TOPIC 1: FORMS OF BUSINESS UNITS

TOPIC OBJECTIVES

BUSINESS UNITS

A business unit is an organization formed by one or more people with a view of engaging in a profitable activity.

Business units are generally classified into private or public sector business units' i.e

N*ote:* Private sector comprises of business organizations owned by private individuals while the public sector comprises business organizations owned by the government.

- ***SOLE PROPRIETORSHIP***

This is a business enterprise owned by one person who is called ***a sole trader or a sole proprietor.*** It is the most common form of business unit and usually found in retail trade e.g. in small shops, kiosks, agriculture e.t.c and for direct services e.g. cobblers saloons e.t.c

Characteristics/Features

- The business is owned by one person
- The capital is contributed by the owner and is usually small. The main source is from his savings and other sources can be from friends, bank or getting an inheritance
- The owner enjoys all the profits alone and also suffers the losses alone
- The owner is personally responsible for the management of the business and sometimes he is assisted by members of his family or a few employees. He remains responsible for the success or failure of his/her business.
- The sole proprietor has unlimited liability meaning that incase of failure to meet debts, his creditor can claim his personal property
- There are very few legal requirements to start the business unit.
- Sole proprietorship is flexible; it is very easy to change the location or the nature of business.

Formation

The formation of a sole proprietorship is very simple. Few legal formalities are required i.e. to start a sole proprietorship, one need only to raise the capital required and then apply for a trading license to operate the business small fee is paid and the trade license issued.

Sources of capital

The amount of capital required to start a sole proprietorship is small compared to other forms of business organizations. The main source of capital is the ***Owners savings.*** Additional capital may however be raised from the following;

- Borrowing from friends, banks and other money lending institutions such as industries and commercial Development corporation(ICDC)and Kenya industrial estates
- Inheritance
- Personal savings
- Getting goods on credit
- Getting goods on hire purchase
- Leasing or renting out one's properties
- Donations from friends and relatives
- Ploughing back profit.

Management

The management of this kind of a business is under one person. The owner may however employ other people or get assistance from family members to run the business.

Some sole proprietorship may be big business organizations with several departments and quite a number of employees. However, the sole proprietor remains solely responsible for the success of failure of the business

Advantages of sole proprietorship

- The capital required to start the business is small hence anybody who can spare small amounts of money can start one.
- Few formal/legal procedures are required to set up this business
- Decision making and implementation is fast because the proprietor does not have to consult anybody
- The trader has close and personal contact with customers. This helps them in knowing exactly what the customers need and hence satisfying those needs
- A sole proprietor is able to assess the credit-worthiness of his or her customers because of close personal relationship. Extending credit to a few carefully selected customers reduce the probability of bad debts.
- The trader is accountable to him/herself
- A sole trader is able to keep the top secrets of the business operations
- He/she enjoys all the profit

- A sole proprietorship is flexible. One can change the nature or even the location of business as need arises.

Disadvantages of sole proprietorship

- Has unlimited liability. This means that if the assets available in the business are not enough to pay all the business debts the personal property of the owner such as house will be sold to meet the debts
- There is insufficient capital for expansion because of scarce resources and lack of access to other sources
- He/she is overworked and has no time for recreation.
- There is lack of continuity in the sole proprietorship i.e the business is affected by sickness or death of the owner.
- A sole proprietorship may not benefit from advantages realized by large scale enterprises (economies of large scale) such as access to loan facilities and large trade discounts.
- Lack of specialization in the running of the business may lead to poor performance. This is because one person cannot manage all aspects of the business effectively. One maybe a good salesman for examples but a poor accountant.
- Due to the size of the business, sole proprietorships do not attract and retain highly qualified and trained personnel.

Dissolution of sole proprietorships

Dissolution refers to the termination of the legal life of a business. The following circumstances may lead to the dissolution of a sole proprietorship:

- Death or insanity of the owner.
- Transfer of the business to another person- this transfers the rights and obligations of the business to the new owner.
- Bankruptcy of the owner- this means that the owner lacks the financial capability to run the business.
- The owner voluntarily decides to dissolve the business e.g due to continued loss making.
- Passing of a law which renders the activities of the business illegal.
- The expiry of the period during which the business was meant to operate

PARTNERSHIP:

This is a relationship between persons who engage in a business with an aim of making profits/ an association of two or more persons who run a business as ***co-owners***. The owners are called ***Partners.***

It is owned by a minimum of 2 and a maximum of 20 except for partnership who provide professional services e.g medicine and law which have a maximum of 50 persons.

Characteristics of partnership

- Capital is contributed by the partners themselves.
- Partnership has limited life that is it may end anytime because of the death, bankruptcy or withdrawal of partners.
- Each partner acts as an agent of the firm with authority to enter into contracts.
- Partners are co owners of a business, having an interest or claim in the business.
- Responsibility, profit and losses are shared on an agreed basis.
- All partners have equal right to participate in the management of the business. This right arises from the interest or claim of the partner as a co owner of the business.

*Types of partner*ship

Partnerships can be classified/ categorized in either of the following ways:

- According to the type/liability of partners
- According to the period of operation
- According to their activities.

According to the type or liability of partners

Under this classification, partnerships can either be;

- ***General/ordinary partnership-*** Here all members have unlimited liability which means in case a partnership is unable to pay its debts, the personal properties of the partner will be sold off to pay the debts.
- ***Limited partnerships-*** In limited partnership members have limited liabilities where liability or responsibility is restricted to the capital contributed.

This means that incase the partnership cannot pay its debts; the partners only lose the amount of capital each has contributed to the business and not their personal property. However, there must be one partner whose liabilities are unlimited.

- **According to the period/duration of operation**

  When partnerships are classified according to duration of operation, they can either be;

- **Temporary partnership-**These are partnerships that are formed to carry out a specific task for a specific time after which the business automatically dissolves.
- **Permanent partnerships-** These are partnerships formed to operate indefinitely. They are also called a partnership at will.

