relations between the owners start to get rearranged.
8. Consolidation: conscious organizational, ownership rethinking, they rearrange the internal relationships of the organization: decision making system, financial and accounting system, etc.
9. Professional diversification: they expand the frames of activity, but it's connected to the profile of their own.
10. Diversification of capital: exclusively for profit making purposes, they invest the generated profit into other enterprises.
11. Extension of the organization system: the entrepreneur connects several organizations, e.g. franchise, networks of agents.
12. Political network: the entrepreneur opens to politics, public administration, the civil sphere.

### **7.2.2 Company growth**

As you can see in the theories introduced earlier, growth is influenced by many factors. You can approach it from different sides, size, organization, control, and many others, but it's very difficult to set up one single model. László Szerb summed up some of the more important factors influencing growth in a figure. When making it he relied on theories by other authors, and also on his own empirical research<sup>65</sup>

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<sup>65</sup> Dr. Szerb László: A növekedés meghatározó tényezői a magyar kis- és középvállalati szektorban A Magyar Közgazdasági Egyesület Konferenciája 2007 alapján

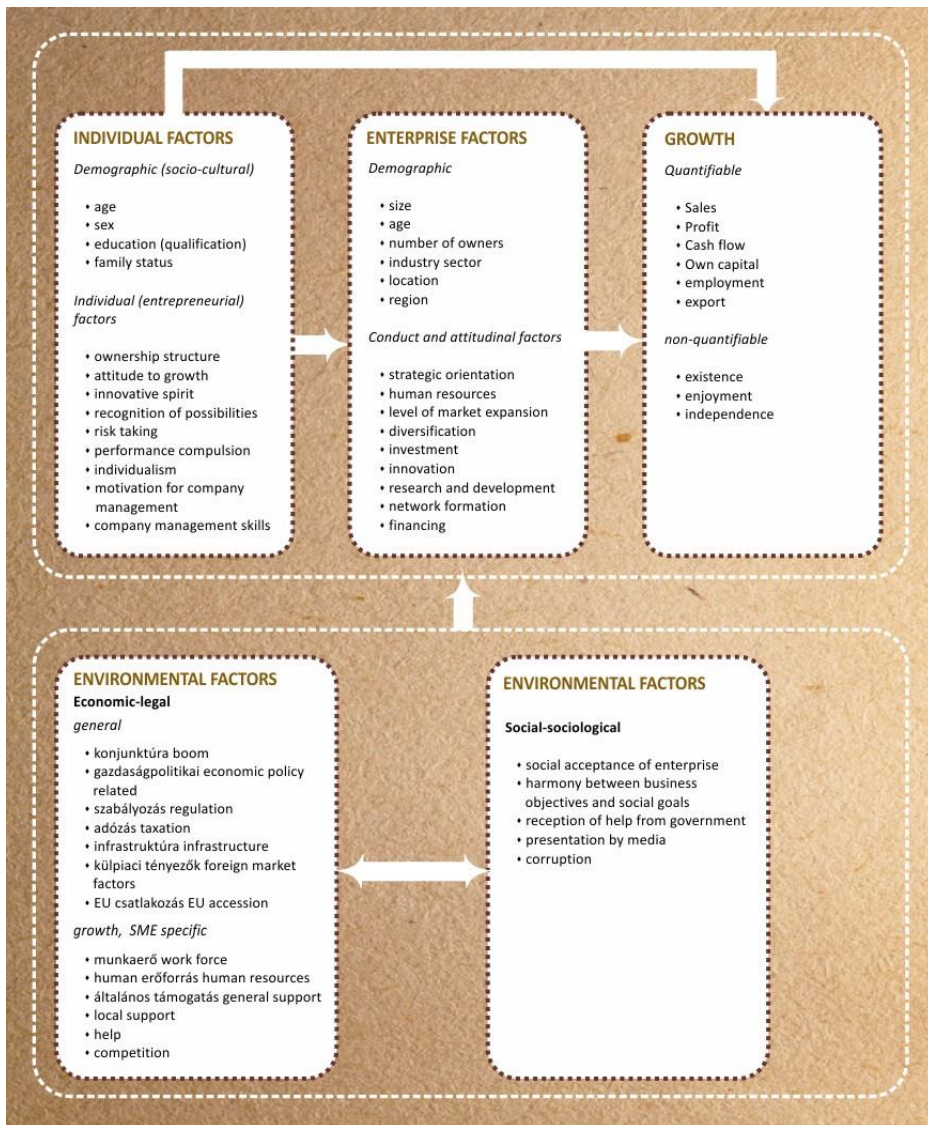


Figure 20: The Szerb model of the factors of company growth

### 7.2.3 Financing in particular life-cycles

We examined the factors of growth, and also showed what organizational, management problems the enterprise has to struggle with it the particular cycles. After this, we briefly touch upon the different

financing tasks of the enterprise in the particular life-cycles. We interpret the growth life-cycle in 5 steps.

### **Stage 1: Start-up company**

In this stage, enterprises are usually in the red, since they have to provide the capital necessary for the start, the return of which will only be realized later. The management and the owner(s) are usually the same persons, the enterprise has only as much means as it needs for the start.

The aim of financing is to provide wealth to start the operation. Financing here is investment-driven, it's defined on the basis of strategy what financial means are destined to which tasks. If the owner's wealth is not enough for this, often they have to use external resources of significant size (e.g. loan, venture capital)<sup>66</sup>. Demand for capital is high, income making ability is low.

The risk of the stage is whether the enterprise becomes successful, initial investment is refunded or not.

### **Stage 2: Growth**

In this stage the company is in the black. With the pace of growth (developments, capacity expansion) the demand for financing significantly grows. Growth is hard to follow from internal sources (owner's capital, profit, tax savings), so in this stage there is also significant demand for external sources<sup>67</sup>. Here the bank loan and the venture capital are financing forms completing each other.

The basis of financing strategy is competitive position and human resources strategy.

The risk of the stage is excessive growth, which the equipment, the capacities and the organization system can't keep up with.

### **Stage 3: Fast growth**

In this stage the enterprise generates significant profit, which can be ploughed back into the means financing growth. The position of the company in the market is significant, stable, it has a broad clientele, and it's increasing, which envisages further developments. Demand for means grows. The internal source ratio is growing, less and less external source is needed, their term decreases. The owners' wealth proportion

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<sup>66</sup> Since the enterprise is still new, for long tm tasks they can only gat short term loans, so they rather turn to venture capital.

<sup>67</sup> In this stage enterprises can claim for a special type of capital, for the companies which have already started, and have been growing: it's the early stage capital. With the expertise of the capitalist, it also contributes to decreasing the investment risk.

grows in the total capital. In external financing the role of the loan is evaluated higher and higher.

#### **Stage 4: Maturity**

The company has strong market position, its clientele is stable, it's characterized by profitability. Growth is slow, or stagnates. The enterprise has already created its market, the growth of which is slight. Marketing actions serve to maintain consumer interest. The enterprise has a significant stock of means, to maintain it there is a demand for financing, the demand for means for the growth is not significant. The task of financing is to maintain stable operation and liquidity. The internal sources mean the base for this, short term external sources might emerge as a demand.

#### **Stage 5: Decline**

The company loses market position, clientele and turnover decrease. Innovation is not significant. Investments are used up, downsizing characterizes the company. The task of financing is covering quits and ownership demands. Using external sources wouldn't be refunded, so in this stage it is not at all advisable.

### **7.3 SUMMARY, QUESTIONS**

#### **7.3.1 Summary**

In this lesson we introduced the general characteristics of company growth and development, based on the theories of several researchers. Researchers described the features of the particular stages, some models also include the periods of the stages. First we learnt about the Timmons model, in which the life of the company is divided into 5 stages:

- Research and development stage
- „Start-up”
- High-growth stage
- Maturity
- Stabilization

In their model the authors Hisrich-Peters divide the preparation phase preceding company establishment into several parts, and based on this they define the following life-cycles:

- Idea phase
- Product vision phase
- Product development phase
- Pilot production phase
- Preliminary product trial phase
- Introduction
- Growth
- Maturity
- Decline

László Szerb defined the following phases:

- Beginning
- Start
- Early growth
- Expansion
- Maturity
- Innovation or decline.

Adizes created the model used as a starting point in many researches. The stages of this are as follows:

- courting: satisfying needs
- infancy: cash
- stage of youthful mobility: sales and market share
- adolescence: profit
- the prime of life: sales and profit
- stage of stability: preserving status quo
- aristocracy: ROI
- death: miracles

Greiner highlights 5 factors along which he examined growth:

- Age of the company
- Size of the company
- Evolution stages

- Revolution stages
- Pace of growth in the sector

Based on this, he divided his organization management model into the following stages:

- Creativity
- Management
- Delegating
- Co-ordination
- Co-operation

Finally, we learnt the Jávör model, which indicates 12 life stages, a lot more than any earlier models. They are as follows:

- Preparatory stage
- Establishment
- Market acquisition
- Slow growth
- Preparation for great headway
- Accumulation
- Crisis phenomena
- Consolidation
- Professional diversification
- Diversification of capital
- Extension of the organization system
- Political network

Szerb summed up the main conclusions of authors he examined considering which factors influence, or define company growth, its process and dynamism.

Finally, we examined company growth from the financing side, too. We surveyed what kind of financial processes characterize the particular stages, and what financing means can mean a solution for the emerging problems of the given phase.

### **7.3.2 Self-testing questions**

1. What does a 'life-cycle' mean in the life of the enterprise?
2. On the basis of what criteria did Timmons examine enterprises?
3. What stages did Timmons divide the company life-cycle into?
4. In what way is Hisrich-Peters' model different than that of Timmons'?
5. What stages did László Szerb define, and what time intervals did he assign to them?
6. Introduce Adizes' model, the features of the particular stages?
7. How do manageability and flexibility form depending on time in Adizes' model?
8. What are the key factors of growth according to Greiner?
9. What stages did Greiner divide the life of companies into?
10. Introduce the 12 stages of the Jávör model.
11. How did László Szerb sum up the factors influencing company growth?
12. What kind of financing tasks and possibilities do companies have in the particular life stages?

### **7.3.3 Practice tests**

1. Complete the figure below based on Timmons' life-cycle theory. What are there on the two axis? What kind of stages can you see in the figure? Write them in.



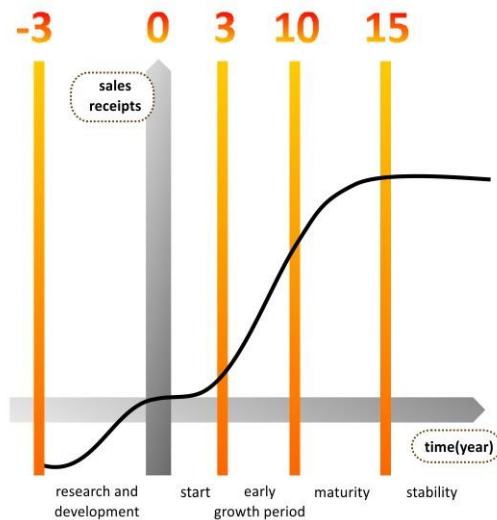


Figure 21: Timmons life-cycle model task

(Answer: 16)

2. Match the appropriate life-cycles with the authors who created them.

Life-cycles	Author
1) beginning, start, initial growth, expansion, maturity, innovation or decline ...	a) Timmons
2) courting, infancy, youthful mobility, adolescence, the prime of life ...	b) Hisrich-Peters
3) preparatory phase, establishment, market acquisition ...	c) László Szerb
4) R&D, start-up, high-growth stage, maturity, stabilization ...	d) Adizes
5) creativity, management, delegating, co-ordination, co-operation ...	e) Greiner
6) idea, product vision, product development, pilot production, preliminary market trial ...	f) Jávör

(answer: 1) c), 2) d), 3) f), 4) a), 5) e), 6) b))

3. Mark the statements if they are True (T) or False (F).

1. Timmons grouped enterprises according to time, revenues and number of staff. (T)
2. The Hisrich-Peters model divides the life-cycle of the company into 8 phases. (F)
3. In László Szerb's model the initial phase is characterized by the growth of demand, revenues and profit. (F)
4. Timmons says, the starting phase of the company is the first 3 years after establishment. (T)
5. Adizes created his model at the end of the 1990s. (T)
6. Adizes thinks, the character of growth depends on time and flexibility. (F)
7. Szerb thinks, growth depends on how the organization can solve the problems emerged earlier. (F)
8. Greiner thinks the pace of growth in the sector influences how the life of enterprises are formed. (T)
9. In the delegating stage, Greiner says, the top management assigns managers into the system to solve the supervision crisis, whose task is to keep contact with parts of the company so to help supervision. (F)
10. In Jávör's model, in the consolidation stage conscious organizational, ownership rethinking is characteristic, and they also rearrange the internal relationships of the organization. (T)

4. Match the appropriate life-cycle stages with the financing tasks!

<b>Financing task</b>	<b>Life-cycle stage</b>
1) Start	a) In this stage the results of the company turn into positive.
2) Growth	b) The task of financing is to maintain stable operation.
3) Fast growth	c) The task of financing is to provide costs for quits and ownership demands.
4) Maturity	d) In this stage enterprises are usually in the red, they have to provide the capital at disposal, the result of which is only realized later.
5) Decline	e) The position of the company in the

	market is significant, stable, the internal source ratio of financing is growing.
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(answer: 1) d), 2) a), 3) e), 4) b), 5) c))

5. Complete the statements with the surname of those, whose theory it is connected to.

The main factors influencing growth ..... summed up in a figure. (Szerb)

In the professional diversification stage, ..... says, the frames of activity are expanded, but it is connected to the profile of their own. (Jávor)

..... approached growth from the side of management control. (Greiner)

In .....’s theory in the life of an enterprise, evolutionary and revolutionary periods follow one another. (Greiner)

The character of growth, ..... says, depends on manageability and flexibility. (Adizes)

According to ..... in the stage of pilot production small-scale production starts, and the test of operation is done. (Hisrich-Peters)

In .....’s life-cycle model the last stage is innovation or decline. (Szerb)

1. .... thinks a young organization can be transformed easily and is flexible, like an infant, but it’s less manageable, and its future is not calculable. (Adizes)
2. .... with Adizes that a young organization is flexible, whereas an aging one has routine behavior patterns. (Greiner)
3. In .....’s model 12 life stages are separated. (Jávor)

6. Match the characteristic financing sources with the particular life-cycle.

Life-cycle	Characteristic source
1) Start	a) internal source and short-term loan
2) Growth	b) internal source in growing

	proportion, and loan
3) Fast growth	c) bank loan and venture capital
4) Maturity	d) only internal sources
5) Decline	e) venture capital

(answer: 1) e), 2) c), 3) b), 4) a), 5) d)

7. Make a drawing in your exercise-book about the connection between management and flexibility in Adizes' model. Mind the marking of the axes.

(answer: 03\_07\_K04)

8. Describe Greiner's growth model. Mind the marking of the axes and the stages.

(answer: 03\_07\_K05)

## 8. LESSON: THE BASIC FUNCTIONS OF ENTERPRISES

### 8.1 OBJECTIVES, COMPETENCIES

In this lesson the students learn about the basic functions of enterprises, the most important endeavors, which equally characterize these enterprises, independent of their nature.

In the lesson we show those main company activities which the enterprise carries out to achieve its aims. Though the tasks can factually be different with each organization, the basic functions can appear in any enterprise, so knowing them is an important part of company planning and management.

When the students learn the lesson, they will be able to draw up the necessary activity system of the given company, identify their basic functions, and to help the management concerning activity co-ordination.

### 8.2 CURRICULUM

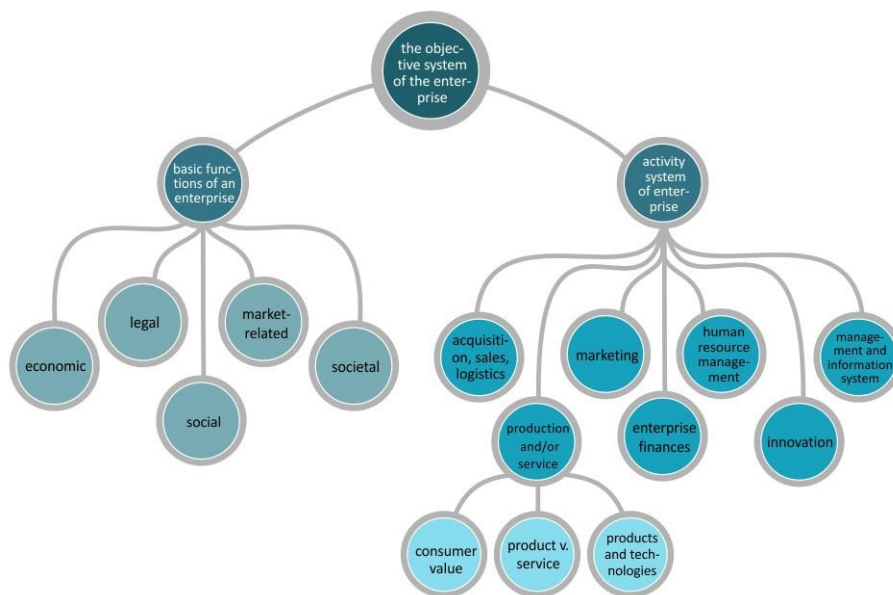


Figure 22: Concept map

### 8.2.1 The basic functions of enterprises

Based on their potentials, enterprises can be very much different. A different size, organization, sphere of activity, pace of growth, strategy, etc. characterizes them. But all enterprises have basic functions, their proportions, priority may differ inside the enterprises, but appear with all role players in some shape. All company functions work to achieve the basic aims. First and foremost, they have to satisfy consumer demand the best possible way, and of course, they must make profit.

The **most important aims** in the life of the company may be as follows:

- satisfying consumer demands
- gaining profit, increasing wealth
- lasting survival (except for project companies)<sup>68</sup>
- growth, development
- production, sale, development of goods, services
- reasonable risk taking
- effective relationship with the internal and external environment
- accomplishing social mission
- continuous liquidity

Accordingly, the **basic functions** of companies are as follows:


- **Business basic function:** gaining profit, increasing wealth.
- **Welfare basic functions:** providing jobs, ensuring the living and personal development of employees.
- **Social function:** converting resources into output (of product or service), thus satisfying consumer demands, effectively fitting into the social environment, this way the company is the basic business unit of the society. Environment protection is also a social function.
- **Legal function:** ensuring legal, lawful operation, legitimate relationship with the environment.

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<sup>68</sup> Project companies are made for achieving a determined aim, when it's completed, they cease.


- **Market function:** providing supply (in the consumer, producer, distributor market), creating demand (in the resource market), influencing market prices and processes.

To accomplish functions, the company carries out different activities. The bigger the organization, the more difficult the system of activities is. A one-man entrepreneur can do the production activity himself, perform the duties of management, does the accounting, handles legal affairs.

 *E.g. an entrepreneur making fried dough does the purchase of basic material, makes and sells fried dough, and can do the accounting if he knows how to do it.*

Functions merging to this extent make it even more difficult for the companies as they grow (revenues, number of staff, product scale). As the enterprise grows, functions to be performed get more and more separated, and in the particular areas specialized professionals appear (accountants, marketing professionals, manufacturers, quality controllers, etc.) and the management (heads-of-department, middle management) connected to it will also be created.

Big companies already operate a complex system of activities, each has its own management, a separated but integrated organization.

 *At the link below you can see the organizational structure of ZF.*

[http://www.zf.com/corporate/en/company/organization/divisions\\_business\\_units/divisions\\_business\\_units.html](http://www.zf.com/corporate/en/company/organization/divisions_business_units/divisions_business_units.html)

## **8.2.2 The activity system of enterprises**

Enterprises depending which area they operate on (trade, manufacturing, service, etc.), create a different activity system. But their main activities are more or less the same. In the following, we briefly introduce those areas of enterprises which appear at most of the organizations.

### *8.2.2.1. Production and/or service*

The basic motivation of producing products or services is satisfying consumer demands in the most effective way possible. The consumers are willing to buy the product because it represents value for them.

### 8.2.2.1.1. Consumer value and its dimensions

☞ **Consumer value is the consumers' subjective opinion of the product, as for to what extent it met their expectations.**<sup>69</sup>

Consumer value is characterized by the following features:

- **consumer specific:** the same product can be evaluated differently by the particular consumers
- **changing:** the same consumer can have different expectations at different times
- **is under continuous control:** the multitude of consumers constantly compares the product with their expectations
- **influences the present and future demand for the product:** based on the expectations before shopping, and the experience after shopping.<sup>70</sup>

We differentiate three basic dimensions of consumer value, which significantly influences the company activity:

1. **Use value:** it consists of features of the product which make it suitable for satisfying demand.

☞ *E.g. in the case of a loaf, it's size, material, color, water resistance, etc.*

4. **Place value:** it expresses that the product is available for the consumer, it is there where demand satisfaction can be carried out.

☞ *E.g.: In the case of a loaf, it's available in the shop located where the consumer lives. This dimension is getting broader with the extending possibilities of Internet shopping, since products physically far away from the consumer become also available. E.g. ordering a Kindle book reader from the USA.*

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<sup>69</sup> Chikán Attila – Demeter Krisztina: Az értékteremtő folyamatok menedzsmentje Aula Kiadó Budapest 2001. 6. o.

<sup>70</sup> Chikán Attila – Demeter Krisztina: Az értékteremtő folyamatok menedzsmentje Aula Kiadó Budapest 2001. 6. o.



3. **Time value:** it expresses that the product is available when consumer demand appears.

☒ *E.g. If I'm abroad, and my single pair of shoes gets torn, shoes that will arrive after a week, don't represent value for me.*

#### 8.2.2.1.2. Manufacturing/servicing activity

To create the values above, the company carries out manufacturing/servicing activity. It means, the company uses part of the resources at its disposal to make lasting changes on other resources by converting them to create new products.<sup>71</sup>

#### 8.2.2.1.3. The difference between products and services<sup>72</sup>

Although in this chapter we discuss them together, products and services significantly differ from each other by their nature. We have to handle these important qualities while manufacturing and/or servicing, so we will sum up the information briefly.

The basic differences between products and services are the following:

##### 1. Not physical nature

While products are concrete, services are not, they are intangible, they don't have physical characteristics (weight, size, etc.).

☒ *A TV-set has weight, size, color, which is clearly written in the product description, so it can be compared with other products. Based on the diagonal the prices of two sets can also be compared. At the hairdresser's you can't make a clear-cut difference between two trims based on how much hair had to be cut off. Hairdo is intangible, hair that it is made of is.*

##### 5. Heterogeneity

Identical quality is easily achievable concerning products by introducing standardization, quality assurance systems, but service is different each time it is performed. What's more, the perception of quality by the consumer can also differ each time the service is used.

<sup>71</sup> Chikán Attila: Vállalatgazdaságtan Aula Kiadó Budapest 2003. 366. o.

<sup>72</sup> Veres Zoltán: A szolgáltatásmarketing alapkönyve Akadémiai Kiadó Budapest 2009. 48-55. o. alapján

☞ *If I bought a pair of shoes which performed well (comfortable, lasting, etc.) after the first few uses, then it is expectable that if I again buy identical shoes they will have the same qualities. After leaving the hairdresser I will look at my current hairdo with different feelings, since it is not always made the same way. Sometimes I like it, sometimes I don't. As an extra, it also depends on my mood how I evaluate the different hairdos. If I'm to meet a young company, I'm happy with extravagant style, but if I'm going to a business meeting, more conventional style suits me better.*

### **6. Storability**

The finished goods – depending on their expiry – can be stored before they are sold. Services can't be stored, stocked. But availability must be adapted to the fluctuation and changeability of demand.

☞ *The flour made in the mill is stored within expiry time before it is sold. The trader stores it before it gets to the consumers. If I provide massage therapy, it can't be stored until a consumer comes, I must provide it when there's demand.*

### **7. Coincidence of production and consumption**

Products are manufactured at a certain point of the world, they are stored, then via traders they can get to faraway destinations. At another place, at another time consumers will buy them. Production and consumption are separated in place and time. In the case of services when the service is provided the consumer is already „consuming” it, here production and consumption concur.

☞ *My car was made in Japan at the end of 2013, I bought it first-hand in 2014 in Budapest. If I go to a water park because I want to slide, when the service is provided I'm already using it, I'm sliding down. Unfortunately, I can't say I will store five slides for worse times.*

### **8. Shoddy goods**

In the case of products, shoddy goods made during production get out of the system, in an optimum situation, before they are sold, so the consumer doesn't see them. The consumer will only get the good quality product. The quality of the service only becomes known when it's being performed, so consumers will only encounter it through their own experience. Quality will affect directly buying process later.

☞ *If the brakes are faulty in a series of cars, it turns out at the brake test, the product can't be sold. If I use some Internet service, but*

*the service falters, the consumer faces bad quality straight away, and will probably leave the provider.*

#### 8.2.2.1.4. Products and technologies<sup>73</sup>

Products and the applied technologies are different in the particular life-cycles of the enterprises.

In the **introduction** stage production unit costs are high due to small quantity and initial costs. The volume of production is low, technological development is small, workshop system<sup>74</sup> production is characteristic. Most of the work processes are of handwork, or of living labor nature<sup>75</sup>.

In the stage of growth specific production cost<sup>76</sup> decreases, technology changes for series production<sup>77</sup>, production volume increases, technological development starts, automation, dead labor<sup>78</sup> grows.

In the stage of maturity the production unit cost is low, technology applies assembly system, production volume is high, large scale technological development characterizes the stage. In the labor processes a medium scale automation is present.

In the stage of **decline** technology is process-like<sup>79</sup>. Production volume is high, medium scale technological development is characteristic, and the automation of labor processes is at a high level.

<sup>73</sup> Chikán Attila: Vállalatgazdaságtan Aula Kiadó Budapest 2003. 376-377. o. alapján

<sup>74</sup> The single labor phases are arranged in order by their functional character, and in each production unit only one technological phase is done. Technological control can be done well, the machines are seen clearly, the production area can be utilized well, many different items can be produced at the same time. With operations carried out in different workshops transit-time is long, material movement distances a big, the specific costs of production are high.

<sup>75</sup> work done by man

<sup>76</sup> per one production unit (item)

<sup>77</sup> they produce the same kind of product at the same place and time, or right after, regularly, quality standards are identical inside a series, it is relatively easy to swap from one series to another.

<sup>78</sup> work done by machines

<sup>79</sup> The individual work phases are arranged according to product principles. Products go along the product process following the same order of steps. Product volume is big, cost per item is low, it can easily be automated. The disadvantage is that it's difficult to switch to manufacturing a different product, it's sensitive to supply disturbances.

### 8.2.2.2. Purchase, sales, logistics

For the production process of companies it's indispensable to provide basic material, machines, and also to sell the goods in the market. With each company purchase and sales are important processes.

In the course of purchase, the company provides materials, machines, instruments necessary for production or service, and also the equipment (e.g. forms for accounting, computers) for processes outside production.

- ☞ **Production supply is the management of inter-production stock placed or flowing between different production phases.<sup>80</sup>**

To provide undisturbed production it's necessary to keep appropriate stock of necessary materials, instruments.

- ☞ **The stock is the store of products at the disposal of the company at a given time.<sup>81</sup> Since the consumers have a demand for the given product at a time and place independent of production, It has to be bridged by piling up stock.**

☞ *Wine-making is of seasonal character, harvest is done in the fall, wine-making depending on the wine takes several months, or years. But consumers want to buy wine all the year round. So, to satisfy demand producers, traders have to keep a suitable stock.*

- ☞ **Sales connect company and consumer, it forwards the items produced by the company to the consumer, manages the transport, packing, paying, information tasks necessary for this.**

- ☞ **Logistics is the company activity which ensures that the goods necessary for the undisturbed arrangement of business processes will be at disposal at the right time and place, in a volume, quality and selection meeting demand.<sup>82</sup>**

### 8.2.2.3. Company finances

Company finances embrace the whole of the company activity. They have to provide the backing for production, sales and other company processes, give an account of revenues, manage payments to the tax authorities, banks and other organizations, and to continuously provide the owners and the management with information about the financial

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<sup>80</sup> Chikán Attila: Vállalatgazdaságtan Aula Kiadó Budapest 2003. 332. o.

<sup>81</sup> Chikán Attila: Vállalatgazdaságtan Aula Kiadó Budapest 2003. 330. o.

<sup>82</sup> Chikán Attila: Vállalatgazdaságtan Aula Kiadó Budapest 2003. 331. o.

position, so that they could make the optimum decisions in connection with the company (e.g. decision about the realization of an investment).

The main areas of finances are:

- to care about ensuring the necessary sources for effective operation,
- to effectively distribute the available sources.

The main principles of the financing strategy are<sup>83</sup>:

- **security**: the proportion of own and external sources defines how much risk there is in the financial situation of the company (big proportion of external capital always means significant risk)
- **profitability**: costs of financing and the profitability of an investment define how an investment is refunded
- **liquidity**: means continuous ability to pay, that the company is always able to fulfill its payment obligations
- **independence**: to what extent the management depends on creditors, investors, if the owner of the source limits the use of sources or decision making

To ensure financial processes it's indispensable to keep the appropriate records, which is the task of accounting.

#### 8.2.2.4. Marketing

The company plans and realizes its marketing strategy to know customer demand, to create the products satisfying this demand, to make them attractive for the consumers.

The first step of the marketing activity has to precede production. Market research helps size up consumer demand, and based on the results, product development can start.

The marketing activity weaves through the complete company process through the elements of the marketing mix. The marketing mix is the optimum combination of marketing tools in a given market situation.

**Product policy** is part of the marketing mix, which can help discover product qualities, design optimum packing (attractive, practical and informative), plan design, create brand name.

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<sup>83</sup> Chikán Attila: Vállalatgazdaságtan Aula Kiadó Budapest 2003. 418. o. alapján

**Price policy** includes company decisions which set prices, and price changes (extra charge, discounts, differentiating).

In the decisions of **sales policy** the management makes decisions about the sales channels, through which distribution channels the product must get to the consumers.

**Communication policy**, or promotion means the planning of application of instruments through which the company can reach the consumers, can pass on information to them in order to boost sales, create or improve image.

You will learn more in detail about the marketing mix in the subject of Marketing.

#### *8.2.2.5. Human resources management*

☞ **Human resources are the collectivity of company employees, structured according to their expertise, qualities necessary for their work, and to the place taken in the division of labor.**<sup>84</sup>

Human resources are essential for the successful management of company processes., Though it can be substituted with machines to a certain extent, living labor can't be excluded, what's more, the employees' experience, expertise, attitude fundamentally determines the success of the company.

Human resources, just like any other resources of the company, need careful management. **The main tasks of human resources management** are as follows<sup>85</sup>:

- to form the task, responsibilities and authority areas
- to define the company's labor force needs and demand
- to get, develop and preserve labor force
- to handle work relationships, to have talks with labor unions, to involve workers in decision making
- to manage salaries and wages, to form the incentive system, to word performance expectations
- to organize work, effective employment, to manage working hours

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<sup>84</sup> Chikán Attila: Vállalatgazdaságtan Aula Kiadó Budapest 2003. 254. o.

<sup>85</sup> Chikán Attila: Based on Vállalatgazdaságtan Aula Kiadó Budapest 2003. 255. o.

#### 8.2.2.6. Innovation


Innovation is always the key to development in the life of the enterprise, it often means the possibility to survive.

Innovation in general is a new way of satisfying consumer demand at a higher level than earlier.<sup>86</sup>

The most tangible form of innovation is product innovation, that is the creation of new products. But innovation can be manifested in another way, too. The product can be made with a different technology, it can mean a new organization system at the company. But in total, it makes it possible for the consumer to get a new, bigger value.

About the role and types of innovation you can read more details in [Lesson 12](#).

#### 8.2.2.7. Management and the information system


 **Management is the area of company human resources which makes decisions at different levels (strategic, tactical and operative), plans the resources necessary for company operation, organizes and manages company processes, and co-ordinates the work of participants in the activity.**

The basic tasks of the management are:

- to determine the aims of the organization, to ensure that aims are achieved
- to regulate, to co-ordinate processes
- to ensure the optimum use of organizational resources
- to ensure the successful and effective operation of human resources

You can read more in detail about company management in [Lesson 10](#).

The management can make decisions if they have appropriate information. For this it's indispensable that they have up-to-date information about the factors influencing decision areas.

 **Information is data meaning new knowledge, which influences entrepreneurial decision making.**

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<sup>86</sup> Chikán Attila: Vállalatgazdaságtan Aula Kiadó Budapest 2003. 214. o.

'Producing', obtaining and keeping information up to date gives a serious task for company management. Especially with bigger enterprises, for the effective operation it's necessary to create a serious information system.

- ☞ **The information system is the complexity of personnel, activities and technical instruments, to perform collecting, processing, storing and providing information concerning the environment, the internal operation of the company, and the transactions between the company and its environment.**<sup>87</sup>

The managers typically deal with problem solving.

- ☞ **Problem solving is a creative process, which is aimed at the way of utilizing an arising opportunity, or at resolving an unsuitable situation, or fending off tension.**<sup>88</sup>
- ☞ **The choice between action alternatives, solutions is called decision making.**

In the course of decision making we build upon information and forward information. The area of the information to be obtained is also influenced by the problem, and what solution the manager strives for.<sup>89</sup>

## 8.3 SUMMARY, QUESTIONS

### 8.3.1 Summary

Enterprises can a lot different concerning their activity, size and organization. Yet, there are functions which can be found at most of them, since their basic aims are similar, and they are:

- satisfying consumer demand
- making profit, increasing wealth
- lasting survival (except for project companies<sup>90</sup>)
- growth, development

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<sup>87</sup> Chikán Attila: Vállalatgazdaságtan Aula Kiadó Budapest 2003. 293. o.

<sup>88</sup> Chikán Attila: Vállalatgazdaságtan Aula Kiadó Budapest 2003. 294. o.

<sup>89</sup> Chikán Attila: Vállalatgazdaságtan Aula Kiadó Budapest 2003. 295. o.

<sup>90</sup> Project companies are made for achieving a determined aim, after accomplishment they are terminated.



- producing, selling, developing products, services
- taking reasonable risks
- efficient relationship with internal and external environment
- realizing social mission
- continuous liquidity

According to these aims, each company has these basic functions:

- Economic basic function
- Welfare basic function
- Social function
- Legal function
- Market function

Beyond the basic functions companies have a specific activity system of their own. There are, however, basic activities which can be found at most companies. They are:

- Manufacturing and/or service
- Purchase, sales, logistics
- Company finances
- Marketing
- Human resources management
- Innovation
- Management and information system

The character, weight and composition may be different with each enterprise, but the particular activities appear in some form in the structure.

### **8.3.2 Self-testing questions**

1. What are the basic aims of most enterprises?
2. What are the basic functions of enterprises?
3. In which type of enterprises do the different functions, activities merge or separate?
4. What does consumer value mean?
5. What are the features of consumer value?
6. What are the dimensions of consumer value? Tell a concrete product example for the particular dimensions.

7. Introduce the basic structure of the production system.
8. What are the main differences between products and services?
9. What kinds of technologies characterize the particular company life-cycles?
10. What's the function of purchasing among the activities of the company?
11. What do you call production supply?
12. What is stock?
13. What's the role of sales?
14. What does logistics mean, and how is it connected to the company processes?
15. What's the role of financial activity at the company?
16. What are the basic principles of the financing strategy?
17. How does marketing fit into the activity system of the company?
18. What are the basic elements of the marketing mix?
19. What do human resources mean in the life of the company?
20. What are the role and tasks of human resources management?
21. What does innovation mean among company activities?
22. Why is innovation important in the life of an enterprise?
23. What's the function of management? What are their tasks?
24. Why is the state of information supply important for the management?
25. What is information?
26. What's the role of the information system?
27. How is problem solving connected to the management, and what's the role of decision making?

### 8.3.3 Practice tests

1. Find activity and organizational structures concerning well-known multinational companies. Describe the system of activities.

Match the appropriate name with the basic function of the enterprise.

Name of function	Contents of function
A) Social	1. ensuring the personal development of employees
B) Economic	2. environment protection

C) Legal	3. creating demand
D) Market	4. making profit
E) Welfare	5. ensuring lawful operation

(answer: A) 2., B) 4., C) 5., D) 3., E) 1.)

9. You want to open a gym. Plan what functions, activities you have to perform at the start and in the operation later. What kind of resources do you need to realize them?

10. Fill in the chart with the features concerning the appropriate product examples.

Consumer value	laptop ordered via Internet	pizza	car
Use value			
Place value			
Time value			

11. Mark which features below characterize products (P) or services (S).

- Homogeneous (S)
- Storable (P)
- Consumer doesn't encounter shoddy goods (P)
- Tangible (P)
- Heterogeneous (S)
- Production and consumption coincide (S)
- Non-storable (S)
- Intangible (S)
- Consumer encounters shoddy product (S)
- Production and consumption separate (P)

12. Match the features of technology with the particular company life-cycles.

Life-cycle stage	Technology
A) Introduction	1. series production

B) Growth	2. process-like
C) Maturity	3. assembly system
D) Decline	4. workshop system production

(answer: A) 4., B) 1., C) 3., D) 2.)

13. Match the strategic principles of financing with the appropriate meaning.

Basic principle	Meaning
A) profitability	1. continuous liquidity
B) liquidity	2. proportion of own and external sources
C) independence	3. Does the owner of the source limit business decisions?
D) security	4. return of investment

(answer: A) 4., B) 1., C) 3., D) 2.)

14. List the main tasks of human resources management.

15. List the main tasks of the management.

16. Mark which statement is true (T) or false (F).

1. Innovation can be creating a cheaper version of a product. (T)
2. The social functions of the company include ensuring jobs, ensuring the living and personal development of employees. (F)
3. An entrepreneur making fried dough is obliged to employ an accountant to do accounting. (F)
4. The bigger the company, the more the different functions separate concerning activity and organization (T)
5. The basic motivation to produce products and services is satisfying consumer demand in the most effective way. (T)
6. Consumer value is the objective opinion of consumers as to what extent the product met expectations. (F)
7. Consumer value changes, because the multitude of consumers always compares the product with the expectations. (F)

8. It's generally characteristic for services that they can't be stored. (T)
9. In the case of products the consumer can often encounter shoddy goods, while with services there's little chance of this to happen due to quality assurance. (F)
10. As for technology, it's characteristic for the maturity stage of the company that production volume is low, technological development is small-scale. (F)

## 9. LESSON: THE BUSINESS PLAN OF THE ENTERPRISE

### 9.1 OBJECTIVES AND COMPETENCIES

In this lesson we show how enterprises plan their future operation, by what principles they make their strategy. We examine in detail the ways of making a business plan, the areas of planning, and the main features of the particular areas.

Learning the lesson, students will be able to recognize the role and importance of company planning, and to draw up the aims and tasks of strategy making. They will be able to deduce the aims of the business plan from the company strategy, and to compile the business plan of the company.