- **According to their Activity-** Under this mode of classification, partnerships can either be:

- **Trading partnerships**

  This is a partnership whose main activity is processing, manufacturing, construction or purchase and sale of goods.

- **Non – trading partnerships**

  This is a partnership whose main activity is to offer services such as legal, medical or accounting services to members of the public.

Types of partners

Partners may be classified according to;

Role played by the partners

- ***Active partner;*** He is also known as acting partner as he plays an active part in the day-to-day running of the business.

- ***Sleeping/dormant partner;*** He does not participate in the management of the partnership business. Although he invests his capital in the partnership, his profit is lower as he is not active. He is also referred to as passive or silent partner.

Liabilities of the partners for the business debts;

- ***General partner;*** He/she has unlimited liabilities.

- ***Limited partner;*** He/she has limited liabilities

Ages of partners

- ***Major partner;*** This is a partner who is 18 years and above. He is responsible for all debts of the business.

- ***Minor partner;*** This is a partner who has not attained the age of 18 years but has been admitted with the consent of other partners. Once he reaches 18 years, he then decides if he wants to be a partner or not. Before he attains the age of 18, he takes part in the sharing of profits but does not take part in the management of the business.

iv) Capital contribution

- ***Nominal/Quasi partner;*** He does not contribute capital but allows the business to use his/ her name as a partner; for the purpose of influencing customers or for prestige.

-He/she can also be a person who was once a partner and has retired in form of a loan. This loan carries interest at an agreed rate.

-The quasi partner shares the profit of the business as a reward for using his/her name.

b) Real partner; He/she is one who contributes capital to the business.

-Other types of partners include secret partners, retiring partners and incoming partners

i) A secret partner; is one who actively participates in the management of the firm but is not disclosed to the public. In most cases secret partners are also limited partners.

ii) A retiring partner; Also known as outgoing partner is one who is leaving a partnership

-He may retire with the consent of all the other partners or according to a previous agreement.

iii) Incoming partner; Is one who is admitted to an existing partnership.

Formation

-People who want to form a partnership must come together and agree on how the proposed business will be run to avoid future misunderstanding.

-The agreement can either be oral (by use of mouth) or within down. A written agreement is called a ***partnership deed.***

-The contents of the partnership deed vary from one partnership to another depending on the nature of the business, but generally it contains;

- Name, location and address of the business
- Name, address and occupation of the partners
- The purpose of the business
- Capital to be contributed by cash partner
- Rate of interest on capital
- Drawings by partners and rate of interest on drawings
- Salaries and commissions to partners
- Rate of interests on loans from partners to the business
- Procedures of dissolving the partnership
- Profit and loss sharing ratio
- How to admit a new partner
- What to do when a partner retires dies or is expelled
- The rights to inspect books of accounts
- Who has the authority to act on behalf of other partners.

Once the partnership deed is ready, the business may be registered with the registrar of firms on payment of a registration fee.

In case a partnership deed is not drawn, the provisions of partnership act of 1963 (Kenya) applies. The act contains the following rights and duties of a partner;

- All partners are entitled to equal contribution of capital
- No salary is to be allowed to any partner
- No interest is to be allowed on capital
- No interest is to be charged on drawings
- All profits and losses are to be shared equally
- Every partner has the right to inspect the books of accounts
- Every partner has the right to take part in decision making
- Interest is to paid on any loans borrowed by partners (The % rate varies from one country to another)
- During dissolution the debts from outside people are paid first then loans from partners and lastly partners capital.
- No partner should carry out a competing business
- Any change in business such as admission of new partners must be through the agreement of all existing partners.
- Compensation must be given to a partner who incurs any loss when executing the duties of the business.

Sources of capital

- Partners contribution
- Loans from banks and other financial institutions
- Getting items on hire purchase
- Trade credit
- Ploughing back profit
- Leasing and renting.

Advantages of partnership

- Unlike sole proprietorship, partnership can raise more capital.
- Work is distributed among the partners. This reduces the workload for each partner
- Varied professional/skilled labour; various partners are professionals in various different areas leading to specialization
- They can undertake any form of business agreed upon by all the partners

- There are few legal requirements in the formation of a partnership compared to a limited liability company.
- Losses and liabilities are shared among partners
- Continuity of business is not affected by death or absence of a partner as would be in the case of a sole proprietorship
- Members of partnership enjoy more free days and are flexible than owners of a company
- A Partnership just like sole proprietorship is exempted from payment of certain taxes paid by large business organizations.

Disadvantages of partnership

- A mistake made by one of the partners may result in losses which are shared by all the partners
- Continued disagreement among the partners can lead to termination of the partnership
- Decision-making is slow since all the partners must agree
- A partnership that relies heavily on one partner may be adversely affected on retirement or death of the partner
- A hard working partner may not be rewarded in proportion to his/her effort because the profits are shared among all the partners
- There is sharing of profits by the partners hence less is received by each partner
- Few sources of capital, due to uncertainty in the continuity of the business few financial institutions will be willing to give long-term loans to the firm.

Dissolution of partnership

A partnership may be dissolved under any of the following circumstances:

- A mutual agreement by all the partners to dissolve the business
- Death insanity or bankrupting of a partner
- A temporary partnership on completion of the intended purpose or at the end of the agreed time.
- A court order to dissolve the partnership
- Written request for dissolution by a partner
- If the business engages in unlawful practices
- Retirement or admission of a new partner may lead to a permanent or temporary dissolution
- Continued disagreements among the partners

INCORPORATED FORMS OF BUSINESS UNITS

These are businesses that have separate legal entities from that of their owners. They include:

CO-OPERATIVES

-A co-operative society is a form of business organization that is owned by and run for the economic welfare of its members

-It is a body of persons who have joined together to do collectively what they were previously doing individually for mutual benefit.