### 9.2 CURRICULUM

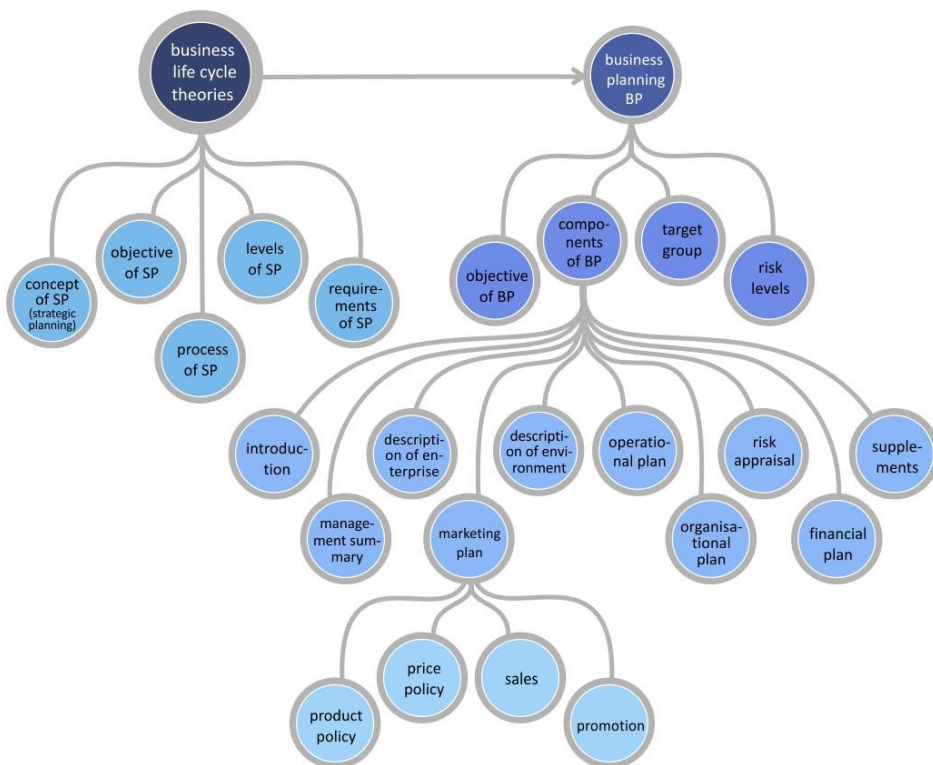


Figure 23: Concept map

### 9.2.1 The basics of strategic planning

*„Unless commitment is made, there are only promises and hopes; but no plans.” (Peter Drucker)*

The activity of the enterprise can be determined by its managers in an intuitive way, with ad hoc decisions, but it is not definitely the condition for long term success. To make the company operation successful on the long run, the management's important task is planning.

The planning task in total:

- Complex, analytical, prognosticating, discovering, concept making and proposing activity.
- Drawing up a desirable future state, defining the methods, conditions and tasks to achieve it.
- The work in the course of which we determine the direction of future development in advance, the aims to achieve, and the means and measures necessary for this.

The aim of planning is:

- to develop the company
- to determine its aims
- to ground management
- to decrease insecurity
- to co-ordinate, supervise company processes

☞ **Shaping strategy includes the selection of business area or areas, drawing up the mission and vision, setting strategic aims, designating the means and methods of serving the realization of strategy.**

☞ **We only speak about strategic planning, if the strategy is shaped in the framework of a regulated planning process<sup>91</sup>.**

The process of strategic planning is shown in the figure below:

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<sup>91</sup> Balaton Károly – Tari Ernő: Stratégiai és üzleti tervezés Aula Kiadó Budapest 2007. 15. o.

Planning can/must be realized at different levels. Level can be interpreted at the level of company organization, and depending on the time factor. The levels of planning are summed up in the following figure:

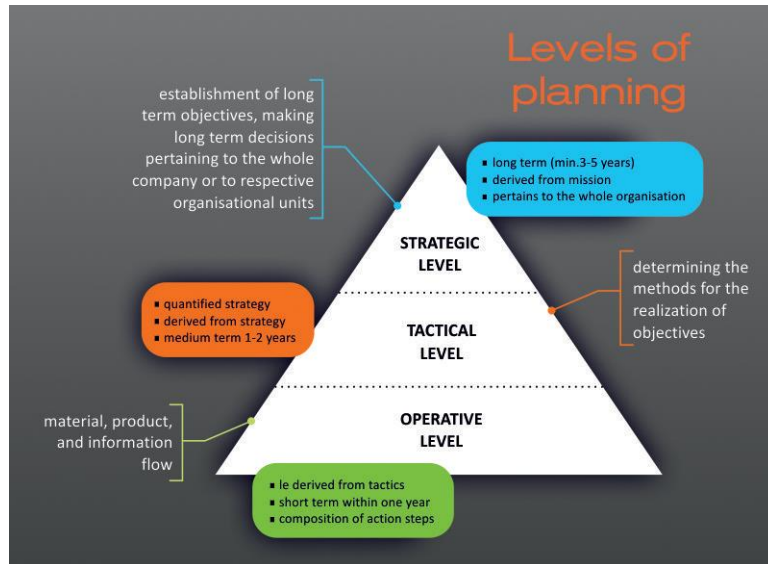


Figure 24. The levels of strategic planning

To create the strategy, following the analysis of the internal and external environment, first you need to draw up the mission of the company.

- ☞ **Mission expresses the function of the organization, its relationship with the world, and also what values the company operates by.**
- ☞ **The vision sets the states to achieve in the further future (5-10 years), towards which the company advances by realizing short term strategies.**
- ☞ **The business plan is usually an action plan for several years, which is shaped on the basis of strategic actions and projects.**
- ☞ **The strategic actions are highlighted tasks deducted from strategic aims. The project is a task package usually for several**



**years compiled from strategic actions, which we assign schedule, responsible person and resource demand to.**<sup>92</sup>

The most important requirements in connection with planning:

**reality:** the analysis of internal and external conditions must mirror the real picture, too pessimistic or too optimistic estimates significantly increase the risk of planning

**complexity:** all factors in connection with each other have to be measured, they will play a role in the operation in the future, you have to determine their weight, importance, their relationship, interaction.

**consistency:** (freedom from controversy) the differing interests of organizational units, organizational levels have to be harmonized while planning.

**flexibility:** in the course of planning you must consider that the internal and external condition systems keep changing, you have to examine their tendency, and build them into the plan.

### 9.2.2 Business planning

The business plan is the determinative document of starting and running an enterprise, which gives a convincing picture if the enterprise profitably operates and is able to recognize and tackle risks in the forthcoming mid-range period, with the visualized products, in the aimed market, with the help of people participating in the enterprise.

The business plan usually shows the aims of the enterprise, the internal and external factors affecting the aims, their expectable effect, and also the resources and activities necessary to achieve these aims in the different company areas concerning a 1 to 3 year period.

Plans always hide some risks at a given level, since we don't have safe and comprehensive information, and estimates might be inaccurate. In spite of this, planning is essential, since we consider the factors influencing the enterprise, determine the aim and direction of operation, so to decrease insecurity.

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<sup>92</sup> Balaton Károly – Tari Ernő: Stratégiai és üzleti tervezés Aula Kiadó Budapest 2007. 14-16. o.

As for the level of risk, we can talk about the following types of information/factors:

- **Certain factor:** all the information is known about the factor, its behavior can be anticipated, planned in advance. The risk connected to it is small.
- **Uncertain factor:** not all data are known about the factor, some circumstances of its behavior can't be planned securely. Its risk is moderate.
- **Risky factor:** little information, factor changes, direction and extent is not known. Risk is big when planning is done.

#### *9.2.2.1. The aim of business planning*

Making a **business plan** may have several **purposes**, the concrete contents of the plan depends on the purpose of making. The aims can typically be:

- Introducing the activity to owners, investors, preparing for an investment decision, convincing new investors (banks, organizations dealing with tenders, etc.)
- Realizing new ideas, innovations with big risk factor, modeling an expected result
- Monitoring continuously business results and the expected development
- Plan made for business partners, strategic alliances
- Grounding company risk management, controlling activity.

#### *9.2.2.2. Target groups of making a business plan*

The target groups of making a business plan are:

- Owners
- Management
- Creditors, investors (venture capitalists)
- Tender evaluators and supporting (co-operating) organizations
- Strategic partners

The purpose of making a business plan for the **owners** is to introduce the current operation and successfulness of the enterprise, to assure them that the invested capital will return, will make a profit. A further purpose may be raise the owners' capital for a bigger investment, that is

claiming newer investments, instead of using external sources, or to complete it, to decrease being exposed to external sources too much.

The **management** makes a business plan to size up the factors affecting the enterprise, to determine the direction of operation, to plane the measures which lead to achieving the planned aims. In case deviation from the plan, they can immediately intervene in the processes, so to decrease the risk of operation and to continuously keep the influencing factors under control. Planning at the same time helps the co-ordination of part areas of the company. Professional tasks, calculations belonging to them, and control figures helping controlling are highlighted in the plan,

**Creditors** ensure external sources for the company for realizing the aims. The aim of the business plane made for them is to introduce the planned development, its necessity, the resources necessary to realize them, and the return of the investment. In this plan usually financial calculations are given special emphasis. The plan has to be made and handed in in a form of the financial institution or crediting organization, according to their principles, expectations.

The aim of venture capitalists is to support new enterprises, start-ups, to realize genuine ideas, so the risk is big. They want to ascertain about the expected success of the project, and want to make sure they can pull out from the enterprise after a given time (3 to 5 years) with a profit. In the plan you have to introduce the idea, the analysis of the expected demand and also, similarly to the plan made for creditors, compile an emphatic financial plan.

**Organizations supporting tenders** want to ascertain about the appropriate use of sources claimed for in the tender, and if you have your own sources at disposal. It's also important to introduce that using the source of the tender helps realize the aims of the enterprise and those of the tendering organization alike. The plan is aimed at introducing the aim of development, the return of the investment, to introduce sustainability, and to introduce the profitability of the company/project.

The aim of creating **strategic partnerships** is to ensure long term, successful co-operation. For this you need to introduce the activity system of the enterprise, and to make a comprehensive plan analysis. You have to highlight those company areas which the co-operation is aimed at (it may be purchasing, sales, social relationships, or any other part area).

At this link you can read the concept of the strategic plan of Johns Hopkins Medicine. [http://www.hopkinsmedicine.org/strategic\\_plan/](http://www.hopkinsmedicine.org/strategic_plan/)

### 9.2.2.3. *Parts of the business plan*

In general, the business plan consists of the following parts, chapters:

#### 9.2.2.3.1. Introduction

This chapter contains the general data, designations, main features of the enterprise. These data can partly be found in the certificate of incorporation, partly in the official registers of the enterprise. They are, e.g. the:

- name of enterprise (full and abbreviated name<sup>93</sup>)
- availability of enterprise (address, phone number, e-mail, etc.)
- other identification data (bank account number, tax number, statistical code, etc.)
- legal form of enterprise
- owners of enterprise and their availability, and that of the persons' entitled to represent the enterprise
- main scope of activity (according to TEÁOR, SZJ<sup>94</sup>)
- main products, services
- founding capital of enterprise
- date of making and approving the business plan
- warning to tackle confidential data

#### 9.2.2.3.2. Management summary

The aim of the summary is to give a broad picture of the most important factors connected to and discovered about the enterprise, of the aims to achieve, of the demands necessary for development, and of the main points of measures necessary to achieve the aims. You have to compile the summary of the main statements of the plan in a way that those who don't want to or can't read the whole plan could also get a picture of it. It's worth introducing the most important characteristics of the enterprise, its main aims, motivation, significant changes occurred recently.

In the management summary it's worth touching upon the following:

- purpose of making a business plan

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<sup>93</sup> full name like: Mole Commercial and Service Limited liability company, shortened name: Mole Ltd.

<sup>94</sup> the two nomenclatures, that is categorization systems can be found completely on the website of the Central Statistical Office (CSO).

- its strategic aspects
- aim of enterprise, main facts, expectations, aspirations grounding aims
- focus points of industry branch, market situation
- financing situation (with the help of a few figures)
- earlier significant changes
- summary of most important conclusions

#### **9.2.2.3.3. Introduction of enterprise**

In this chapter you have to introduce the enterprise with text in detail. The more important areas in the chapter are:

- key areas of the enterprise, its strategic products
- features of the operation of the enterprise so far (activities, parts, management, general financial situation, market success, the basic principles of operation so far, etc.)
- situation in the industry branch, competitive position
- targeted market, result of market segmentation, main features of targeted market segment

#### **9.2.2.3.4. Introduction of environment, industry characteristics**

We have several methods to examine the environment. We can examine it according to its levels:

- macro-environment (political, legal, social, welfare)
- industry sector environment
- microenvironment (direct competitive environment)

A frequent method of analyzing the macro-environment is the PESTEL, or STEEPLE analysis. We often examine the industry branch environment with Porter's Five Forces model, and with the industry branch life-cycle model. The strategic map and the consumer value analysis belong to the methods of analyzing the microenvironment.

In total you have to analyze the following:

- factors of macro-environment affecting the enterprise
- industry branch prospects (situation of industry branch, innovations, growth opportunities, dynamism, etc.)

- competition (market structure, market share of the enterprise, bargaining power of expected entrants, suppliers, buyers, risks, etc.)
- level of co-operation inside the industry branch, and its opportunities
- government plans, measures concerning the industry branch
- the most important active components of the operational environment

#### **9.2.2.3.5. Marketing plan**

The marketing plan, according to the 4Ps<sup>95</sup> known from the theory of marketing, includes the following examined areas:

##### *1. Introduction and planning of products, services*

In the course of planning you have to analyze the successfulness of the existing products, and the changes in consumer demands connected to them. The Marketing subject shows the methods with the help of which the enterprise can decide which products are the most successful, which one have to be accentuated, which products have to be improved, or withdrawn from the market. It can also be a product policy decision if the enterprise develops a new product. Creating a product range is also an important product policy decision. The aim is to meet consumer demands the best possible way. So, here you have to introduce the following:

- evaluation of existing products (BCG matrix, ABC method, etc.)
- planned product decisions (Ansoff matrix, product innovation, etc.)
- creating a product range and – choice
- expected return on product development
- competitive position based on product strategy

##### *2. Price policy*

Price policy is a series of decisions which determine what price the goods for sale have to be sold at. It's calculated on the basis of costs for manufacturing and the profit to be achieved. For this you need to

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<sup>95</sup> Depending on the operation sphere of the enterprise, instead of the 4Ps, here you can encounter the 5Ps, and also the 7Ps, in the case of enterprises providing primarily services, you'll find the 7Ps and the 8Ps, as well. You'll find more information about this in the Marketing curriculum.

consider the role of the enterprise filled in competition, and in connection with it, the basic principles of strategy to be followed.

Together with market prices you also have to determine the possibilities of differentiating (seasonal prices, discounts, sales, etc.). The most important factors are:

- planned prices
- planned sales
- package offers, price differentiation
- competitive position based on prices

### *3.Sales plan*

As starting point of the sales plan, you have to work out how big turnover you can expect from the individual products. Together with this you have to determine the sales channels that you can use (different business types of wholesale trade, retail trade), the different ways of selling (direct sales, personal sales, sales via dealer, automatic trade, etc.). You have to determine the following:

- planned return of sales
- distribution of returns according to markets/products
- current and desired market share
- employed distribution channels, and the ones to be extended, and their distribution according to turnover
- profitability of sales channels
- new sales methods

### *4.Promotion plan*

In the promotion plan you have to determine what marketing tools, what marketing mix the enterprise will use in the period of planning. You have to harmonize Public Relations, Sales Promotion, Direct marketing and other tools<sup>96</sup> based on the aims described in the strategy. Based on this you have to make decisions about the following:

- marketing mix planning
- communication mix planning
- determining advertisement aims
- way of measuring advertising efficiency

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<sup>96</sup> You can read more about these means in the Marketing subject.

#### 9.2.2.3.6. Functional, operational plan

The functional plan shows in detail the processes of the company, the system of processes. The character of the plan depends on the type of the enterprise. Manufacturing companies make a production plan, service providers make a servicing plan, while for commercial companies a trade plan is characteristic.

In the case of making a **production and servicing plan** you have to present the current production volume, the applied technologies, and the capacity, machinery, labor force necessary for this. You have to plan the necessary changes to achieve the aims expected in the future, and also their cost.

In the **turnover plan** you can find the methods of purchasing goods, its conditions, the current and expected speed of turnover, packing, method of handling orders, demand for machines and human resources, and also the costs emerging from this.

In the plan you have to introduce the necessary resources, the way and costs of them to be at disposal:

- Manufacturing capacity (real estate, technical and other machines, intangible products)
- stocks
- means
- energy

(We discuss human resources in the next chapter.)

#### 9.2.2.3.7. Organizational plan

The organizational plan introduces the ownership structure, the management of the company, the organizational structure and the main principles and aims of staff management. Based on the aims, you have to determine how you have to develop human resources capacity at disposal for the realization. It's possible to hire new staff, to regroup labor force inside the company, to further develop the abilities, skills of employees, to regroup authorities and responsibilities.

- current and planned spheres of activity
- necessary staff number to perform the work, and their regrouping
- introduction of leading officials, authorities and responsibilities, necessary changes
- basic principles of the wage-system
- incentive systems
- principles of promotion



- ways of developing human resources
- principles and ways of organizational development

#### **9.2.2.3.8. Risk assessment**

On the basis of environment analysis and internal examinations, you have to size up the risks emerging in every area of planning, the possibility of them to happen, the ideas, measures to avoid or eliminate them.

It's important that risk assessment be thorough and extend to all areas, this way it can provide the possibility of flexible adaptability for risks that can be planned, for the company.

- classification of risk factors according to the extent of insecurity
- the assessment of probability of them to happen
- planning solving or avoiding measures

#### **9.2.2.3.9. Financial, financing plan**

The financing plan introduces the current financial situation of the company (revenues, costs, outgoings, expenses, liquidity, profitability, proportion of foreign capital, etc.), the result to be achieved, the stock and movement of financial means necessary to provide this. The financial plan usually contains a scheduled financial statement, an income plan, a liquidity plan, and a scheduled cash flow. Together with this, it introduces the development of factors essential from the point of view of company operation, (liquidity, profitability, etc.), it evaluates them, and based on this it determines the necessary measures and aims to follow in the financing field (e.g. borrowing, issuing bonds, share redemption, etc.).

If the financial plan was primarily made for the purpose of borrowing, then this planning area is the most accentuated, in this case a separate plan must be made for the realization of the investment, and a financial plan for the repayment of the given source, and for the returns of the investment.

Characteristic parts of the financial plan:

- revenues plan
- expenditure plan
- financial statement plan (balance, financial statement, and cash flow plan)
- liquidity plan
- methods, indexes used for financial planning, and their reasons

### 9.2.2.3.10. Appendices

In the appendices you can find all documents, background studies, supplementary notes connected to the business plan which grounded planning, or which supports the thoughts, aims, calculations worded in the plan. It can be market survey results, price offers, consumer or trader feedback, letters of intent, declarations of intent, technical descriptions, publications, list of patents, etc.

Of course, business plans can't only be made by the companies of the for-profit sphere, the planning method also appears in the non-profit sphere. Obviously, in the case of non-profit oriented enterprises the structure of the plan, the proportions of the particular chapters are different, the emphasis is on the activity, and financing is aimed at ensuring the financial background of the activity.

## 9.3 SUMMARY, QUESTIONS

### 9.3.1 Summary

Planning is an important task of the management of the enterprise. The aim of the strategy is to draw up a desired future status, and to determine the methods, conditions, tasks to be done to make it possible to achieve the aims.

The main steps of strategic planning are as follows:

1. Analysis of external and internal environment
2. Selection of business areas
3. Wording of mission and vision
4. Forming strategic aims
5. Determining means and methods serving the realization of aims

Planning can be interpreted at different levels:

1. Strategic level
2. Tactical level
3. Operative level

The particular planning levels based on period, target area, worded aims and measures differ from each other.

**Mission** expresses the purpose of the company, its relationship with the world, and also, what values the enterprises considers when it operates.

**Vision** sets the conditions to achieve in the further future (5 to 10 years), which the organization is getting ahead to by realizing short term strategies.

The **business plan** is an action plan for many years, which is made on the basis of strategic actions and projects.

The **strategic actions** are highlighted tasks deducted from strategic aims. The project is a task package compiled from the strategic point of view, it lasts for several years, with a schedule, a responsible person, and resource need.<sup>97</sup>

The main requirements of planning:

- reality
- complexity
- consistency
- flexibility

The business plan introduces the aims, external and internal factors affecting them, their possible changes, and the resources and actions to achieve these aims in different part areas of the company in the medium term, 1 to 3 years.

The enterprise considers different factors according to risk level, and makes its plan based on this.

- certain factor
- uncertain factor
- risky factor

The aim of making the business plan

- Introducing the activity to owners, creditors, preparing for investment decision, convincing new investors (banks, tendering organizations, etc.)
- Realizing new ideas, innovations, realizing innovations with big risk factor, modeling expected result
- Monitoring continuously business results and the expected development
- Plan made for business partners, strategic allies

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<sup>97</sup> Balaton Károly – Tari Ernő: Stratégiai és üzleti tervezés Aula Kiadó Budapest 2007. 14-16. o.

- Grounding company risk management, the realization of controlling activity

The main target groups of making a business plan:

- Owners
- Management
- Creditors, investors (venture capitalists)
- Tender evaluators, and supporting (co-operating) organizations
- Strategic partners

Parts of the business plan:

1. Introduction
2. Management summary
3. Introduction of the enterprise
4. Introduction of environment, industry branch features
5. Marketing plan
6. Functional, operational plan
7. Organizational plan
8. Risk assessment
9. Financial, financing plan
10. Appendices

### **9.3.2 Self-testing questions**

1. What is planning?
2. What are the aims of planning?
3. What is strategy and what is strategic planning?
4. Introduce the process of strategic planning.
5. Introduce the levels of company planning, and the features of the different levels.
6. What are the requirements of planning?
7. What is the business plan, and how is it connected to strategy?
8. What risk levels can we speak of in the course of planning?
9. What are the aims of business planning?
10. Who can a business plan be made for?

11. Which areas are accentuated in the business plans made for different target groups?
12. Introduce the parts of the business plan, and introduce what the different parts contain in general.

### **9.3.3 Practice tests**

1. Mark if the following statements are true (T), or false (F).
  1. Strategy is deducted from the business plan (F)
  2. Mission sets the conditions to be achieved in the further future (5 to 10 years), which the organization moves to by realizing short term strategies. (F)
  3. The business plan is typically made for a 1 to 3-year period. (T)
  4. The aim of the business plane made for the owners is to introduce the activity of the company to ensure them their investment will return. (T)
  5. Planning increases the risk of operation. (F)
  6. The requirement of complexity means that the aims and means of a given plan be free of controversy. (F)
  7. If the aim of making a business plan is to use venture capital, then financial calculations and the introduction of the project plan are more accentuated in the course of planning. (T)
  8. Uncertain data are the ones, in the case of which not all information is known about the factor, some momentums of their behavior can't be planned safely. (T)
  9. The summary in the business plan has to be compiled the way that it could give a picture of the main statements of the plan even for those who don't want to or can't read it in detail. (T)
  10. In the promotion plan you have to determine what sales tools and channels the enterprise is going to use in the period of planning. (F)

2. Match chapters of the plan with their contents.

Chapter of plan	Contents of chapter
III. Introduction of the company	a) It must give a picture about the main statements of the plan to those who don't want or can't read the detailed plan.
X. Appendices	b) Plans the marketing mix to be used.
VIII. Risk assessment and plan	c) It contains information about the perspectives and competitive situation in the industry branch.
IV. Introduction of environment, industry branch features	d) In this chapter you can find the signed letters of intent, and declarations of intent.
V.1. Introduction, planning of products, services	e) Data of this chapter can partly be found in the certificate of incorporation.
I. Introduction, general data	f) It shows if labor reallocation or hiring new staff is necessary.
V.2. Price policy	g) It shows at what price you need to sell the product, costs and scheduled profit concerned.
V.3. Sales plan	h) It often contains cash flow.
VI. Functional, operational plan	i) It shows which sales channels the company targets.
VII. Organizational, or human resources plan	j) For commercial companies, the goods turnover plan is characteristic.
IX. Financial, financing plan	k) Current features of company operation (activities, parts, management, etc.).
II. Management summary	l) It describes which products have to be further developed, or withdrawn from the market.
V.4. Promotion plan	m) Concerning all company parts, reliability and accuracy of data, the probability of events to happen have to be examined.

Answer:

I. – e)

II. – a)

III. – k)

IV. – c)

V.1. – f)

- V.2. – g)
- V.3. – i)
- V.4. – b)
- VI. – j)
- VII. – f)
- VIII. – m)
- IX. – h)
- X. – d)

3. Which area is more accentuated in business plans? Match the plans made for particular purposes with the accent of planning parts.

Plan	Accentuated area
(1) for owners	a) in case of deviation from the plan they can immediately intervene in the processes
(2) for management	b) return of required source, realization of financed aim, ensuring own resources
(3) for creditors	c) detailed analysis of professional tasks, the activity system, areas of co-operation
(4) for tender supporters	d) demand for source to increase capital, show successful operation of invested capital
(5) for strategic partners	e) return calculations, the financial plan is accentuated

Answer:

- (1) – d)
- (2) – a)
- (3) – e)
- (4) – b)
- (5) – c)

4. Match the types of risk with its features.

Risk	Feature of risk
(1) Risky data	a) all information is known about the factor, its behavior is calculable, can be planned in advance
(2) Certain data	b) not all information is known about the factor, some momentums of its behavior can't be planned safely.

(3) Uncertain data	c) little information, factor changes, direction and extent of change is not known
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(Answer: (1) – c), (2) – a), (3) – b))

5. Show the process of strategic planning in the figure below.

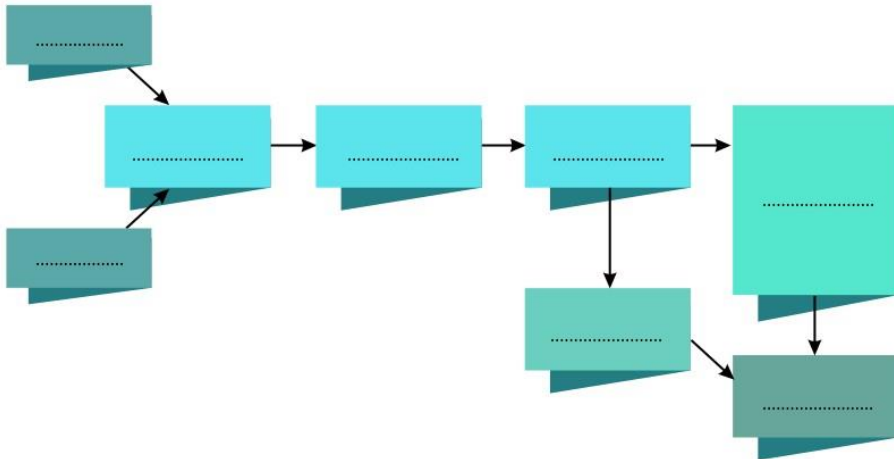


Figure 25

6. Have a look at the mission of Unilever Magyarország at this link: <http://www.unilever.hu/vallalatunk/ourmission/>.

What kind of enterprise would you like to start? Draw up the mission and vision of your company, and the strategic aims that can be created at the start.

7. List the parts of the business plan of the enterprise.

- .....
- .....
- .....
- .....
- .....
- .....
- .....
- .....
- .....



.....  
 .....

(Answer:  
 Introduction  
 Management summary  
 Introduction of the enterprise  
 Introduction of the environment, industry branch features  
 Marketing plan  
 Functional, operational plan  
 Organizational plan  
 Risk assessment  
 Financial, financing plan  
 Appendices)

8. Match the contents of plans with the corresponding chapter of the business plan.

Chapter of business plan	Area of analysis
1) Introduction	a) incentive systems
2) Management summary	b) current features of company operation
3) Introduction of enterprise	c) scheduled price actions
4) Introduction of environment, features of industry branch	d) letters of intent, patents
5) Marketing plan	e) summary of the most important conclusions
6) Functional, operational plan	f) classification of risk factors
7) Organizational plan	g) availabilities of the enterprise
8) Risk assessment	h) liquidity plan
9) Financial, financing plan	i) competitive situation, market structure
10) Appendices	j) production capacity, stocks

(Answer: 1) g), 2) e), 3) b), 4) i), 5) c), 6) j), 7) a), 8) f), 9) h), 10) d)

## 10. LESSON: THE MAIN ASPECTS OF COMPANY MANAGEMENT

### 10.1 OBJECTIVES AND COMPETENCIES

The aim of the unit is to familiarize students with the theoretical background of company management, with its aim, requirements and process. Even today, many company managers think anybody can be suitable for managing a company without knowing its main aspects, and mere instinct is enough for leadership. As we briefly sum up in the unit, leadership, or management looks back on a long research past, many approached the main factors from different aspects, and described how one can manage a company not efficiently and successfully.

By learning this unit, students will be able to identify the essence, function of the manager's role, and the requirements coming with it. They will be able to sum up the management functions and plan the general process of management at a given company. They will understand and use the main management roles.

### 10.2 CURRICULUM

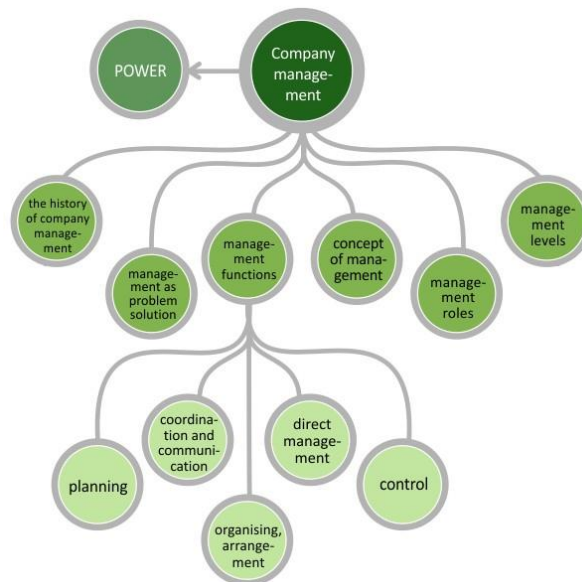


Figure 26: Concept map

### 10.2.1 A short historical overview of management<sup>98</sup>

Out of the functions of an enterprise one of the most prominent ones is the activity of the management. The most important decisions are made here, and the future of the enterprise is basically determined here.

The science of management goes back to the ancient times. However, theoretical, scientific research only started to develop after the industrial revolution, **from the second half of the 1800s**. Significant theories are owed to *Frederick Winslow Taylor* and *Henri Fayol*, who recognizing the challenges of the industry of the era, supported their conclusions with empirical research.

Taylor dealt with the rationalization of company processes, with the co-ordination of the organizational background of production planning with scientific character, he created labor and time study principles, wage and incentive systems.

Pierre Morin summed up briefly Fayol's work:

1. management is a general method
2. management concerns the governance of operations of the organization
3. management rests on system concept

The science of management further developed **between the two world wars**. Its noted researchers were: *Mayo*, *Roethlisberger* and *Dickson*. In this period the role of man comes to the foreground, a series of analyses about behavioral-science aspects appeared.

**After WW II** researchers cast a new light on the science of management. The works by *Ernest Dale*, *Peter F. Drucker*, *Maynard* and *Mintzberg* aroused significant interest. Decision oriented approaches often rested on mathematical grounds, operation research, cybernetics gained significant role.

Beginning with the 1970s, due to the changing effects of the times, the science of management also went through significant transformation. The interaction of sciences affected the work of researchers of the time, mostly sociology, political economy, biology and anthropology. Contingency theory was formed around the same time. It empirically and comparatively analyzed the connections between the features of functional conditions (context) and organizational structure, and examined the interaction between organization and environment. The

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<sup>98</sup> Dobák Miklós: Szervezeti formák és vezetés Akadémiai Kiadó Budapest, 2008. 11-22. o. alapján

noted researchers of the time were: Child, Friedberg, Simon, and the Hungarian researchers were Andics, Rozgonyi, Nemes and Dobák.

The science of management is still developing today, newer and newer surveys, theories appear. You can get informed about the current trends from the periodicals *Vezetéstudomány*<sup>99</sup>, and *Journal of Management*<sup>100</sup>.

### 10.2.2 Management activity

At this link you can read about the reasons and principles of management restructuring at Coca-Cola Co.:

<http://www.coca-colacompany.com/press-center/press-releases/the-coca-cola-company-announces-coca-cola-americas-management-and-organizational-changes>

First get familiarized with the notion of management.

☞ **Management is a process in which activities serve to achieve efficiency through the control of other people's work.**<sup>101</sup>

The management controls the combined work of the participants of the organization in order to realize company processes most efficiently. For this, it co-ordinates the work of the participating people, and has an indirect impact on them.

☞ **Management means direct impact on employees. Management is an activity that sets the aims for the organization, defines the necessary means to achieve them, starts, controls and co-ordinates the necessary activities to achieve the aims.**

Organizations are aim-oriented, their operation is submitted to determined aims. The aim system of the organizations doesn't always harmonize with the aims of managers and employees. A management task is to co-ordinate them.

#### 10.2.2.1. Management levels

Management function creates a hierarchical system at organization level. Its general pattern is as follows:

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<sup>99</sup> *Vezetéstudomány*: <http://corvinus-mba.hu/hungarian/vezetestudomany/>

<sup>100</sup> *Journal of Management* <http://jom.sagepub.com/>

<sup>101</sup> Robbins in Dobák Miklós: *Szervezeti formák és vezetés Akadémiai Kiadó Budapest, 2008. 127. o.*

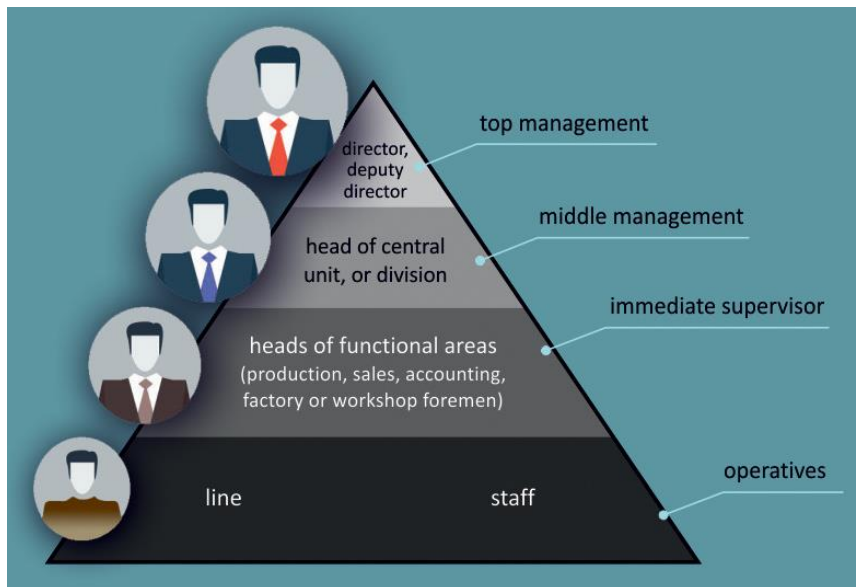


Figure 27: Management levels in the organizational hierarchy<sup>102</sup>

Managers at different levels must be characterized by different attributes. Whereas for top managers concept creation knowledge is needed significantly, they also must have some minor technical knowledge, too, and they must have outstanding planning and significant organizational knowledge. At the same time, with direct leaders the proportions are the other way round, they must have better technical knowledge, and management skills are standard. But the skills to manage people are important at every level.

#### 10.2.2.2. Management as problem solving<sup>103</sup>

As a function, management is a series of problem solving. Based on this, the elements of the problem solving process can be the following:

- problem discovery
- determination of aims
- problem analysis
- decision preparation and decision

<sup>102</sup> Dobák Miklós: Szervezeti formák és vezetés Akadémiai Kiadó Budapest, 2008. 128. o.

<sup>103</sup> Dobák Miklós: Szervezeti formák és vezetés Akadémiai Kiadó Budapest, 2008. 130. o.

- execution, control, feedback

From this approach, the management/manager's task is to solve the problems emerging at the organization. First, you have to recognize and determine the problem, based on this, you have to designate what aims the organization wants to achieve. Discovering the reasons and effects of the problem helps the enterprise make appropriate decisions to eliminate them. After this, you must give concrete instructions to those executing the decision, which later you have to check. Based on the experience, the next problem discovery and decision making process has to be modified for more efficient operation.

#### 10.2.2.3. Management roles<sup>104</sup>

Mintzberg's work was the starting point for the approach aimed at what roles the manager has to play in his work. They are the following:

- Interpersonal roles
  - role of public appearances (figurehead)
  - the role of the boss (leader)
  - the role of making and maintaining connections (liaison)
- Information roles
  - the role of collecting information (monitor)
  - the role of distributing information (disseminator)
  - the role of the spokesman (spokesperson)
- Decision roles
  - entrepreneur
  - disturbance handler
  - resource allocator
  - negotiator

#### 10.2.3 Management functions<sup>105</sup>

Starting from the Fayol approach, the main functions of the management are:

1. planning
2. organizing
3. direct control

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<sup>104</sup> Dobák Miklós: Szervezeti formák és vezetés Akadémiai Kiadó Budapest, 2008. 130. o.

<sup>105</sup> Dobák Miklós: Szervezeti formák és vezetés Akadémiai Kiadó Budapest, 2008. 127-144. o. alapján

4. co-ordination and communication
5. supervision

As you could see in the previous unit ([9. lesson 03 09 K02: Levels of strategic planning](#)) **planning** can be interpreted at several levels. Levels separate according to period and decision maker. Strategic planning is separated from operative planning in its function, task, and considering the character of realization, as well.

**Organizing** means the shaping and operation of processes, work phases and the creation of the organization belonging to it. Part of organizing is job planning, managing work share, and sharing authority, as well.

The main points of **direct control** are the distribution of tasks, dividing responsibilities and authorities, direct instruction of employees.

**Co-ordination** is the harmonization of work processes with the participants of the organization. Adjusting plans to organizational capabilities, employee aims in the process of strategy making also belongs to it.

**Supervision** means the scheduled and directed control of processes. In the course of supervision they examine if the realized tasks correspond with the given instructions and with the plans at different levels.

#### *10.2.3.1. Setting aims and creating strategy (planning)*

In Unit 9 you learnt about the main points of planning. The function of the management is to determine aims and to define the necessary means and processes to realize aims.

In connection with this, the management draws up the strategy, which can be

- **basic strategy** which is aimed at profitability and development concerning the whole of the company
- **competition strategy**, which is connected to the industry branch competitive position of the organization's products
- **functional strategy**, which means the necessary organizational background to realize basic and competition strategies, actions, creation of functions.

The strategies above are realized with the help of **actions and programs**. Time schedules, resource requirements, measures package, responsibility allocation and deadlines belong to the measures drawn up

in the **business plan**. The business plan connects the long term strategy with the yearly **operative plan** (budget).

Beyond strategy making, the management has to **activate organizational actors** participating in realizing strategy. This is the realization of the program through which the manager ensures with the balance between contribution (performed by subordinates) and incentives (rewards offered by the organization, benefits, coercive means) that the employees can harmonize their individual aims with the aims of the organization. The aim is to create such an organizational 'atmosphere' where subordinates themselves get identified with the aims, and assume the aims of the organization as their own.