Example

In Kenya the co-operative movement was started by white settlers in 1908 to market their agricultural produce. In this case, they knew that they could sell their produce better if they were as a group and not alone

Principles of co-operatives

- ***Open and voluntary membership***

  Membership is open and voluntary to any person who has attained the age of 18 years. No one should be denied membership due to social, political, tribal or religious differences. A member is also free to leave the society at will

- ***Democratic Administration***

The principle is one man one vote. Each member of the co-operative has only one vote irrespective of the number of shares held by him or how much he buys or sells to the society

- ***Dividend or repayment***

-Any profit/surplus made at the end of every financial year should be distributed to the members in relations to their contribution.

-Part of the profit may be retained/reserved/put in to strengthen the financial position of the society.

- ***Limited interest on share capital***

-A little or no interest is paid on share capital contributed (co-operatives do not encourage financial investment habits but to enhance production, to encourage savings and serve the members)

- ***Promotion of Education***

Co-operative societies should endeavor to educate their members and staff on the ideas of the society in order to enhance/improve quality of decisions made by the concerned parties.

Education is conducted through seminars, study tours, open days

- ***Co-operation with other co-operatives***

C-operatives must learn from each others experience since they have a lot in common.

-Their co-operation should be extended to local national and international.

Features of co-operatives

- Membership is open to all persons so long as they have a common interest. Members are also free to discontinue their membership when they desire so
- Co-operative societies have a perpetual existence; death, bankruptcy or retirement of a member does not affect its operations
- They are managed in a democratic manner. Every member has one vote when electing the managerial committee irrespective of the number of shares held.
- The main aim is to serve the interest of the members where profit is not the over riding factor.
- Co-operative societies have limited liabilities
- There must be a minimum of 10 people with no maximum membership.
- Co-operatives have a separate legal entity from the members who formed it i.e they can own property sue and be sued

- Any profit made by the society is distributed to the members on the basis of the services rendered by each member but not according to the capital contributed.

Formation

-Co-operative societies can be formed by people who are over eighteen years regardless of their economic, political or social background.

-There must be a minimum of 10 persons and no maximum no.

-The members draft rules and regulations to govern the operations of the proposed society i.e. by-laws, which are then submitted to the commissioner of co-operatives for approval

-The registrar then approves the by-laws and issues a certificate of registration

-If the members are unable to draw up their own by-laws, the co-operative societies Act of 1966 can be adopted in part or whole

M*anagement*

-A co-perative society is composed/run by a committee usually of nine members elected by the members in a general meeting

-The management committee elects the chairman, secretary and treasurer as the executive committee members, who act on behalf of all the members and can enter into contracts borrow money institute and depend suits and other legal proceedings for the society

-The committee members can be voted out in an A.G.M if they don't perform as expected.

TYPES OF CO-OPERATIVES SOCIETIES IN KENYA

May be grouped according to;

Nature of their activities

- Producer co-operatives
- Consumer co-operatives
- Savings and credit co-operatives

Level of operations

- Primary co-operatives
- Secondary co-operatives

Producer co-operatives

This is an association of producers who have come together to improve the production and marketing of their products.

Functions

- Obtaining better prices for their members products
- Providing better storage facilities for their products
- Providing better and reliable transport means for moving the products from the sources to the market and building feeder roads
- Providing loans to members
- Providing services of grading, packing and processing to the members
- Providing farm inputs e.g. fertilizers, seeds, insecticides e.t.c on credit to members
- Educating and advising members on better methods of farming through seminars, field trips, films and demonstration

-In this type of co-operative members are paid according to the quantity of the produce a member has delivered to the society.

Examples,

KCC-Kenya Co-operative Creameries

K.P.C.U-Kenya Planters Co-operatives Union

K.G.G.C.U-Kenya Grain Growers Co-operative Union

- ***Consumer Co-operatives***

-These are formed by a group of consumers to buy goods on wholesome and sell them to the members at existing market prices.

-Their aim is to eliminate the wholesalers and retailers and hence obtain goods more cheaply

-The co-operatives allow their members to buy goods on credit or in cash

-Members of the public are also allowed to buy from the society at normal prices thereby enabling the society to make more profits

-The profits realized is shared among the members in proportion to their purchases i.ethe more a member buys, the buyer his/her share of profit

*Examples;***-**Nairobi consumer co-operative union, Bee-hive consumer co-operative society *and* City-chicken consumer co-operative society

Advantages

- Sell goods of high quality
- Sell goods to members at fair prices
- Sell goods to other people at normal prices thereby making more profit

- Buy goods directly from the producers thereby eliminating middlemen. They are therefore able to make more profit
- Can give credit facilities to the members
- Can pay interest on capital to the members
- Sell a variety of goods to the members at a place where they can easily get them

Disadvantages

Consumer co-operatives are not popular in Kenya because of the following

- They face stiff competition from large scale retailers such as supermarkets and multiple shops who buy goods directly from the producers and sell-them to consumers at low prices
- Cannot offer to employ qualified staff
- Majority of their members have low income, so raising off capital is a problem
- Kenya, being an agricultural country, produces enough subsistence goods for itself. It therefore does not require consumer co-operatives
- Reluctance of non-members to buy from the shops lowers the turn-over
- Mismanagement of the shops is rampant

Savings and credit co-operatives societies (SACCO'S)

-They are usually formed by employed persons who save part of their monthly salary with their co-operative society, through check-off system

-Their money earns goods interest and when one has a significant amount saved, he/she become entitled to borrow money from the society for any personal project e.g. improving their farms, constructing houses, paying school fees e.t.c

-The SACCOS charge lower interest on loans given to members than ordinary banks and other financial institutions.