#### *10.2.3.2. Organizing*

##### **10.2.3.2.1. The notion of organizing**

☞ **Organizing, as management function, is an activity which is aimed at the realization of pre-determined goals, by harmonizing the personal and material resources of the organization (optimum combination).**

Organizing means tasks aimed at

- harmonizing processes (process organization)
- forming and changing organizational structures (organization planning)
- creating the order of work (work organization), and creating jobs<sup>106</sup>.

Considering the organizational side of organizing, the management has two basic tasks:

1. Division of labor (specialization): creating organizational units, authority system, organizational proportions, determining the organizational structure.
2. Reorganization: organizational planning tasks to change the already working organization.

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<sup>106</sup> Dobák Miklós: Szervezeti formák és vezetés Akadémiai Kiadó Budapest, 2008. 137. o.



**10.2.3.2.2. The process of organizing**

- The main point of the division of labor is that we divide the tasks of the whole of the organization into part tasks, and we assign organizational units, or individuals to them.
- After this, based on the part tasks we create organizational units. We assign individuals, tasks to the units.
- We create the authority system of the organization. The regulation of authorities is the activity which is aimed at determining the competency of organizational units and individuals assigned to the particular tasks coming from the division of labor. The division of authority to make decisions belongs to this.
- We assign the staff belonging to one manager, thus we create the span of control. The organizational configuration is formed this way.

The optimum creation/transformation of the organization is the condition of efficient and successful work. The organization has to continuously adapt to aims, tasks, and the changing environmental effects. Organization is not a single or rare activity, but a continuous one.

**10.2.3.3. Direct management**

The good manager must have the necessary skills and knowledge, about which several theories were made, and which we don't discuss in this unit. In the course of direct management the manager has to perform the following functions:

- human resources management
- motivation
- communication
- creating and managing groups

**10.2.3.3.1. Human resources management**

The task of human resources management is to attract, keep and develop the necessary employees as for their skills and knowledge is concerned. It also has to create a harmony between expectations and claims originating from jobs and work tasks, and the knowledge, skills and attitude of those doing the work. After a certain organizational size is reached, the tasks of human resources management are performed by an independent organizational unit.

Part tasks of human resources management:

- human resources planning,
- finding, selecting, hiring devoted people with appropriate skills,
- determining sphere of activity,
- creating remuneration, wage system,
- evaluating the performance of employees,
- education, further training,
- handling the emerging disciplinary and other problems at work,
- managing labor connections (with unions),
- operating an information system concerning the tasks above.

**10.2.3.3.2. Motivation**

The motivation of employees significantly determines the performance of the organization. The performance of employees is basically influenced by three factors:

- environmental conditions
- their abilities, knowledge and skills
- their motivation

Individuals join an organization because they want to satisfy certain needs, and they will stay its members, if their needs are permanently satisfied. The company can only survive long and operate efficiently if it can motivate its members to achieve organizational and individual aims jointly. Managers are not just to provide suitable working conditions, but they also have to be aware of the factors which influence to what extent the employees are motivated by what factors.

From the management approach, **motivation** is a cyclic process which influences those internal needs and driving forces that trigger, control and maintain the efforts aimed at performance.<sup>107</sup>

**10.2.3.3.3. Communication**

Managers spend most of their time communicating. They have meetings, take part in discussions, manage tasks on the phone, write letters and read.

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<sup>107</sup> Dobák Miklós: Szervezeti formák és vezetés Akadémiai Kiadó Budapest, 2008. 145. o.

☞ **Communication is a two-sided process through which two or more people exchange information and interpret with some purpose.**<sup>108</sup>

Efficient communication basically determines the success of the company. An important task of the management is to create an information system. The tasks of communication are:

- to distribute and collect information
- to boost motivation and persuasion
- to enhance understanding
- to support decision making

Directions of communication inside the organization:

#### **Downward communication:**

- **realization of aims:** communicating strategic, organizational, individual aims and behavioral patterns
- **instructions and explanations for work:** determining concrete tasks, and the way of doing the work, harmonizing activities
- communication of processes, regulations: determining the frames of operation
- **feedback about performance:** the evaluation of the level of work done by subordinates
- **messages meant to educate:** messages with the help of which managers would like to get the support of employees

#### **1. Upward communication**

- **communicating problems:** the employee or the managers tells to a top manager if the implementation of the tasks is impeded
- **suggestions for development:**, communicating innovations, suggestions for rationalization to the manager
- **making reports:** regularly or occasionally, subordinates give an account of the activity, results of the assigned organization, or of their own
- **communicating grievances and arguments:** the managers task is to relieve tensions between employees

<sup>108</sup> Dobák Miklós: Szervezeti formák és vezetés Akadémiai Kiadó Budapest, 2008. 151. o.

## 2. Horizontal communication

Horizontal communication means the communication between people at the same level in the organization structure.

- **problem solving:** knowledge of different professional areas is used in the joint problem solving of different professional areas
- **co-ordination:** harmonization of tasks, aims, work of those at the same level
- **counseling, professional supervision:** staff organizations help activities in line

Horizontal communication is often realized with the help of committees, work groups.

## 3. Informal communication

Information exchange forming naturally is an important element of life of an organization, which is based on personal, informal and accidental connections. Informal communication can help, but also pull back efficient communication. False or half-true information can have a negative effect on work processes, on performance, too, but a good manager tries to make use of the informal sources, too.

### 10.2.3.4. Control<sup>109</sup>

In the course of management activities presented earlier, the management takes several measures. However, it is not enough to decide in a situation, you also have to examine to what extent the decision was successful, and how it affected company operation and efficiency.

#### 10.2.3.4.1. The notion of control

Control is process helping achieve organizational aims, based on feedback, through which managers

- determine standards in advance for the particular features of the controlled unit
- the current values of which they measure through the control process
- and compare them with the standard.

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<sup>109</sup> Dobák Miklós: Szervezeti formák és vezetés Akadémiai Kiadó Budapest, 2008. 157-166. o. alapján

- and in case of deviation between values defined in the standard and the actual values, they intervene.<sup>110</sup>

#### **10.2.3.4.2. Criteria of control**

Control, as management function, is an important process for the company management from several points of view.

1. Economic point: if control ceases in an organization, part processes may deviate from the predetermined aims, efficiency of using resources worsens, and negative result doesn't come out to light, or not early enough.
2. Psychological point: control creates a stable, foreseeable environment, marks off the aims, the frames of work, manages operation.
3. Political (power) point: the right to order about resources, and to limit decisions of lower level managers, will remain in the hands of managers with the help of control.

#### **10.2.3.4.3. Characteristics of efficient control**

1. Relative accuracy: If surveys provide inaccurate data, managers might not make appropriate decisions when making comparisons, or giving feedback.
2. Being up-to-date: the system must provide up-to-date information, so that managers could make decisions based on the actual situation.
3. Economy: the budget for operating the control system shouldn't be more than the efficiency that could be achieved with it.
4. Flexibility: the system must adapt to the ever changing conditions.
5. Intelligibility: the categories used, the determined standards have to be understood by all participants.
6. Drawing up achievable aims: real goals motivate participants, unreal ones trigger adverse effect, and pull back the realization of processes.
7. Accent on essential dimensions: due to demand for costs and time, you only have to control features which are critical for the successful operation of the organization.

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<sup>110</sup> Dobák Miklós: Szervezeti formák és vezetés Akadémiai Kiadó Budapest, 2008. 157. o.

8. Accent on deviation: for managers, only the information where the measured result deviates from the standard means the necessity of intervention, so this has to be accentuated.
  9. Multi-pointedness: if you only measure performance from one point of view, participants will only concentrate on it, and the rest will be pushed in the background. The aim is to create such a system of points of view which motivates the complete system and the achievement of the given aim, and not just a part process.
  10. Suggestion for intervention: the efficient control system doesn't only point out deviation, but makes a suggestion for intervention, too.
- ✿ As for management, it's worth reading Organizational behavior and management<sup>111</sup> by Gyula Bakacsi considering the information about the notion of power, which often determines management behavior.

Please, watch this video recording.

### 10.3 SUMMARY, QUESTIONS

#### 10.3.1 Summary

The science of management has its history, since also the activity of war-lords required serious management skills, though at that time it was rather a talent. The first empiric scientific researches about management were born after the industrial revolution, at the end of the 1800s, and have gone through several changes since then.

Management has been approached from several sides, and is still researched today: from psychological, organizational, functional, behavioral and many other points of view.

**Management** is a process in which activities serve to achieve efficiency through managing the work of other people.

**Management** is an activity which sets the goals of the organization, determines the means necessary to achieve those goals, starts, manages, and co-ordinates the activities to achieve goals.

Management is realized at different organizational levels. The top management consists of directors, deputies. Central department heads,

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<sup>111</sup> Aula Kiadó Budapest 2007. 155-164. o.

division leaders belong to the middle management. Leaders of functional part areas are the direct leaders.

Management process as problem solving consists of the following steps: problem discovery, aim determination, problem analysis, decision preparation and decision, execution, control, feedback.

Managers have to play different roles in their activities. They are: interpersonal role, information role, decision making role.

The basic functions of management are planning, organizing, direct control, co-ordination, communication and supervision.

### **10.3.2 Self-testing questions**

1. When did the first scientific theories about management appear?
2. Whose theories were significant at the end of the 1800s?
3. How did Fayol sum up the main points of his theory?
4. Who were the determinative researchers between the two world wars?
5. What did management theory focus on in the period between the two world wars?
6. Who were the determinant researchers following WW II?
7. What did management theory focus on after WW II?
8. Recommend a journal with the help of which one can get informed about the current trends, researches of management theory.
9. What does the notion of management include?
10. How do we define the notion of management?
11. Introduce the organizational management levels, and the characteristic positions belonging to the particular levels.
12. Describe management as the process of problem solving.
13. What roles does a manager have to play?
14. What are the functions of managers in general (based on Fayol's theory)?
15. Which two basic strategy types do we distinguish in the course of creating strategy and setting aims?
16. What does organizing mean?
17. What are the basic tasks of organizing?
18. Describe the process of organizing.
19. What does direct control mean out of the management functions?

20. What are the tasks of human resources management?
21. What influences basically the performance of employees?
22. What does motivation mean from the point of view of management theory?
23. What's the role of communication in management? What are its tasks?
24. Concerning its direction, what kind of communication forms do we distinguish? Tell examples on each.
25. What's the role of control in company management?
26. Describe the notion of control.
27. Explain the system of aspects of control.
28. What are the attributes of efficient control?
29. What does power mean, and how does it prevail at an enterprise?

### 10.3.3 Practice tests

1. Which management theory researcher worked in the given periods? Put an X into the appropriate column.

Researcher	from the end of the 1800s to WW I	between the two world wars	after WW II	today
Dickson		X		
Fayol	X			
Drucker			X	
Taylor	X			
Mintzberg			X	
Mayo		X		
Bakacsi				X
Friedberg				X
Maynard			X	
Roethlisberger		X		

(Answer: marked in red in the table!)



4. Match the notions with the definitions.

Notion	Definition
1) organizing	a) bilateral process in which two or more people exchange and interpret information for some purpose
2) co-ordination	b) it's directed at profitability, productiveness and development as for the whole of the company
3) managing	c) process in which activities serve to achieve efficiency through managing other people's work
4) control	d) activity aimed at the realization of pre-determined goals by harmonizing the personal and material resources of the organization
5) communication	e) harmonizing the tasks, aims and work of those at the same level
6) management	f) activity which sets the aims of the organization, determines the necessary means to achieve the aims, manages and co-ordinates the necessary activities to achieve aims
7) basic strategy	g) process based on feedback, helping to achieve the aims of the organization

(answer: 1) d), 2) e), 3) f), 4) g), 5) a), 6) c), 7) b))

5. Mark if the following statements are true (T) or false (F).

1. Taylor dealt with the rationalization of company process with scientific character. (T)

2. Between the two world wars noted researchers of management science were Ernest Dale, Peter F. Drucker, Maynard és Mintzberg. (F)

3. Management is a process in which activities serve to achieve efficiency through managing other people's work. (T)

4. Top managers need a smaller proportion of concept making knowledge, together with a bigger proportion of technical skills. (F)

5. The elements of the problem solving process are problem discovery, aim determination, communication, problem analysis, decision and feedback. (F)

6. We defined management roles based on Drucker's work (F)

7. Co-ordination is harmonizing work processes with the actors of the organization. (T)

8. Functional strategy is connected to the industrial competitive position of different products of the organization. (F)

9. One way of activating actors of the organization is incentives, like cafeteria. (T)

10. The task of human resources management is to attract and keep the necessary employees. (T)

6. Mark roles belonging to the particular group. Several roles may belong to one group.

Group	Role
A) Interpersonal roles	1. disturbance elimination role
	2. spokesperson role
B) Information roles	3. manager role
	4. resource distributor role
C) Decision roles	5. public appearance role
	6. entrepreneur role

(answer: A: 3., 5., B: 2., C: 1., 4., 6. )

7. Make a list of the main tasks of direct management, as management function.

1. ....
2. ....
3. ....
4. ....

(answer: 1. human resources management, 2. motivation, 3. communication, 4. creating and leading groups)

8. Place the following manager types at the appropriate managing level.

- division leader
- director
- head of production
- executor in line

- marketing manager
- deputy director
- central unit leader

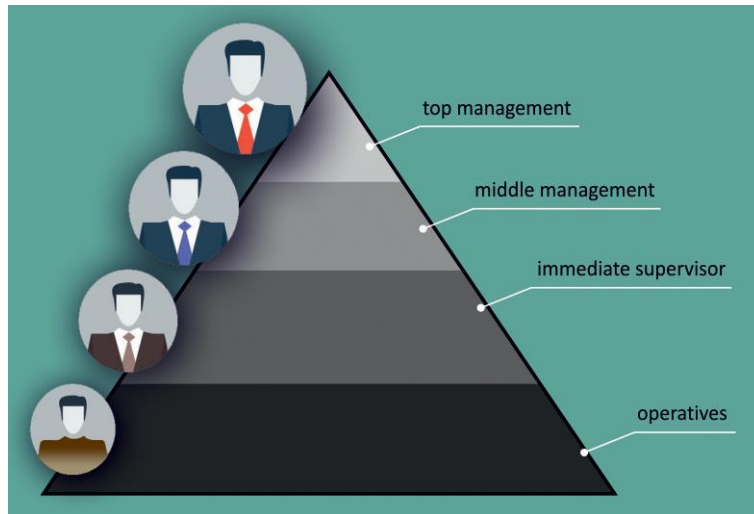


Figure 28: Figure of Task 6

(answer: figure 27)

9. Arrange the steps of the control process in the appropriate order.

1. Survey of features
2. Feedback
3. Determination of standards
4. Determination of organization aims
5. Comparison

(answer: 1. determination of organization aims, 2. Determination of standards, 3. Survey of features, 4: Comparison, 5. Feedback)

10. Select the tasks below which are NOT the tasks of human resources management.

1. finding, selecting, hiring devoted people with suitable skills
2. determining spheres of activity,
3. distributing and collecting information,
4. creating remuneration, payment system,
5. employees' performance evaluation,
6. education, further training,
7. public appearances,
8. disturbance elimination,
9. handling emerging disciplinary and other work problems,
10. handling work connections (with unions),
11. co-ordination
12. operating a planning and information system concerning the tasks above.

(answer: 3, 7, 8, 11)

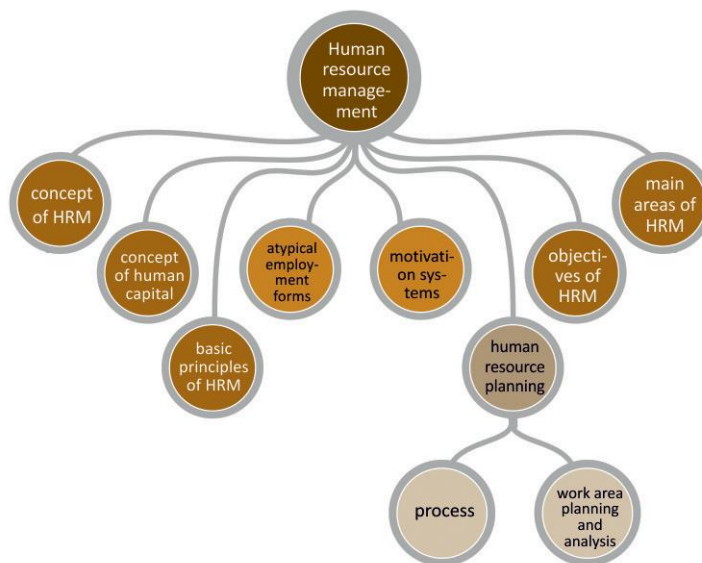
## 11. LESSON: THE IMPORTANCE OF KNOWLEDGE AND OF HUMAN CAPITAL IN THE LIFE OF ENTERPRISES

### 11.1 OBJECTIVES AND COMPETENCIES

In this unit students learn about the notion of human resources management, its aim, tasks, basic principles and main areas. They will learn the process of human resources planning, and the methods of sphere of activity planning and analysis.

Students are allowed to examine atypical employment types which are becoming more and more frequent and are more and more often used to manage difficulties, and will learn the methods of the incentive system.

### 11.2 CURRICULUM



*Figure 29: Concept map*

#### 11.2.1 The notion of human resources management

The success of a company, in a significant part, depends on the resources which they already have, or can obtain, and on their quality and value. Out of the resources of the enterprise, earlier the material

assets were emphasized, most recently, however, the role of human resources, human capital has been more and more appreciated.

The resources of the enterprise are:

- tangible assets: real estate, machines, equipment
- financial means: credit money, cash, loan, initial capital
- intangible (immaterial) assets: patents, trade marks, brand
- human capita: knowledge of employees, their skills, experience, system of connections, motivation

In this unit we deal with this latter one, the human capital.

☞ **Human capital is a collective value based on the knowledge and skills of the organization members, and added up of life and work experience, and motivations.**<sup>112</sup>

Human resources differ from other resources (e.g. tangible assets) t several points:

- they can't be stored
- they are innovative, it can renew
- they make decisions, with which they influence their performance
- they are not the property of the company, it only „rents” them

You have to husband human capital just as the company's money, or other tangible assets. The process of husbandry, however, is a lot more complex and less palpable, than the material assets.

☞ **The point of human resources management is that it determines the demand for human resources of the necessary quality and quantity to achieve the aims of the organization. It finds, selects, „obtains” the resources, manages their efficient use, development, or if it's necessary, handles their lay-off. Together with this, it co-ordinates the aims and demands of the organization and the employees, and takes them mutually into consideration when making decisions.**<sup>113</sup>

☞ **According to another wording, human resources are a strategy with which the company obtains, develops, manages, motivates**

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<sup>112</sup> Karoliny Mártonné – Poór József: Emberi erőforrás menedzsment kézikönyv Complex Kiadó Budapest 2010. 25. o.

<sup>113</sup> Karoliny Mártonné – Poór József: Emberi erőforrás menedzsment kézikönyv Complex Kiadó Budapest 2010. 26. o. alapján

**and makes devoted the resource of key importance in the organization, for the organization, the working people.<sup>114</sup>**

Human resources management influences the life of the company in several fields. The system of these influences can be seen in the figure below:

The four basic principles of human resources management are:

- human resources are the most important asset of the organization, their efficient management is a key to the success of the organization
- most probably, you can only achieve organizational success if human strategy and human politics are tightly connected to strategic plans, and contributes to achieving company aims.
- company culture, values, work atmosphere, and management behavior are the main components of organizational success, this culture must continuously be maintained, shaped
- continuous efforts have to be made to improve unity between people, so that the members of the organization achieve their own goals by working to realize organizational aims<sup>115</sup>.

### **11.2.2 The aim of human resources management**

The main aim of human resources management is, as you could see it in the figure above, to **improve organizational performance**. The two main categories of it are **successfulness** (the extent of fulfillment of requirements set by the actors, and of the worded aims), and **efficiency** (the most economical use of resources to achieve the given satisfaction level of the actors).

Since efficiency greatly depends on the attitude and motivation of employees, it's important to create a fair connection in both directions between the organization and the employees. This is also the condition to achieve success on the long run. Continuously improving the satisfaction of employees, the safe and healthy working conditions greatly influence the relationship between the organization and the employee. The

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<sup>114</sup> Armstrong, M. in: Matiscsákné Lizák Marianna: Emberi erőforrás gazdálkodás Complex Kiadó Budapest 2012 84.o.

<sup>115</sup> Matiscsákné Lizák Marianna: Emberi erőforrás gazdálkodás Complex Kiadó Budapest 2012 84-85.o.

continuous improvement of knowledge and skills contributes to achieving individual aims.<sup>116</sup>

The goal of human resources management is organizational efficiency, and to ensure the sustainability and growth of the organization. Their direct goal is to work out economic principles and methods that can be used in practice, which consider, on the one hand, the needs and efforts of groups and individuals contributing to the successful operation of the organization, on the other hand, the aims and requirements of the organization.<sup>117</sup>

### **11.2.3 The main areas of human resources management**

HR roles, and spheres of tasks have gone through significant changes in the history, and they keep changing and expanding. In general, the main areas of human resources management are the following:

1. Working out human resources strategy.
2. Planning, auditing and supervision.
3. Analysis and planning of sphere of activity
4. Ensuring human resources.
5. Evaluation of sphere of activity.
6. Incentive management.
7. Evaluation of performance.
8. Improving human resources.
9. Managing work connections.
10. Operating an information system.
11. Culture change – change management.
12. Competency and EI (emotional intelligence)120
13. Internal communication.

The task system of human resources management is summed up in the figure below:

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<sup>116</sup> Karoliny Mártonné – Poór József: Emberi erőforrás menedzsment kézikönyv Complex Kiadó Budapest 2010. 28-29. o. alapján

<sup>117</sup> Matiscsákné Lizák Marianna: Emberi erőforrás gazdálkodás Complex Kiadó Budapest 2012 86.o.





Figure 30: The HRM system of staff activity: employment segment

### 11.2.4 Planning human resources

Planning of human resources, and the economy with them is influenced by several external factors. Such factors can be the *general operation of the economy* (prosperity, stagnation or recession, demography, development), the *situation of the labor market* (if there's unemployment or lack of labor force, the number of missing professions), what *legal regulations* define the frames of employment and labor force market (strict administration, financial support), *workers' unions*.

In the course of planning, you, of course, have to consider the internal factors of the company, too. Such factors can be the *size, structure of the company, pace of innovation, spheres of activity, market situation, use of modern management concepts, features of spheres of activity, characteristics of current employees, organizational culture*.

The factors above, and several other factors affect the area of resource economy. In the course of planning, you have to examine the traceable influencing factors, to examine the current and expected future value of it, and the effect on the organization. According to this you have to shape the future aims, and the necessary means to achieve them.


- ☞ **Planning human resources is a complex, cyclic planning process, the steps of which are analysis (considering the current situation**

**and future developments, deviation analysis within), setting aims, and making action plans.<sup>118</sup>**


The figure below sums up the method of estimating organizational labor force supply:

- In the course of *analyzing the current situation* they size up the current staff activity, they analyze the operation and features of employees and spheres of activity, and they size up if the employees are suitable for the tasks to be carried out.
- To carry out future tasks first they have examine the external environment, then the internal environment, finally they analyze the aims drawn up in the strategy and the business plan.
- Considering present and future, with the help of deviation analysis, they compile the actions, *action planning* is done. A human resources aim can be e.g. to strengthen productivity, carry out stronger labor cost control, or to comply with laws that have changed. When drawing up actions you have to consider the following:
  - likely profits, advantages,
  - foreseen costs,
  - technical feasibility,
  - possible consequences in human resources economy,
  - acceptance with managers and employees,
  - role of key people (keeping, hiring, laying off, promoting),
  - factors influencing, limiting or encouraging successful employment.<sup>119</sup>

The figure below shows the system of human resources action plans:

 At the link below you can read the analysis of the US labor statistical office about how recession affects labor force, and what methods there are to eliminate unemployment.:

<http://www.bls.gov/opub/mlr/2014/article/public-workforce-programs-during-the-great-recession-1.htm>

 At the link below you can read an interview with David Fairhurst, HR manager of McDonalds Co. about how McDonalds manages the HR effects of the crisis:

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<sup>118</sup> Karoliny Mártonné – Poór József: Emberi erőforrás menedzsment kézikönyv Complex Kiadó Budapest 2010. 138. o.

<sup>119</sup> Karoliny Mártonné – Poór József: Emberi erőforrás menedzsment kézikönyv Complex Kiadó Budapest 2010. 143. o. alapján

<http://www.hrzone.com/topic/managing-people/david-fairhurst-interview-managing-workforce-recession>

### 11.2.5 Sphere of activity planning and analysis<sup>120</sup>

#### 11.2.5.1. *The notion of sphere of activity and of sphere of activity analysis*

A marked task of human resources management is the planning of the sphere of activity.

- ☞ **The sphere of activity is the smallest identified unit of the organization, which has an aim, dynamics and an individual responsible person, the employee.**
- ☞ **The analysis of the sphere of activity provides information about the points of the sphere of activity, the tasks to be done, the rules of responsibility and authority, the requirements to be met by the employee.**

It's a general systematic procedure with the help of which we determine things connected to performing tasks of the sphere of activity:

- organizational relationships (e.g. superior, direct subordinate),
- tasks and responsibilities,
- connections,
- possibilities and limits,
- requirements of the sphere of activity (knowledge, experience, skills).

#### 11.2.5.2. *The process of analyzing the sphere of activity*

Several forms of analyzing the sphere of activity are known, but in the best case, it consists of the following steps:

- selection of analyzing method
- information collection
- observation and analysis of work processes
- systematization of information
- security viewing

<sup>120</sup> Karoliny Mártonné – Poór József: Emberi erőforrás menedzsment kézikönyv Complex Kiadó Budapest 2010. 167-179. o. alapján

- update (in certain periods)

The analysis of the sphere of activity starts with background examination. For this, you have to examine the aims, expectations, main tasks, spheres of activity, authorities, and other requirements necessary to fulfill the job.

Information can be obtained by *observation*, too. The analyzer observes the employee while it is working, and notes down the details connected to the sphere of activity. Observation can be personal, or can be carried out by video recording.

A frequent observation method is *sampling workday recording*. In the case of frequently repeated tasks they only observe one part of the working time, not the whole of it. It can be completed with an *interview* made with the employee. Instead of interviews, filling in *questionnaires* is also a useful method for collecting information.

The information collected with the methods above is worked up by analyzers, finally the result of the research is ready. It's important to remark, though, sphere of activity analysis has to be not a single event, but a cyclic repeated process, since the changing conditions might justify the change of conditions in connection with the sphere of activity.

#### 11.2.5.3. *The result of the analysis of the sphere of activity*

The result of the analysis is the following:

##### **Sphere of activity specification:**

- necessary education
- special education (postgraduate training)
- necessary experience
- qualification
- practice time
- competencies
- physiological and psychological conditions

11. **Description of sphere of activity:** a document drawn up at high level, based on the analysis of the spheres of activity, containing the aim of the particular spheres of activity, their place in the organizational hierarchy, their main responsibilities, the performance indexes belonging to them.<sup>121</sup>

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<sup>121</sup> Karoliny Mártonné – Poór József: Emberi erőforrás menedzsment kézikönyv Complex Kiadó Budapest 2010. 174. o.

- personal particulars
- the aim of the sphere of activity
- the task of the employee doing the job
- required qualification
- authority
- responsibility
- place in the organizational structure (subordinates, superiors)
- performance indexes
- supplementary information (place, salary, working time, working schedule).

#### 11.2.5.4. *Atypical employment forms*<sup>122</sup>

Different than the usual employment forms, there are several other legal forms of employment, which can be applied in the case of certain spheres of activity.

☞ **Atypical employments are the ones which are different from the traditional full-time employment for unlimited period.**

They are e.g.:

- **Telework:** flexible employment form in time and space, where the employee doesn't work at a traditional workplace, but far away from it, and the result of the regular daily work is passed on to the employer through information and communication technologies.
- **Part-time employment:** Part-timers are employees whose working time is calculated on a weekly, monthly or yearly average is less than that of the full-timers' compared to them.
- **Fixed-term or project employment:** In the work contract they can determine the finishing date of employment. After this, without any special agreement, the employment is terminated, or on common consent, it can be extended.
- **Manpower leasing:** activity in the framework of which leaser temporarily lets borrower have the employee in contract with leaser for use for compensation (leasing)<sup>123</sup>.

<sup>122</sup> Karoliny Mártonné – Poór József: Emberi erőforrás menedzsment kézikönyv Complex Kiadó Budapest 2010. 213-216. o. alapján

<sup>123</sup> Munka törvénykönyve (2012. évi I. törvény a munka törvénykönyvéről) 214. §

- **Work done not in employment (commissioning):** With an agency contract the commissioned person is entrusted to do the given work, but he doesn't become the employee of the company.
- **Self-employment:** owners of enterprises without an independent company (private enterprise).
- **Outworker relationship:** outworkers do the work in their own home, with their own tools, independently, without the direct control of the employer, but with the material provided by the employer. Outworkers usually do this as a second job.
- **Occasional employment (simplified employment):** temporary, only occasional, but legal employment. In the frames of simplified employment you can hire employees for the following work: household work, work done for prominently public benefit organization, agricultural seasonal work, tourism seasonal work, odd job.
- **Transit and fixed-term employment (with government support):** special employment form, especially used for lasting unemployed, starters, socially needy, and people with changed working abilities. In the course of temporary employment it turns out who becomes a good workforce. Transit employment is a kind of transition between the primary labor market and therapeutic employment, since its aim is to physically and mentally strengthen those who are underprivileged from the labor market point of view, to facilitate their employment.
- **Student work:** according to the Labor Code, young employees are the ones who are not 18 years old yet. For their employment they need the consent of their legal representative. For them work at night, or extra work time can't be ordained. The daily working time of a young employee can only be the maximum of 8 hours.
- **Public work:** transitional employment of lasting job seekers, people in their active age out of job seeking benefits, in spheres of activity where they realize local, community aims. The public work program prefers settlements and regions, and also social groups which are most underprivileged from the labor market point of view. It can be given through competition, it's central subsidy<sup>124</sup>.

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<sup>124</sup> 49/1999 (III. 26.) Korm. rendelet a közmunkaprogramok támogatási rendjéről

### 11.2.6 Incentive systems<sup>125</sup>

The incentive system is the complex of those rules, procedures and methods on the basis of which the organization realizes the employees' concrete incentives, and establishes their salary and benefits.

The aim of the incentive system is to motivate employees

- to work their working time,
- to boost performance,
- to improve their professional knowledge and ability,
- to work flexibly,
- to strive for promotion.

The elements of the incentive package are:

**Basic wage:** the individual wage is built up of the following elements:

- **basic wage:** place on the payroll, respectively wage given in the case of 100% performance,
- **ordinary wage:** usually the wage accounted for the actual work done (wage by results), or depending on the length of time spent working (hourly wage),
- **allowance:** extra wage compensating for special conditions connected to a given activity or sphere of work (danger money, overtime, night payment),
- **premium:** extra wage given for doing extra work determined previously, or in the case of achieving a previously assigned aim,
- **bonus:** extra wage given on the basis of a complex, follow-up evaluation of the work,
- **supplementary wage:** wage due to working time legally not spent with work (yearly regular holiday, commission, foreign service),
- **other wage:** wage due to notice period not spent working, wage for work not connected with sphere of work, innovation prize, wage of casual workers, wage of those doing a second job, etc.

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<sup>125</sup> Karoliny Mártonné – Poór József: Emberi erőforrás menedzsment kézikönyv Complex Kiadó Budapest 2010. 332-345. o. alapján

The basic wage can be:

- **Hourly wage:** payment is determined on the basis of the period of time worked.
- **Wage by results:** type of wage used in manual work, connected to the realized performance compared to the established norm of the sphere of work.

The incentive methods of the hourly wage:

- **Payroll place and tariff systems:** spheres of activity, employees are categorized, and the basic wage is determined by categories, similar work is paid similarly.
- **Wage systems based on seniority:** payroll place categories are further divided into periods depending on period of service, since employees get more experienced and proficient, so they work more efficiently and productively.
- **Competency-based wage system:** the grades of the basic wage are connected to competencies necessary for the particular sphere of activity. Based on the necessary and useful competencies, the particular payroll and wage categories can be further broken down.
- **Differentiation according to individual performance:** it evaluates the deviation from the basic expectation, it motivates higher performance.

The incentive methods of performance based wages:

- **Bonus, commission:** bonus can be built into performance wages, as well, it can be combined with premium. The commission system is mostly used in commerce, and it means the wage is supplemented with a certain per cent of the turnover after the turnover is realized.
- **Group wage:** we don't want to make the members of a group interested in maximizing their own individual performance, but in helping the total performance of the group, that is we want them to do what is necessary for the whole of the group.

**Long term incentives, share techniques:** everybody is interested in getting a share from the company's result, it motivates all employees of the company if they are granted a possibility of getting a share free or at discount price. An ownership connection, stronger than just being an



employee, is created, at the same time devotion towards the company increases.

**Incentive methods of non-wage character:** These methods don't primarily appear in money, wages. They can be e.g.:

- possibility for promotion connected to conditions
- increasing responsibilities or authorities
- reassignment to a more prominent place
- incentive trips
- improving working conditions (new computer, office, quality instrument).

As you can see, human resources management is an activity closely and directly influencing the performance of the company. With bigger companies, a well-prepared department performs this activity, and strives to continuously improve its methods, competencies, to meet the values of employees, owners and managers.

### 11.3 SUMMARY, QUESTIONS

#### 11.3.1 Summary

The performance, success greatly depends on the employees' and managers' abilities, experience, motivation.

**Human capital** is a complex value of work and life experience, and also of motivation, based on the organization members' abilities and knowledge.

The company's human resources management is aimed at determining the demand for human resources of the necessary quality and quantity to achieve the aims of the organization. It finds, selects, 'obtains' them cares about their efficient employment, development, or in case it's necessary, about their lay-off. It harmonizes the aims, demands of the organization and of the employees, considers them all when making decisions.

The main aim of human resources management is to **boost organizational performance: successfulness and efficiency.**

The main areas of human resources management are the following:

1. Working out human resources strategy.
2. Planning and auditing, supervising.
3. Analysis and planning of the sphere of activity.

4. Providing resources.
5. Evaluating the sphere of activity.
6. Incentives management.
7. Evaluating performance.
8. Developing human resources.
9. Managing labor connections.
10. Operating an information system.
11. Changing culture – managing changes.
12. Competency and emotional intelligence.
13. Internal communication.

**Human resources management** is a complex, cyclic planning process, the steps of which are (analysis, with considering the current situation and future developments within, deviation analysis), setting aims and action planning.

- Analysis of the current situation
- Realizing future tasks
- Action planning

The **sphere of activity** is the smallest identifiable unit of the organization, which has an aim, dynamics, and an individual responsible person, the employee.

The **sphere of activity analysis** provides information about the main points of the job, activities to be done, responsibility and authority rules, the demand made on the employee.

The steps of sphere of activity analysis:

- selecting method of analysis
- collecting information
- observing and analyzing work processes
- organizing data
- security screening
- updating (periodically)

The result of the job analysis is the *specification of the sphere of activity* and *job description*. A munkakörelemzés eredménye a *munkakör-specifikáció* és a *munkaköri leírás*.

**Atypical employment** is the one which is different from the traditionally used full-time employment of unlimited period. The main types of this are:

- Teleworking
- Part-time employment
- Fixed-term, or project employment
- Manpower lease
- Work done not in employment (commissioning)
- Self-employment
- Outworker relationship
- Occasional employment (simplified employment)
- Transit and fixed term employment (with government support)
- Student work
- Public work

The **incentive system** is the complex of rules, procedures and methods, on the basis of which the organization realizes the concrete incentives of employees, and establishes salaries, allowances.

Basic wage: the individual basic wage is usually built of the following elements:

- basic wage
- ordinary wage
- allowance
- premium
- reward (bonus)
- supplementary wage
- other wage

The basic wage can be:

- Hourly wage
- Payment on results

The incentive methods of the hourly wage:

- Payroll place and tariff systems
- Wage based on seniority
- Competency based wage system

- Differentiation by individual performance

The incentive methods of performance based on remuneration:

- Bonus, commission
- Group wage
- Long term incentives and share techniques.

### **11.3.2 Self-testing questions**

1. What does human capital mean?
2. Compared to other resources of the company, what kind of role do human resources play?
3. What does human resources management mean?
4. What are the basic principles of human resources management?
5. What are the aims of human resource management?
6. What are the main areas of human resources management?
7. What external and internal factors influence human resources planning?
8. What steps does human resources planning have?
9. What factors have to be considered when making an action plan?
10. How does McDonalds handle the HR effects of the crisis.
11. What does sphere of activity mean?
12. How do we define the notion of sphere of work analysis.
13. What do we have to determine through the analysis of the sphere of work.
14. Describe the process of job analysis.
15. What sources can we get information from for the background analysis?
16. What are the result(s) of the job description?
17. Introduce the known typical employment forms of atypical employment, and their main points.
18. What is the incentives system?
19. What is the aim of the intensive system?
20. What are the basic elements of the information package?
21. What kind of basic wage types do we use?
22. What are the incentive methods of the different basic wages?

23. What kind of incentive methods do you know besides the ones of non-payment character?

### 11.3.3 Gyakorló tesztek

1. Mark the statements below if they are true (T), or false.
  1. Human resources can't be stored. (T)
  2. One of the tasks of human resources management is to efficiently husband human capital. (T)
  3. Human resources management has an effect on the employees' motivation. (T)
  4. The source of inflow of employees at a company can be internal relocation and quitting. (F)
  5. The continuous improvement of employee satisfaction and the safe and healthy work environment have a minor effect on th relationship between the employee and the organization. (F)
  6. While planning human resources, you have to consider external factors of the company, too. Such factors can be, e.g. the size and the structure of the company. (F)
  7. The steps of human resources planning are analysis, setting aims and action planning. (T)
  8. The job analysis starts with the arrangement of data. (F)
  9. The sampling work day recording is used to observe rare, individual tasks. (F)
  10. The aim of job specification is to determine aim of the individual jobs, their place in the organizational structure, and their main responsibilities. (F)

1. Match the atypical employment ways with their definitions.

Way of employment	Definition
1) Part-time employment	a) the employee doesn't regularly do the daily work at a traditional work place, but away from it, and the result is forwarded to the employer via information and communication technologies
	b) in the work contract there is a date until which the work relationship is operative. After this the work relationship is terminated without special agreement.

3) Fixed term employment	c) owners of enterprises having no individual companies
4) Assignment	d) employees work at home, with their own tools, independently, without the direct control of the employer, but with materials provided by the employer
5) Simplified employment	e) the company temporarily assigns its employee in work contract with it in exchange for payment to another company
6) Teleworking	f) E.g. You can employ this way employees for seasonal work, occasionally.
7) Self-employment	g) with the help of a contract the employer is assigned the work but it doesn't become the employee of the company
8) Labor force leasing	h) the employment time of the employee is less on the weekly, monthly or yearly average than that of a full-time employee in comparison
9) Public work	i) Temporary employment mainly for the permanently unemployed, socially underprivileged, when it turns out who can become a good work force.
10) Transit employment	j) work provided for young employees, where daily working time can be the maximum of 8 hours.
11) Student work	h) transitional employment in contract for permanent job seekers, in jobs where they realize local, community aims.