-The societies have few formalities or requirements to be completed before giving a loan. These are:

- *Membership*
- *Members salary*
- *Members saving*
- *Guarantee from fellow members*

-Profits earned by the SACCO'S maybe shared among the members inform of dividends.

-Most SACCO'S have insured their members savings and loans with co-operative insurance services (CIS).This means if a member dies his/her beneficiaries are not called upon to repay the loan and the members savings/shares is given to the beneficiaries.

-They are the main institutions that provide loans to most people who do not qualify for loans from commercial banks because they do not ask for securities such as title deeds required by the bank.

d) Primary co-operative societies

-These are co-operative societies composed of individuals who are either actual producers, consumers or people who join up together to save and obtain credit most conveniently

-Consumer co-operative societies and most SACCO'S are primary co-operative societies because they are composed of individuals.

-Most primary co-operative societies operate at the village level, others at district levels and a few at national levels.

e) Secondary co-operative societies

-They are usually referred to as unions

-They are generally composed of primary co-operative societies as their members

-They are either found at district levels or at national levels.

Advantages of co-operative societies;

- Since the properties of co-operatives are owned collectively, they are able to serve the interest of the members affectively
- They have limited liability
- Membership is free and voluntary
- Members share profits of a co-operative through dividend that are given
- They have improved the standards of living of their members through increased income from their produce and through savings from incomes.
- Co-operatives benefit their members through giving them credit facilities and financial loans which they could not have got from local banks
- They are run on a democratic basis i.e. all members have an equal chance of being elected to the management committee.
- Many co-operatives are large scale organizations hence able to get the benefits of large scale organizations e.g low production costs leading to low prices of products
- Co-operative enjoy a lot of support from the government and when they are in financial and managerial problems, the government steps in to assist them

Disadvantages

- Majority of the co-operatives are small in size and therefore cannot benefit from economies of scale.
- Members have a right to withdraw from the society and when they do, co-operatives refunds the capital back which might create financial problems to the society.
- Corruption and embezzlement of funds is a problem for many co-operatives.
- Most co-operatives are not able to attract qualified managerial staff hence leading to mismanagement.
- Many suffer from political interference. Sometimes; the election of the management committee is interceded with by some people with personal interest in certain candidates hence the best person may not be elected to run the affairs of the society. This leads to poor management and inefficiency.
- Members may not take keen interest in the affairs of a co-operative society because their capital contribution is small.

Dissolution of co-operative societies

-A co-operative society may be dissolved under any of the following circumstances.

- Order from commissioner of co-operatives
- Voluntary dissolution by members
- Withdrawal of members from the society leaving less than ten members
- If the society is declared bankrupt

LIMITED LIABILITY COMPANIES (JOINT STOCK COMPANIES)

Defn: A company; Is an association of persons registered under the companies act who contribute capital in order to carry out business with a view of making a profit. The act of registering a company is referred to as **incorporation. Incorporation** creates an organization that is separate and distinct from the person forming it.

-A company is a legal entity that has the status of an ‘’**artificial person”.** It therefore has most of the rights and obligations of a human being. A company can therefore do the following;

- Own property
- Enter into contracts in its own name.
- Borrow money.

- Hire and fire employees.
- Sue and be sued on its own right.
- Form subordinate agencies, ie, agencies under its authority.
- Disseminate or spread information.

-The owners (members) of a company are referred to as shareholders

FEATURES OF COMPANIES (LIMITED LIABILITY COMPANIES)

-A company in an artificial person and has the same rights as a natural person. It can therefore sue and be sued in a court of law, own property and enter into contracts in its own name.

-The members have limited liabilities.

-Companies have perpetual life which is independent of the lives of its owners. Death, insanity or bankruptcy of a member does not affect the existence of the company. (this is referred to as **perpetual existence or perpetual succession)**

- A company is created for a particular purpose or purposes.

Formation

-People who wish to form company are referred to as ***promoters***

-The promoters submit the following documents to the registrar of companies:

Memorandum of Association

-This is a document that defines the relationship between the company and the outsiders. It contains the following:

a) ***Name of the company/Name clause;*** -The name of the company must be started and should end with the word "*Limited" (Ltd).*This indicates that the liability of the company is limited.

-Some companies end their names with ***"PLC"*** which stands for "***Public limited company"*** which makes the public aware that although it is a limited liability company it is a public not private.

b) ***The objects of the company/objective clause***;-This set out the activities that the company should engage in

-The activities listed in this clause serve as a warning to outsiders that the company is authorized in these activities only.

c) ***Situation clause;***-Every company must have a registered office where official notices and other communication can be received and sent

d) ***Capital clause;***-It also states that the amount of capital which the business can raise and the divisions of this capital into units of equal value called shares i.e. authorized share capital also called registered or nominal share capital.

-It also specifies the types of shares and the value of each share

e) ***Declaration clause:***-This is a declaration signed by the promoters stating that they wish to form the company and undertake to buy shares in the proposed firm

-The declaration is signed by a minimum of seven promoters for public limited company and a minimum of two for private company.

-The memorandum of association also contains the names of the promoters

-The promoters signs against the memorandum showing details of their names, addresses, occupation and shares they intend to buy. Each signatory should agree to take at least one share.

- ***Articles of Association***

-This is a document that governs the internal operations of the company

-It also contains rules and regulations affecting the shareholders in relation to the company and in relation to the shareholders themselves.

-It contains the following;

- Rights of each type of shareholder e.g. voting rights
- Methods of calling meeting and procedures
- Rules governing election of officials such as chairman of the company, directors and auditors
- Rules regarding preparation and auditing of accounts
- Powers, duties and rights of directors
- Methods dealing with any alterations on the capital.