(answer: 1) h), 2) d), 3) b), 4) g), 5) f), 6) a), 7) c), 8) e), 9) h), 10) i), 11) j)

2. Mark which tasks of human resources management are of organizational (O), labor force (L) or service (S) character.

1. organizational structure (O)
2. recruitment, selection (L)
3. payment (L)
4. decision system (O)
5. welfare, social programs (S)
6. co-ordination (O)
7. information, personnel recording (S)
8. human resources planning (L)
9. job description (O)
10. job evaluation (L)
11. organization development (O)
12. work security, company healthcare (S)
13. practical issues of employment (L)
14. performance evaluation (L)

3. How shall we plan next year's internal human resources supply?  
Complete the formula.

..... - ..... + ..... = .....

4. Mark with X in the table which are the inflow and outflow sources of human resources at the company. One source might mean inflow and outflow at the same time.

Source	Inflow source	Outflow source
internal relocation	X	X
quitting		X
hiring from external source	X	
dismissal notice		X
promotion	X	X
death		X
withdrawal	X	
pensioning		X
downsizing		X

5. Human resources management tries to influence the employees' personal and behavioral factors. From below, choose which ones belong to the personal (P), or behavioral (B) factors.

- devotion (B)
- learning (P)
- motivation (B)
- relationships (P)
- skills (P)
- competencies (P)
- experience (P)
- performance (B)
- knowledge (P)
- practice (P)

6. Match the wage type allowances with their definition.

Allowance form	Definition
1) supplementary payment	a) wage for warning time not worked, work fees not connected to job,
2) core wage	b) wage for time depending on period actually spent with work, wage for work actually performed
3) bonus	c) wage for 100% performance
4) premium	d) wage for working time legally not spent with work (e.g. for foreign service)
5) other wage	e) extra wage compensating for special conditions connected to a given job
6) extra wage	f) extra wage based on a complex, subsequent evaluation of the activity
7) basic wage	g) extra wage for doing a predetermined extra task, or for achieving an appointed aim

(answer: 1) d), 2) b), 3) f), 4) g), 5) a), 6) e), 7) c))

7. Mark which incentive form is more characteristic for the payment by time or the payment by result system. It might happen that a form can be used at both types.

Type of incentives	Payment by time	Payment by result
Differentiating by individual performance	X	
Group wage		X
Payroll place and tariff systems	X	
Incentive methods of non-wage character	X	X
Wage systems based on seniority	X	
Bonus, reward		X
Long term incentives,	X	X



share techniques		
Competency based wage system	X	

## 12. UNIT: ROLE OF INNOVATION

### 12.1 UNIT: ROLE OF INNOVATION

#### 12.2 OBJECTIVES AND COMPETENCIES

In this unit students will learn the concept, importance, and process of innovation. They will know the main types of innovation and the main usages. By acquiring the unit they will recognize the importance of innovation, applicable innovation types, and factors of innovation.

#### 12.2.1 Curriculum

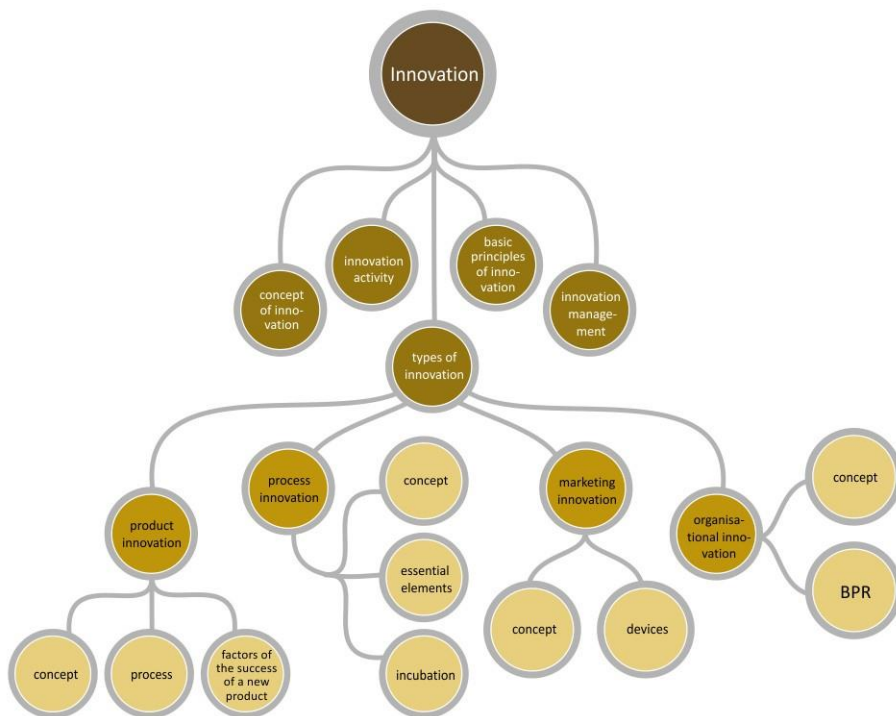


Figure 31:

Innovation  
 Concept - Innovation activity - Innovation types - Innovation principles  
 - Innovation management

Product innovation  
Concept - Process - Factors of new product's success  
Process innovation  
Concept - Important elements - Incubation  
Marketing innovation  
Concept - Assets  
Organizational innovation  
Concept - BPR

### **Concept of Innovation**

The word innovation means renewal, reformation. In the life of companies continuous renewal is important especially if they want to stay in competition and keep their position on the market.

The concept of innovation is understood in many different ways, several approaches. The first important definition is connected to Schumpeter.

According to Attila Chikán's concept, innovation is satisfaction of the needs of consumers in a highest than ever quality way.

In the Oslo Manual of Innovation is the implementation of a new or significantly improved product (goods or service), or process, a new marketing method, or a new organizational method in business practices, workplace organization or external relations.

Innovation activities are all the scientific, technological, organisational, financial and commercial steps which actually, or are intended to, lead to the implementation of innovations. Some innovation activities are themselves innovative, others are not novelties but are necessary for the implementation of innovations. Innovation activities also include R&D that is not directly related to the development of a specific innovation.

Main types of innovation according to Oslo Manual:

- product innovation
- productivity (process) innovation
- marketing innovation
- organizational innovation

Product innovations can utilize new knowledge or technologies, or can be based on new usages or combinations of existing knowledge or technologies. The term "product" is used to cover both goods and services. Product innovations include both introduction of new goods and services and significant improvements in functional or user characteristics of existing goods and services.

Process innovations: use of new or modified production or support methods. Process innovation includes significant changes in techniques, assets, and software. Process innovation is closely connected to reducing production and shipping costs, increasing of quality results, new or significantly improved products during manufacturing and distribution.

Marketing innovation is implementation of a new marketing method involving significant changes in product design or packaging, product placement, product promotion or pricing.

Organizational innovation is the implementation of a new organizational method in the firm's business practices, workplace organization or external relations.

In relation to product creation Booz, Allen and Hamilton consulting firm categorized new products from the perspective of firm and market in the following groups:

- New product all over the world: new products that create a totally new market.
- New product lines: new products with which the company first approaches the market
- Completion of product lines: new products which are used to complete the already available products (for example new aromas, new packing sizes)
- Perfecting and altering available products: new products which substitute available products. They have better performance and higher value.
- Repositioned products: available products which aim new markets, new market segments.
- Reduced cost products: new products with lower costs but same performance.

Principles of innovation:

- consumer orientation: improvements should start from the needs of consumers
- novelty: an available product, technology, organization, etc. should be provided significant novelty
- uncertainty: innovation is always costly, but income is always uncertain, so it is always up to the welcome of the innovation
- sustainability scale: an innovation is successful, if it is sustainable until the investments return, and in longer term it is fit for consumer needs.

### 12.2.2 Product innovation

Product development process means all the activities from searching for new ideas to launching products on the market.

Steps of product development process are shown below:

Search for new ideas > Selection of ideas > Product development > Product testing > Market launch

#### 1. Collection of product ideas

To stay in competition, to keep market position, for development it is needed for the company to improve its offer, produce a better, more modern products that can satisfy consumer needs. To achieve it the company needs to seek ideas permanently, should consider terms of external environment, internal capabilities, offers of competitors and consumer needs. Information can be acquired from the following sources:

##### *External sources:*

- consumers
- users
- suppliers
- competitors
- companies specialized in product development
- research institutes

##### *Internal sources:*

- research department of the firm
- manufacturing units
- sales organization
- market research organization

From the compiled list must be selected those ideas that can be implemented. The **selection of ideas** is done from technical, market and financial point of view and results in achievable idea, or list of ideas. Product concepts are developed in connection with idea collection.

**Product concept** involves product plan stored on computer or on technical drawing, description of the aimed market, planned quality of the performance, costs and financial edges.

If all the decision making parts of the company agree on the product conception, technical improvement starts. This results in a **prototype**.

Next step is the test of the prototype if it fulfils the function, which the product concept was built on and also if it meets technical, safety, or

standard specifications? The product is also subject to market test, expected consumer acceptance is monitored before starting mass production.

Basic concept of test market, is testing in target group in appropriate environment. The product is shown in real, or similar market whose size is known and the market is verifiable (eg. stores). The product is observed among other products on the test market. (presence of competing products)

If the prototype functions properly the trial production begins. The new product should be suitable for mass production, you need to design a new or modify an existing technology. It is important to note that the mass production is different from the production of specific nature pieces. Here it is not about volume increase, but rather the development of appropriate technology.

By reaching the right volume actual **market launch** can be started, which is usually associated with significant marketing action series.

The success of the new product depends on many factors, among which the most important are:

- The benefits offered by the product
- Matching the existing set of values
- The product complexity
- The prerequisites of using the product
- The tangible results

New product development at Rolls- Royce's: you can read more information:

✿ [https://www.press.rolls-roycemotorcars.com/rolls-royce-motor-cars-pressclub/pressDetail.html;jsessionid=vktLTnpXfZrmMjKXy0jyLJV0Rp36921q6W0J2ycrcwrfJg1Twyv!1083177899?title=rolls-royce-motor-cars-confirms-development-of-new-model&outputChannelId=4&id=T0190744EN&left\\_menu\\_item=node\\_5183](https://www.press.rolls-roycemotorcars.com/rolls-royce-motor-cars-pressclub/pressDetail.html;jsessionid=vktLTnpXfZrmMjKXy0jyLJV0Rp36921q6W0J2ycrcwrfJg1Twyv!1083177899?title=rolls-royce-motor-cars-confirms-development-of-new-model&outputChannelId=4&id=T0190744EN&left_menu_item=node_5183)

### 12.2.3 Process of technology innovation

Technology innovation is often the result of product innovation, but also may appear separately.

*For example, if a cheese factory has mass production of cheese but creates artisan cheeses also, a new procedure will be implemented. The product and the quality is likely to be quite different. The new product –*

*although is a type of existing ones - but will be sold in better quality, higher price to other consumers and with different sales process. Thus the process that began as technology innovation will actually interweave several types of innovation.*

Significant elements of technology innovation:

- The choice of technology, the degree of specialization, implantation into corporate processes
- Immersion in the essence of the technology, incorporation of the technology into the company's knowledge material (how much development is desired?)
- The sources of technology (where are they from?)
- Time scheduling (try to be leader, or what kind of delay is allowed for ourselves?)
- size of R&D investment
- R&D organization and politics.

Act 2004 CXXXIV. reveals the concept of technological innovation:

Technology innovation is to improve the efficiency of economic activity, profitability and achieve positive social and environmental effects with the use of scientific, technical, organizational, management and trading operations. This results in new or modified products, processes, services. New or substantially modified procedures, technologies are applied and introduced in the market, including the changes, which constitute novelty only in a particular sector or specific organization.

As the Innovation Law and definitions and Oslo Manual shows the technological innovation is not just about development in the mode of manufacturing the product but also includes the new organizational, economic, commercial technology, equipment, or even the use of new software.

Some of the firms - particularly smaller companies - do not always have the necessary capacity for development, either machines or human resources are concerned. Method for solving the problems of temporary capacity is incubation.

The incubation is to provide comprehensive services that provide businesses the opportunity to develop innovative plans. Businesses do not need to create an expensive infrastructure development and organization, which returns slowly and difficult, they "rent" it. Small investment demand creates an opportunity for small businesses with

lower capital power to improve their chances of survival and establish market positions.

Technology incubator provides technology oriented, knowledge-intensive services to businesses.

In this type of incubation universities and research institutions where technology and research capacity is available play an increasingly important role,. This process is helped by international projects.

#### **12.2.4 Marketing innovation**

Marketing innovation - as we have seen it before - is a new marketing method, includes product design or packing, product placement or product advertisement or a new way of pricing. Marketing innovation aims effective satisfaction of consumer needs, improving consumer outreach, opening new markets and repositioning the company's product to increase the sale on the market.

The distinguishing feature of marketing innovation is implementation of a marketing method not previously used by the firm.. The new marketing method can either be developed by the innovating firm or adopted from other firms or organizations. New marketing methods can be implemented for both new and existing products.

Marketing innovation could be a brand new product-design, this way it fits to the company's new marketing concept. The new design could show up in the form of new packing (for example by food) or in change of the product planning (for example furniture). New channels for sales, new price strategy, use of new advert concepts are the forms of marketing innovation.

The various implementations of marketing tools, will be discussed in the context of marketing subject.

#### **12.2.5 Organizational innovation**

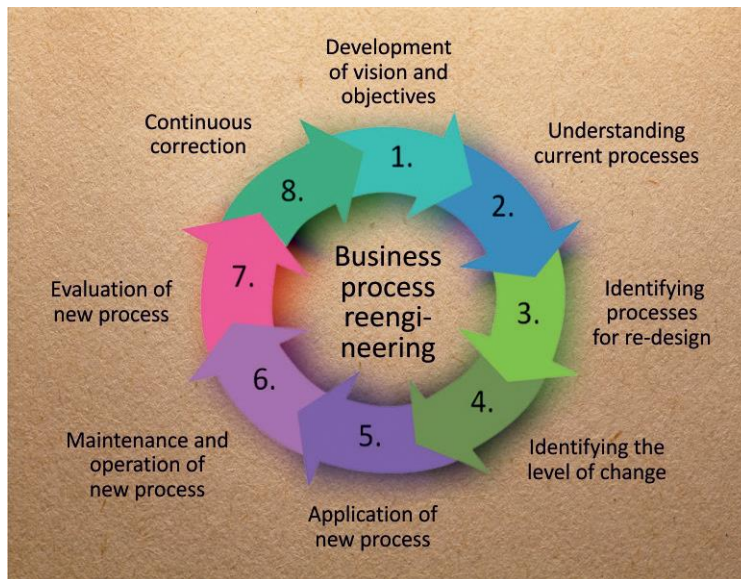
Organizational innovation is a new way of organizing the company's business practices, labor organization or external relations.

Organizational innovations can be intended to increase a firm's performance by reducing administrative costs or transaction costs, improving workplace satisfaction (and thus labour productivity), gaining access to nontrade able assets (such as non-codified external knowledge) or reducing costs of supplies. 151

A form of organizational innovation is reorganization of business processes. (BPR: Business Process Reengineering). The BPR is



fundamental rethinking and radical redesign of business processes in the indicators of performance, such as cost, quality, service and speed.



*Figure 32.*

### 12.2.6 Innovation-management

**Innovation-management** helps with implementation of above mentioned innovations which can be a separate organizational unit of the company or just a part-activity.

📖 **Innovation-management is to lead, organize, direct research and development and other innovation activities from exploring ideas to checking and feed-back of the outcome of the innovation, so it joins and directs necessary resources and knowledge-base necessary to development**

Since change (especially organizational) always evokes a certain resistance of the participants and others involved, so elimination of this resistance is a serious task of innovation-management.

The most frequent forms of organizational opposition are the following:

- Insisting on present (managerial) positions, responsibilities, authorities.
- Mystification of existing market, fear of losing it

- Considering innovation negligible, debasing
- Professional and personal conflicts in its manifestation.

Innovation is very important in the life of enterprises. Staying competitive, preserving market position often is only possible through well thought and implemented innovation strategy. A lot of enterprises survived long years of recession when instead of redundancy and reducing operation they rather chose innovations.

- ✿ Read the following link of TNS research on innovation done during recession:  
[http://www.tnscanada.ca/files/innovation\\_in\\_a\\_recession-8.pdf](http://www.tnscanada.ca/files/innovation_in_a_recession-8.pdf),  
and another link about another research from the united Kingdom:  
[http://i.telegraph.co.uk/telegraph/multimedia/archive/01584/Innovation\\_in\\_Rece\\_1584440a.pdf](http://i.telegraph.co.uk/telegraph/multimedia/archive/01584/Innovation_in_Rece_1584440a.pdf)
- ✿ In the video materials find referencies on how the two enterprises shown utilized innovation in the years of crysis!

## 12.3 SUMMARY, QUESTIONS

### 12.3.1 Summary

**Innovation** is a new, higher quality way than before of satisfying consumer needs. Oslo Manual describes concept of innovation as a new, significantly improved product, service or process, marketing method, new organizational method, labour management or external connections.

**Innovation activity** is any scientific, technological, organizational, financial and commercial action which deliberately or consciously leads to implementation of innovation.

**Product innovation** is introduction of products or services which are new or significantly improved taking character and purpose of utilization. It involves significant renewal of technical features, components and materials, software, customer service or other functional features.

**Process innovation** is application of new or significantly improved production or distribution method. Process innovation involves significant change of technics, appliances or softwares. It results in decreasing unit costs of production or transport, increasing quality, production and distribution of significantly improved goods.

**Marketing innovation** is a new marketing method including considerably new ways of design or packaging, product placement or product advertising or pricing.

**Structural innovation** is a new organisational way of business practice of the firm, recruitment or public relations

According to Booz, Allen and Hamilton product novelty categories are the following:

- New product all over the world
- New product lines
- Completion of existing product lines
- Improvement and altering existing products
- Re-positioned products
- Products of reduced cost

Principles of innovation:

- consumer consciousness
- novelty
- uncertainty
- extent of sustainability

By the **process of product development** the whole of the activities from looking for ideas to launching the products are meant. Its steps are:

2. Searching for new ideas
3. Selection of ideas
4. Product development
5. Product testing
6. Launch to the market

**Technological innovation** is improvement of the efficiency and profitability of economic activity and the whole of scientific, technical, organisational, economic and commercial procedures to achieve favourable social and environmental effects as a result of which new or significantly modified products, procedures, services are created to apply, to launch new or significantly modified procedures including changes which are considered novelty only at that branch or organization.

**Incubation** is to ensure complex services providing possibility for enterprises to implement their innovation plans. The concept of technological incubator is that it provides technology-oriented or knowledge intensive services to enterprises.

**Organizational innovation** is a new organisational way of business practice, recruitment or public relations of a firm

**Business Process Reengineering (BPR)** is basic rethinking and radical reorganisation of corporate processes to achieve dramatic improvement in essential output indicators like cost, quality, service and speed.

**Innovation-management** is to lead, organize, direct research and development and other innovation activities from exploring ideas to checking and feed-back of the outcome of the innovation, so it joins and directs necessary resources and knowledge-base necessary to development

The most frequent forms of **organizational opposition** against changes are the following:

- Mystification of existing market, fear of losing it
- Considering innovation negligible, debasing
- Professional and personal conflicts in its manifestation.
- Insisting on present (managerial) positions, responsibilities, authorities.