- A list of directors with details of their names, addresses, occupations, shares subscribed and statements of agreement to serve as directors.
- Declaration that registration requirements as laid down by law (by the companies act) have been met. The declaration must be signed by the secretary or a director or a lawyer.
- A statement signed by the directors stating that they have agreed to act as directors.
- A statement of share capital- this statement gives the amount of capital that the company wishes to raise and its subdivision into shares.

-Once the above documents are ready, they are submitted by the promoters to the registrar of companies. On approval by the Registrar and on payment of a registration fee, a certificate of incorporation (certificate of registration) is issued

-The certificate of incorporation gives the company a separate legal entity.

Sources of capital

- ***Shares;*** The main source of capital for any company is the sale of shares.

  -A share is a unit of capital in a company e.g. if a company states that its capital is ksh.100,000 divided into equal shares of ksh.10 each.

  -Each shareholder is entitled to the company's profit proportionate to the number of shares he/she holds in the company.

Types of shares;

- Ordinary shares
- Preference shares

Ordinary shares;-Ordinary shares have the following rights:

- Have voting rights
- Have no fixed rate of dividends. The dividends on them vary according to the amounts of profit made
- They have a claim to dividends after the preference shares
- If the company is being liquidated, they are paid last after the preference shares

Preference shares;-They have the following characteristics;

- Have a fixed rate of sharing profits(dividends)
- Have a prior claim to dividends over the ordinary shares
- Have no voting rights
- Can be redeemable or irredeemable. Redeemable shares are the ones that can be bought back by the company at a future date while irredeemable ones are ones that cannot be bought back
- Can be cumulative or non-cumulative. Cumulative shares are the ones that are entitled to dividends whether the company makes profit or not. This means if the company makes a loss or a profit which is not enough for dividends in a certain year, the dividends to cumulative shares are carried forward to the next year(s) when enough profit are made

-Non- cumulative shares are the ones whose dividends are not carried forward to the following year(s)

- ***Debentures***

This refers to loans from the public to a company or an acknowledgement of a debt by a company

They carry fixed rate of interest which is payable whether profit are made or not.

They are issued to the public in the same way as shares.

They can be redeemable or irredeemable.

Redeemable debentures are usually secured against the company's assets in which case they termed as *secured debentures or mortgaged debentures.*

NB: Where no security is given, the debentures are called unsecured /naked debentures**.**

- **Loans from bank and other financial institutions;-**A company can borrow long term or short term loans from banks and other money lending institutions such as Industrial and Commercial Development Corporation [I.C.D.C]

These loans are repayable with interest of the agreed rates.

- **Profits ploughed back;-**A company may decide to set aside part of the profit made to be used for specified or general purposes instead of sharing out all the profit as dividends. This money is referred to as a reserve.
- **Bank overdraft;-**A customer to a bank may make arrangements with the bank to be allowed to withdraw more money than he/she has in the account.
- **Leasing and renting of property.**
- **Goods brought on credit.**
- **Acquiring property through hire purchase.**

TYPES OF COMPANIES

- ***PRIVATE LIMITED COMPANY***

Private limited company has the following characteristics;

- Can be formed by a minimum of 2 and a maximum of 50 shareholders, excluding the employees,
- Does not advertise its shares to the public, but sells them privately to specific people
- Restricts transfer of shares i.e. a shareholder cannot sell his/her shares freely without the consent of other shareholders.
- Can be managed by one or two directors. A big private company may however, require a board of directors
- Can start business immediately after receiving the certificate of incorporation without necessarily having to wait for a certificate of trading.
- It does not have an authorized minimum share capital figure.
- Has a separate legal entity and can own property, enter into contracts, sue or be sued.
- Has limited liability.

- Has a perpetual existence.
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Formation

-It must have a memorandum of association, article of association list of directors, declaration signed by a director or lawyer and certificate of incorporation

Advantages of private limited company

- ***Formation:*** The Company can be formed more easily than a public company. The cost of information is less than that of a public company
- ***Legal personality:*** A private company is a separate legal entity from its owners. Like a person, it can own property, sue or be Sued and enter into contacts
- ***Limited liability:*** Shareholders have limited liability meaning that they are not responsible for the company's debts beyond the amount due on the shares
- ***Capital:*** They have access to a large pool of capital than sole proprietorship or a partnership. They can borrow money more easily from financial institutions because it owns assets which can be pledge as security
- ***Management:*** A private company has a larger pool of professional managers than a sole proprietorship or a partnership. These managers bring in professional skills in their own areas which are of great advantage to a private company
- ***Assured continuity of the business:*** Death, bankrupty or withdrawal of a shareholder does not affect the continuity of the company
- ***Trading:*** Unlike a public company a private company can commence trading immediately upon receiving a registration certificate.

Disadvantages of a private company

- ***Returns:*** A private company, unlike sole proprietorship or a partnership, must submit annual returns on prescribed forms to the registrar of companies immediately after the annual general meeting
- ***Capital:*** A private company cannot invite the public to subscribe to its shares like a public limited company. It therefore limited access to a wide source of capital.
- ***Share transfer:*** The law restricts the transfer of shares to its members/shareholders are not free to transfer their shares

II) PUBLIC LIMITED COMPANY;- Public limited companies have the following characteristics:

- Can be formed by a minimum of 7(seven) shareholders and no set maximum.
- Cannot start business before it is issued with a certificate of trading. This is issued after the certificate of incorporation and after the company has raised a minimum amount of capital
- It's managed by a board of directors.
- The shares and debentures are freely transferable from one person to another.
- It advertises its shares to the public/ invites the public to subscribe for/buy its shares and debentures.
- Must publish their end of year accounts and balance sheets.
- Must have an authorized minimum share capital figure.
- Has a separate legal entity and can own property, enter into contracts, sue or be sued.
- Has limited liability.
- Has a perpetual existence.