### **12.3.2 Self-check questions**

1. What is „innovation“?
2. How can innovation concept be described?
3. What is innovation activity?
4. What is Oslo Manual about?
5. What are the main types of innovation by Oslo Manual?
6. What product novelty categories are distinguished by Booz, Allen and Hamilton?
7. What are the principles of innovation?
8. What is product-innovation?
9. How can process of product development be defined?
10. What are the steps of the process of product development?
11. Where can new product idea come from?
12. What are the aspects of the selection of product ideas?
13. What is product concept?
14. What is prototype? What is the role of prototype?
15. What is test-market?
16. How is a product tested before launching it on the market?
17. What does acceptance of a product depend on?
18. What are the essential elements of technology innovation?

19. What is technology innovation by innovation act?
20. What is incubation and how is it connected to product- and technology development?
21. What is marketing-innovation and what are its types?
22. What is organization innovation?
23. What is BPR?
24. Describe BPR process!
25. What is innovation-management?
26. What causes evoke resistance when launching a new innovation?
27. What is the role of innovation in recession period?

### 12.3.3 Practice tests

1. Match the definition with the right type of innovation!

Type of innovation	Definition
1) product	a) application of new or thoroughly improved production or method of distribution
2) technology	b) a new organizational way of business practice of a company, organisation of labour or public relations
3) marketing	c) launching products or services which are new or thoroughly improved
4) organizational	d) new product design or packaging

(right answers: 1) c), 2) a), 3) d), 4) b)

8. Name the following product novelties. Use precise definitions.

Description of product novelty	Name of product novelty
new products which are first launched to the market by the company	New product lines
new products which replace existing products and they exceed	Improvement and altering existing products

them in output and values attributed to them	
new products which create a completely new market	a new product all over the world
new products which give the same output at lower cost	Products of decreased cost
existing products which are aimed at new markets or market segments	Re-positionated products
new products to accomplish already existing products of the company on the market	Accomplishing existing product lines

Name 4 principles of innovation!

1. ....
2. ....
3. ....
4. ....

(right answer: consumer orientation, novelty, uncertainty, (extent of sustainability))

9. Describe steps of product development!

10. Match product development concept with their definition!

Concept	Definition
1) product concept	a) The possible innovations are assessed from technical and financial feasibility aspects.
2) pilot production	b) A sample product suitable for implementing production and consumer tests.
3) test market	c) The new product must be made suitable for mass production, new technology must be designed or the old one must be altered.
4) selection of ideas	d) The product is introduced on a real (or similar to it), controllable market whose size is known and

	where the product is sold in previously unknown conditions.
5) prototype	e) product design in a drawing or on the computer, description of the target market, standard of the expected output, investment consequences, and financial effects
6) market launch	f) sale of the product on a real market, in normal volume

(right answer: 1) e), 2) c, 3) d), 4) a), 5) b), 6) f))

11. Which of the following statements are true (T) or false (F)?

1. Marketing innovation can be more efficient satisfaction of consumer needs, better address of consumers. (T)

2. A frequent example of organizational innovation is altering corporate processes (organisational routines) which results in decreasing administrative and transaction costs. (T)

3. Categories by Booz, Allen and Hamilton are product-, technology-, marketing and organizational innovation. (F)

4. Principles of innovation are consumer-consciousness, novelty, uncertainty and financibility. (F)

5. **Process of product development** means the whole activity beginning from looking for new ideas to making the prototype. (F)

6. Ideas on new products can originate from external and internal company sources. (T)

7. On the test market the product is tested in real production volume. (H)

8. If a ceramics producer firm switches over from manual production to mechanized one, it is considered product innovation. (F)

9. Incubation is a good solution among others, because a small enterprise does not have to finance setting up and functioning a whole research unit. (T)

10. If a shower bath for children is made attractive for adults in the future, it is considered marketing innovation. (T)

Put steps of BPR process in correct order.

1. permanent correction
2. assessment of the new process
3. application of the new process
4. identification of the level of change
5. identification of processes to be reengineered

6. development of vision and aims
7. operating the new process
8. understanding current processes

(answer:

1. development of vision and aims
2. understanding current processes
3. identification of processes to be reengineered
4. identification of the level of change
5. application of the new process
6. operating the new process
7. evaluation of the new process
8. permanent correction

Out of the factors below choose the ones which most often hinder the launch of an innovation. You have to mark several answers.

1. Decreasing zeal to work.
2. Professional and personal conflicts in realization.
3. Managers' desires of power.
4. Considering innovation insignificant, its evaluation.
5. Mystifying current market, fear of losing it.
6. Resistance of external actors, competitors.
7. State regulations, legal limitations.
8. Insistence on current (leading) positions, responsibilities, authorities.
9. Standard limitations.
10. Quality expectations of consumer.

(answer: 2., 4., 5., 8.)



## 13. SUMMARY

### 13.1 CONTENT SUMMARY

**Enterprises** are established to realize production or service aims with which consumer demand is satisfied. The aim of organizing this activity is to gain profit (except for non-profit enterprises). In the system of economy, enterprises provide products for the consumers, they provide work possibilities, in exchange for the offered labor force they pay a salary. They pay taxes to the state, and make use of subsidies.

The exchange of goods takes place on the **market** where demand and supply meet, and trade is done at the shaped prices. When entering a market, you have to consider several limiting factors. At the start and throughout the operation of the enterprise you have to assess the possible risks, and work out the possible ways of managing them.

During its operation, the enterprise gets into connections with different people and institutions. The interests of **actors of the enterprise** might differ, the enterprise has to recognize these interests, and has to consider them for the sake of efficient operation in its activity.

A significant segment of the economy is the **SME sector**, which plays a significant role in the operation of the economy, but their possibilities are limited due to their smaller size and financial standing. It's the stressed task of the state to help, support this sector.

The **history of corporate enterprises** goes back to the ancient times, though their actual development was characteristic in the Middle Ages. Primarily, they were made to carry out certain state tasks, their first forms were made due to state initiatives, in areas where state role decreased.

The first big corporations (British and Dutch East India Companies) were also made in the field of trade, they had a significant role in colonization. The capital necessary for business was first 'recruited' occasionally. Later the companies gained considerable profit, which was distributed between the investors. In activities organized by towns also the inhabitants could be involved as investors. These corporations can be considered the forerunners of public limited companies. The limited liability companies started in the Netherlands and spread from there.

We separate 3 periods in the development of enterprises in Hungary. Until 1945 the Hungarian sector was shaping similarly the way it did in the world. After the guilds got disintegrated at the end of the 1800s, the Industry and Trade Law enacted the first corporate forms.

After 1946 in the framework of socialist planned economy production was carried out in state companies and co-operatives. In the

1980s inside big companies economic work communities were formed, which can be considered the forerunners of general partnerships.

After the change of the regime, state companies and co-operatives were reorganized to be business corporations.

Currently there are about 1.8 million registered business organizations in Hungary.

Non-profit organizations are catching on. Their characteristic forms are foundations, societies and non-profit business associations

Several environmental factors affect **the shaping of enterprises**, the interaction between social, economic, political welfare and other elements is a determinant factor.

The **establishment of enterprises** can be motivated by internal or external factors, or by the combination of both. At the same time, entrepreneurial willingness significantly differs between the different societies, which can go back to different reasons. In Hungary the motivation to start an enterprise is still low, the significant proportion of the active population still opt for the safe employment salaries. The main motivation to start an enterprise in Hungary is to gain higher income.

**The process of becoming an entrepreneur** is complex, it lasts from the idea arising to the operation of the enterprise. The idea arisen is followed by the start of the enterprise, finally the entrepreneur's continuous task is to run it.

We can **group enterprises** in several ways. According to one method, we can examine companies by two dimensions: one is business experience, the other dimension is entrepreneurial willingness which means the adaptation to the changing environmental conditions. Based on this we differentiate four basic types: ants, gazelles, tigers and dinosaurs.

**Success** means the achievement of aims. Success is hard to word objectively, but you can determine the basic factors which are indispensable for every enterprise for success. We know of different levels of achieving success, which can be realized built upon each other. We learnt a few characteristic indicators to size up success.

At the start of the enterprise following the idea emerged the would-be entrepreneurs have to consider several factors. Based on the abilities and plans, they have to decide whether to start the activity as a **private enterprise**, alone, or as an **individual company**, or together with others as a **corporate enterprise**. The particular enterprising forms differ in the way of establishing, in the measure of necessary basic capital and of responsibility to be taken, and in the form of taxation.

During their operation companies go through different **life cycles**. To describe company life cycles several theories were born, we learnt

about the model of Timmons, László Szerb, Adizes and Greiner, and the features of the particular stages. We examined what financing forms, possibilities characterize the particular life cycle stages.

Enterprises may differ a lot, concerning their activity, size, organization. Yet, there are **functions** which can be found at most companies, because their aims are identical, and these are:

- satisfying consumer demands
- gaining profit, increasing wealth
- lasting sustainability (except for project companies)
- growth, development
- producing, selling, developing products
- real risk taking
- efficient relationship with the internal and external environment
- realizing social mission
- continuous liquidity

**Basic activities** that can be found at most companies:

1. Production and/or service
2. Purchase, sale, logistics
3. Company finances
4. Marketing
5. Human resources management
6. Innovation
7. Management and information system

The character, weight and combination of activities might differ with each enterprise, but the particular activities appear in some form in the structure.

For its operation, or for some other purposes, the enterprise makes its plan for the coming period. The main steps of **strategic planning** are:

1. Analysis of external and internal environment
2. Selection of business areas
3. Drawing up mission and vision
4. Shaping strategic aims

5. Determining means and methods of realizing aims

**Planning** can be interpreted at strategic, tactical and operative **level**.

The **business plan** is deduced from the strategic plan. The **purpose** of making it is:

1. Introducing the activity to owners, creditors, preparation for investment decisions, convincing new investors (banks, tendering organizations, etc.)
2. Realizing new ideas, innovations, innovations with great risk factor, modeling expectable result
3. Continuously monitoring business results, expectable development
4. Plan made for business partners, strategic alliances
5. Establishing company risk management, controlling activity

The characteristic parts of the business plan are:

1. Introduction
2. Management summary
3. Introduction of enterprise
4. Introduction of environment, features of industry branch
5. Marketing plan
6. Operation, running plan
7. Organizational plan
8. Risk assessment
9. Financial, financing plan
10. Appendices

**Management** is an activity which sets the goals of the organization, determines the means necessary to achieve these goals, starts, controls and co-ordinates the activities necessary to achieve the goals.

The management process, as **problem solving** consists of the following steps: problem discovery, setting aims, problem analysis, decision preparation and decision, execution, supervision, feedback.

**Managers** have to fill in different **roles** in connection with their activity, they are: interpersonal roles, information roles, decision roles.

The basic **functions of managing** are planning, organizing, direct control, co-ordination and communication, supervision.

Success to a significant extent depends on the employees, besides the company management. That's why human resources management is an extremely important company part area.

Human capital is complex value based on the abilities and knowledge of the members of the organization, and consists of their work and life experience, and motivation.

The company's **human resources management** is aimed at determining the demand for human resources of the necessary quantity and quality to achieve organizational aims, at finding, selecting, „obtaining” the necessary resources, cares about their efficient use, development and in case it's necessary, about their dismissal. Together with this it co-ordinates the aims, requirements of the company and of the employees, and considers them when making decisions.

The main aim of human resources management is to **improve organizational performance: success and efficiency.**

**Human resources planning** is a complex, cyclic planning process the steps of which are (analysis, considering current situation and future developments in it) setting aims and action planning.

The **sphere of activity** is the smallest identifiable unit of the organization, which has an aim, dynamics and with an employee who is responsible for it.

The **job analysis** provides information about the main points of the sphere of activity, the activities to be done, authority rules, demands to be met by the employee filling in the job.

We call **atypical employment** the ones which are different from the unlimited term, traditionally used employment in a work relationship with a contract. Its main types are teleworking, part-time employment, fixed-term or project employment, work force leasing, work done not in work relationship (assignment), outworking, self-employment, occasional employment (simplified employment), transit and fixed term employment with (state) support, student work and public work.

The **incentive system** is the complex of those rules, procedures and methods on the basis of which the organization realizes the concrete incentives, payments and allowances of the employees. Besides the basic salary (which can be payment by result or payment by time) the management can use several incentive methods of wage or non-wage character to motivate workers.

Besides motivating workers, the other way of preserving and improving the competitive position is innovation.

**Innovation** is the new of satisfying consumer demand at a higher quality level. In the Oslo Manual the notion of innovation is interpreted as new, or significantly improved product or service, or process, marketing method, new organizational method, labor force organization or external connections.

**Innovation activity** is every scientific, technological, organizational, financial or commercial step, which consciously or intentionally leads to executing innovation. The main types of innovation are product innovation, process (technological) innovation, marketing innovation and organizational innovation.

**Innovation management** leads, organizes, controls R&D and other company innovation activities, from the discovery of ideas to measuring the results of innovation, and to feedback, and for the sake of this it coordinates and controls the necessary resources and the knowledge base necessary for development.

In its complexity we can examine any part areas of the company, but we have to state that running the company is a complex task which needs the special knowledge to achieve success.

### **13.2 CLOSURE**

With this we have arrived at the end of Business Economics I. I hope that learning the material didn't cause any difficulties to you. Please, review the given professional literature, check your knowledge with the help of the practice tests, and find practical examples based on the entries of the particular units on the Internet. I wish you a successful exam!

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### 14.2.3 Glossarium

1. **Atypical employment:** employment different from traditional full employment of unlimited period.
2. **Decision making:** Choice between solutions, actions.
3. **Business association:** Business associations are collections of individuals to perform common economic business activity, created by asset contribution of the members, they are considered legal entities where members mutually share profit and bear loss. Members get their share of profit according to their contribution and bear loss also in this proportion. Business associations can be established as general partnerships, limited partnerships, limited liability companies, or joint stock companies.
4. **Human resources:** the whole of the employees employed by a company structured by their skills, abilities, professional knowledge and place occupied in the division of labor.
5. **Human resources management:** determines the need for the right quantity and quality human resources necessary to achieve corporate purposes, recruits, chooses, „obtains“, makes sure of their efficient employment, development, if necessary, of their dismissal. At the same time it coordinates aims, needs of the organization and the employees and they are mutually considered when making decisions. Human resources management is a strategy with which key resources of the organization, people working at and for the organization are obtained, developed, directed, motivated and made loyal.
6. **Planning human resources** is a complex cycle planning process the steps of which are assessment (of present situation, assuming future development and difference evaluation), setting objectives and action planning.
7. **Human capital:** collective value combined from skills and knowledge, work and life experience and motivation of corporate members.
8. **Sales:** it connects company with consumers, by this products produced by the company are delivered to the consumers, it arranges necessary transport, packaging, payment and information tasks.
9. **Process innovation:** It means application of new or significantly improved production or distribution methods. It includes significant change of

technology, equipment, or software. It results in decreasing production or transport unit costs, increasing quality, producing and distributing new or significantly improved products.

10. **Information:** data providing new knowledge to the company and influencing entrepreneur's decision.
11. **Information system:** information system is a whole of all the persons, activities and technical appliances devoted to processing (capturing, transmitting, storing, retrieving, manipulating and displaying) information related to the environment, internal operation and transaction between the company and its environs.
12. **Incubation:** providing complex services which makes it possible for enterprises to fulfill their innovation plans. This way businesses do not have to create costly and expensive development infrastructure and organization which clears their costs slowly, but „rent” it. This way lower investment makes smaller, lower-capitalized ventures possible to improve their chances for survival and stabilize their market position.
13. **Innovation** is a new, higher quality way than before of satisfying consumer needs. The Oslo Manual describes concept of innovation as a new, significantly improved product, service or process, marketing method, new organizational method, labor management or external connections.
14. **Innovation-management** is to lead, organize, direct research and development and other innovation activities from exploring ideas to checking and feed-back on the outcome of the innovation, so it joins and directs necessary resources and knowledge-base necessary to development
15. **Innovation activity** is any scientific, technological, organizational, financial and commercial action which deliberately or consciously leads to implementation of innovation.
16. **Forced enterprise:** those organizations that set up a business because they did not have possibility to work as employees (unemployed), so the founders wish to make their living as entrepreneurs.
17. **Stock:** The stock of available products at a company at a given time. Since consumers have demands on a certain product independent of the place and time of production, the demands must be satisfied by proper stocks.

18. **Communication:** is a two-sided process when two or more people exchange and interpret information with a certain aim.
19. **Logistics:** A corporate activity, that grants products to be available in the right place, time, quantity and quality in the business processes.
20. **Marketing innovation** is a new marketing method including considerably new ways of design or packaging, product placement or product advertising or pricing.
21. **Management:** field of human resources of a company which makes various levels of decisions (strategic, tactical, operative), plans resources necessary for operating the company, organizes and directs company processes and coordinates work of the participants.
22. **Mission (message):** it expresses objectives of the organization, its relations to the world and what values is the company operated by.
23. **Motivation** includes all the internal factors which make us act, behave in a certain way. In this case we are looking for the motives which trigger people to set up their own business.
24. **Job title:** the smallest identifiable unit of the organization which has aim, dynamics, and individual responsibility by the person fulfilling it.
25. **Job assessment:** provides information about the job, activities to be done, rules of responsibility, authority, demands towards the person.
26. **Market:** is a system of real and potential sellers and buyers and their exchange connections, the major factors of which are demand, supply, price and income.
27. **Problem solving:** a creative process aimed at finding the way of using an opportunity or eliminating an unsuitable situation, tension.
28. **Strategic actions:** special tasks derived from strategic purposes. The project is a package of tasks usually for several years based on strategic actions, to which a schedule, a responsible person and need for resources are assigned.
29. **Creating strategy:** it includes choosing business area or areas, wording message and vision, setting strategic purposes, deciding on tools and methods to implement strategy.

30. **Strategic planning:** we speak of strategic if it is implemented in a regulated planned process.
31. **Organizational innovation** is a new organizational way of business practice of the firm, recruitment or public relations
32. **Organization:** an activity aimed at fulfilling pre-determined objectives by coordinating (optimum combination) human and material resources of the organization.
33. **Technological incubator:** provide technology-oriented or knowledge intensive services to enterprises.
34. **Technological innovation** is improvement of the efficiency and profitability of economic activity and the whole of scientific, technical, organizational, economic and commercial procedures to achieve favorable social and environmental effects as a result of which new or significantly modified products, procedures, services are created to apply, to launch new or significantly modified procedures including changes which are considered novelty only at that branch or organization.
35. **Process of product development:** all the activities from searching for new ideas to launching the product on the market.
36. **Product innovation** is introduction of products or services which are new or significantly improved considering character and purpose of utilization. It involves significant renewal of technical features, components and materials, software, customer service or other functional features
37. **Production supply:** management of stocks between the various production phases and stocks flowing during production.
38. **Business Process Reengineering (BPR)** is basic rethinking and radical reorganization of corporate processes to achieve dramatic improvement in essential output indicators like cost, quality, service and speed.
39. **Business plan:** an action plan generally for several years based on strategic actions and projects.
40. **Business entity:** Human activity whose basic objective, meaning of its existence is to meet consumers' demands in order to earn profit.

41. **Company:** Organizational frame of a business entity, a structure legally defined in modern societies in which activities to achieve basic target are performed. Business ventures are „production” units of an economy. They provide resources to production (e.g. machines, property, labor force, capital, etc.) with the help of which products, services are produced.
  
42. **Group of companies:** A co-operation having minimum one leading member and minimum three members controlled by the leading member. The group is obliged to perform a combined, consolidated annual report, their work is based on unified business policy defined in agreement. Public limited companies, limited liability companies, associations and co-operatives can be members of groups of companies.
  
43. **Leadership** is direct influence on employees. It is an activity where objectives are determined, and also the ways and methods, necessary to approach them, it also starts, directs and co-ordinates activities necessary to achieve them.
  
44. **Vision:** conditions to be achieved in the later future (5-10 years) by fulfilling shorter term strategies.