Advantages of public limited company

- ***Wide range of sources of capital :***It has access to wide range of sources of capital especially through the sale of shares and debentures

  -They can also borrow money from financial institutions in large sums and have good security to offer to the lenders.

- ***Limited liability:*** Like private companies, public limited company's shareholders have limited liability i.e. the shareholders are not liable for the company's debts beyond the shareholders capital contribution.
- ***Specialized management:*** PLC'S are able to hire qualified and experienced professional staff.
- ***Wide choice of business opportunities:*** Due to large amount of capital a public company may be suitable for any type of investment
- ***Share transferability:*** Shares are freely transferable from one person to another and affects neither the company's capital nor its continuity.
- ***Continuity:*** PLC has a continuous life as it is not affected by the shareholders death, insanity, bankruptcy or transfer of shares
- ***Economies of scale:*** Their large size enables them to enjoy economies of scale operations. This leads to reduced costs of production which raises the levels of profit
- ***Employee's motivation:*** They have schemes which enable employees to be part owners of the company which encourages them to work harder in anticipation of higher dividends and growth in the value of the company's shares.

- ***Share of loss:*** Large membership and the fact that capital is divided into different classes' means that the risk of loss is shared and spread.

- ***Shareholders are safe guarded;*** Publicity of company accounts safeguard against frauds.

Disadvantages of public limited companies

- ***High costs of formation:*** The process of registering a public company is expensive and lengthy. Some of the costs of information are legal costs, registration fees and taxes

- ***Legal restrictions:*** A public company must comply with many legal requirements making its operations inflexible and rigid

- ***Alienation of owners:*** Shareholders non-participation in management is a disadvantage to them

- ***Lack of secrecy:*** The public limited companies are required by law to submit annual returns and accounts to the registrar of companies denying the company the benefit of keeping its affairs secret. They are also required to publish their end of year accounts and balance sheets.

- ***Conflicts of interests:*** Directors may have personal interests that may conflict with those of the company. This may lead to mismanagement***.***

- ***Decision making;*** Important decision are made by the directors and shareholders. The directors and shareholders meet after long periods which make decision making slow/delayed and expensive***.***

- ***Diseconomies of scale:*** The large size and nature of business operations of public limited companies may result in high running/operation costs and inefficiency

- ***Double taxation:*** There is double taxation since the company is fixed and dividends distributed to the shareholders are also taxed

- ***Inflexibility:*** Public limited companies cannot easily change its nature of business in response to the changing circumstances in the market. All shareholders must be consulted and agree.

DISSOLUTION OF A COMPANY

The following are the circumstances that may lead to the dissolution of a company:

- Failure to commence business within one year- If a company does not commence business within one year from the date of registration, it may be wound up by a court order on application of a member of the company.

- Insolvency – when a company is not able to pay its debts, it can be declared insolvent and wound up.

- Ultra- vires – this means a company is acting contrary to what is in its objective clause. In such a case, it may be wound up by a court order.

- Amalgamation – two or more companies may join up to form one large company completely different from the original ones.
- Court order – the court of law can order a company to wind up especially following complaints from creditors.
- Decision by shareholders – the shareholders may decide to dissolve a company in a general meeting.
- Accomplishment of purpose or expiry of period of operation – a company may be dissolved on accomplishment of its objects, or on expiry of period fixed for its existence.

THE ROLE OF STOCK EXCHANGE AS A MARKET FOR SECURITIES

DEFINATIONS

- Stock: a group of shares in a public limited company
    - Stocks are formed when all the authorized shares in a particular category have been issued and fully paid for.
- Stock exchange market: is a market where stocks from Quoted companies are bought and sold
    - Stock exchange markets enable share holders in public companies to sell their shares to other people, usually members of the public interested in buying them.
- A Quoted Company: is a company that has been registered (listed) as a member of the stock exchange market.
    - Companies that are not quoted cannot have their shares traded in the stock exchange market.
- Securities: this could either refer shares or documents used in support of share ownership.
- Initial Public Offer (I. P. O): refers to situations in which a company has floated new shares for public subscription (Has advertised new shares and has invited members of the public to buy them.
- Secondary market: The market that deals in second hand shares i.e. the transfer of shares from one person or organization to another.

There is only one stock exchange market in Kenya i.**e. The Nairobi Stock Exchange.**

A person wishing to acquire shares will do so either at an **IPO** or in the **secondary market.** However, an investor cannot buy or sell stocks directly in the stock exchange market. They can only do so through stock brokers.

ROLES OF THE STOCK EXCHANGE MARKET

- **Facilitates buying of shares-** it provides a conducive environment to investors who want to buy shares in different companies.
- **Facilitates selling of shares-** it creates a market for those who wish to sell their shares.
- **Safeguarding investors' interests-** it monitors the performance of the already quoted companies and those found not meeting expectations are struck off. Companies who want to be quoted must also attain a certain standard of performance.
- **Provides useful information-** it provides timely, accurate and reliable information to investors which enable them to make decisions on the investments to make. The information is passed on through mass media and stock brokers.
- **Assist companies to raise capital-** it assists companies to raise capital by creating an environment through which companies issue new shares to members of the public in an **IPO**.
- **Creation of employment-** it creates employment for those who facilitate the buying and selling of shares eg stock brokers, stock agents etc.
- **Raising revenue for the government-** the government earns revenue by collecting fees and other levies/ dues from activities carried out in the stock exchange market.
- **Availing a variety of securities-** it avails a variety of securities from which an investor can choose from. The market therefore satisfies needs of various investors eg investors who wish to buy from different companies can do so in the market.
- **Fixing of prices-** the stock exchange market is in a position to determine the true market value of the securities through the forces of demand and supply. This is of great importance to both the buyer and the seller.
- **Measures a country's economic progress-** the performance of securities in the stock exchange market may be an indicator of a country's economic progress e.g a constant rise in prices and volumes of securities traded within a given period of time would indicate that the country's economy is positively growing.
- **Promotes the culture of saving-** it provides investors with opportunities to channel their excess funds. Such people act as role models to other members of the society who may emulate them thereby promoting a saving culture.

PUBLIC CORPORATIONS (STATE CORPORATIONS)

These are organizations formed by and/or controlled by the government (the government has a controlling interest). This means that the government owns more than 50% shares in the corporation. Where the government has full ownership, the organization is known as a parastatal

- Public corporations are formed to perform certain/specific functions on behalf of the government.
- They are formed to provide essential services that are generally in the public interest, and that may require heavy initial capital investment which few private investors can afford
- They are formed by the act of parliament.

Examples

- Kenya Railways corporation- provides railway transport
- Telkom Kenya-provides telecommunication services
- Postal corporation of Kenya
- Industrial and commercial Development corporation (ICDC)- financial and management services
- Mumias and Chemelil sugar companies.
- Kenya air ways- provide air transport services. Etc
-

Characteristics/features of public corporations

- They are formed by the government under the existing laws i.e formed by an act of parliament eg education act
- Initial capital is provided by the government.
- They are jointly owned by the government and members of public/private investors.
- They are set up to perform certain specific functions on behalf of the government
- They are managed by a board of directors appointed by the government or appointed by the government and the joint owners.
- They have an entity of their own and can own property, enter contracts, sue and be sued
- They have limited liability
- Some operate without a profit motive while others have a profit motive

Formation

-Some are formed by an act of parliament while others are formed under the existing laws.

-When formed by an act of parliament, the Act defines its status obligations and areas of operation. The Act outlines the following;

- Proposed name of the corporation

- Aims and objectives
- Goods or services to be produced and provided
- Location(Area of operation)
- The appointment of top executives
- The powers of the Board of directors
- The ministry under which it will operate

Management

-The public corporations are managed by a board of directors appointed by the president or the relevant minister.

-The chairman and the board of directors are responsible for the implementation of the aims and objectives of the corporations.

-The chairman of the board of directors reports to the government (president) through the relevant minister.

-The managing director who is usually the secretary of the board of directors in the chief executive officer of the corporation

Sources of capital

-The initial capital is usually provided by the government as a vote of expenditure for the ministry concerned

-Those corporations jointly owned by the government and the public raise capital through the sale of shares

-financial institutions in form of loans

-Retained profits/profits ploughed back.

-Hire purchase.

Advantages of public corporations

- Initial capital is readily available because it is provided by the government
- Can afford to provide goods and services at low prices which would otherwise be expensive if they were left to the private sector.
- Most of them produce goods and services in large quantities thereby reaping the benefits of large scale production
- Some are monopolies. They hence enjoy the benefits of being a monopoly e.g. they do not have to incur costs advertising since there is no competition

- They can be bailed out/assisted by the government when in financial problems
- They have limited liability
- Money for research and development can be made readily available by the government
- Through corporations the government is able to remove foreign domination in the country
- They can afford to hire qualified personnel.

Disadvantages of public corporations

- They are managed by political appointees who may not have the necessary managerial know how.
- When they make losses, they are assisted by the government and this could lead to higher taxation of individuals
- Lack of competition due to monopoly leads to inefficiency and insensitivity to customers feelings.
- Political interference may hamper efficiency in the achievement of set goals and objectives.
- Decision making is slow and difficult because the organizations are large.
- They may lack close supervision because of their large sizes.
- There is embezzlement of large sums of money leading to loss of public funds
- The government is forced to provide goods and services to its citizens in all parts of the country where at times its uneconomical to provide them because the costs of providing them may surpass the returns
- Public funds are wasted by keeping poorly managed public corporations.
- Diseconomies of scale apply in these business units because they are usually very large scale organizations e.g. decision making may take long.

Dissolution of public corporations

They can only be dissolved by the government due to;

- Persistent loss making
- Bankruptcy- where the corporation cannot pay its debts.
- Change in the act of parliament that formed the corporation.
- Privatization.

- Mismanagement, resulting in poor management of the corporation.

TRENDS IN FORMS OF BUSINESS UNITS

- ***Globalizations;***

This refers to the sharing of worlds resources among all regions i.e where there are no boundaries in business transactions

Some companies referred to as multinationals, have branches in many parts of the world e.g coca-cola company

Globalization has been made possible and effective through the development and improvement of information and technology organization i.e

- **World website (internet);** one can acquire and order for goods through the internet. This is referred to as Electronic Commerce (E- Commerce) and E- Banking.
- **Mobile phones** technology has revolutionized ways of life and business and even remote areas have been opened up.

Business Amalgamations/combinations

This occurs when two independent business enterprises combine to form one large organization

Levels of combinations

- ***Vertical combination;*** This is when businesses engaged in different but successive levels of production combine e.g. primary(extractive) level combines with secondary(manufacturing)level or secondary level combining with tertiary level.

  Example; A company producing cotton (raw materials) combining with a textile industry.

- ***Horizontal combination;*** This is where business enterprises of the same level combine e.g. secondary and secondary levels e.t.c

Types of Amalgamation/combination

Amalgamations whether vertical or horizontal can be achieved in these ways;

- ***Holding companies***

-A holding company is one that acquires 51 percent or more shares in one or more other companies.

-The various companies entering into such a combination are brought under a single control.

-These companies are controlled by the holding company and are called ***Subsidiaries***.

-The subsidiary companies are however allowed to retain their original names and status, but the holding company appoints some members to be on the board of directors of these subsidiaries, so as to control their activities.

-Holding companies are usually financial institutions because they are able to buy controlling shares in subsidiary companies

- ***Absorptions (takeovers)***

This refers to a business taking over another business by buying all the assets of the other business which then ceases to exist.

Example; Kenya Breweries took over the castle company in Kenya

- ***Mergers(Amalgamation);***

This is where two or more business organizations combine and form one new business organizations.

-The merging companies cease to exist altogether.

- ***Cartels***

This is a group of related firms/ companies that agree to work together in order to control output, prices and markets of their products – O. P. E. C (organization of petroleum exporting countries) is an example.

- **Privatization**; this is the process of transferring / selling state owned corporations to public limited companies or private investors. This is done by the Government selling their shareholding to members of the public. The main aim is to:
    - ✓ Improve efficiency
    - ✓ Generate revenue for the government.
    - ✓ Reduce government control
    - ✓ To break monopolistic practices
    - ✓ To reduce government expenditure on corporations that relies on government subsidy.
- **Check off system**- this is a method of remitting money especially to **SACCOS** where the employer deducts the contribution from the source and submits it to the SACCO on behalf of the employee who is a member of the SACCO.
- **Burial Benevolent Funds (B. B. F**); some SACCOS have started systems/ funds to assist their members financially in burials through creation of BBF.
- **Front Office Savings Account (FOSA);** SACCOS have expanded their services to members by introducing FOSA. The account enables members to conviniently deposit and withdraws money. A member may also be provided with an ATM card which enables him/her to withdraw money at various pesa points/ ATM’s.

- **Franchising ;** this is where one business grants another the rights to manufacture, distribute or produce its branded products using the name of the business that has granted the rights eg General motors' has been granted franchise to deal in Toyota, Isuzu and Nissan vehicles.
- **Trusts;** This is where a group of Companies work together to reduce competition. Trusts may also be formed where a company buys more than 50% of shares in a competing company so as to reduce competition.
- **Performance contracts;** Employees in state corporations are expected to sign performance contracts in order to improve their efficiency. Other private institutions are also adopting the same practice.

TOPIC 2

GOVERNMENT AND BUSINESS

BY THE END OF THE TOPIC, THE LEARNER SHOULD BE ABLE TO:

- Explain reasons for government involvement in business.
- Explain how the government gets involved in business.
- Discuss the merits and demerits of government involvement in business.
- Discuss the importance of consumer protection.

INTRODUCTION

Government involvement in business activities is one of the commercial duties it owes its citizens. It is the one that provides the necessary environment for investments to be undertaken by itself, or by the local and foreign investors. This, the government may do in various ways, these include;

- Producing goods and services
- Distributing goods and services
- Advising producers and traders
- Promoting trade and economic development.
- Protecting consumers against exploitation by producers and traders.
- As a consumer of goods and services.

Reasons for Government involvement in business

The following are the major reasons for the government's involvement and participation in business activities;

- To prevent exploitation of the public by private business persons especially in the provision of essential goods and services such as sugar, transport, communication etc. the Kenya Bureau of standards (KEBS) regulates the quality of goods consumed in Kenya.
- To provide essential goods and services in areas where private individuals and organizations are unwilling to venture because of low profits/ high risks involved.
- To provide essential goods and services which private organizations and individuals are unable to provide due to the large amount of initial capital required b e.g. generation of electricity, establishment of airlines etc.
- To attract foreign investment by initiating major business projects.
- To stimulate economic development in the country e.g. by providing social services.
- To provide goods and services which are too sensitive to be left in the hands of the private sector e.g. provision of firearms.
- To create employment opportunities by initiating projects such as generation of electricity.
- To prevent foreign dominance of the economy by investing in areas where the locals are not able to.
- To redistribute wealth where returns are very high.
- To prevent establishment of monopolies**.**

METHODS OF GOVERNMENT INVOLVEMENT IN BUSINESS

The government gets involved in business activities through the following methods:

- ***Regulation***

This refers to Rules and restrictions the government requires business units to follow in their business activities. Through this method, the government ensures high quality goods and services and puts in control measures to protect consumers from exploitation. The government regulation measures include;

- **Licensing**

A license is a document that shows that a business has been permitted by the government to operate. It is usually issued upon payment of a small fee.

Licensing is the process of issuing licenses to businesses. Some of the reasons why the government issues licenses include;

- Regulating the number of businesses in a given place at any given time to avoid unhealthy competition.
- To control the type of goods entering and leaving the country.
- To ensure there are no illegal businesses.
- To ensure that traders engage only in trade activities that they have been licensed for.
- To ensure that those who engage in professional activities meet the requirements of the profession.
- To raise revenue for the government.
- **Ensuring standards/ enforcing standards;** The government regulates business activities by setting standards that businesses should and ensuring that the standards are adhered to. To achieve this purpose, the government has established bodies such as;
- ***Kenya bureau of standards (KEBS***) whose main responsibility is to set standards especially for the manufactured goods and see to it that the set standards are adhered to/ met. Goods that meet such standards are given a diamond mark of quality, to show that they are of good quality.
- ***The ministry of public health*** to ensure that businesses meet certain standards as concerning facilities before such businesses can be allowed to operate. Such standards may include clean toilets, clean water and well aerated buildings.

- **Legislation;** The Government may come up with rules and regulations (laws) that regulate business activities e.g. banning hawking in certain areas, matatus required to carry certain number of passengers e.t.c.
- ***Training***

The government takes keen interest in training and advising people in business about business management strategies and better ways of producing goods and services. The government offers these services through seminars and courses. This is mainly done by **the Kenya Business Training Institute (K.B.T.I).**

Reasons for government training include;

- To expose business persons to modern developments in management.
- Introduce modern technology and skills in management
- Educate the business people on efficient methods of operating a business e.g., effective methods of advertising and keeping books of accounts.
- Expose business people to problems/ challenges facing them and their possible solutions for example, problems of raising capital and identifying investment opportunities.
- Impart proper business ethics e.g. good customer relations and honesty.
- Creating awareness of the available profitable business opportunities in their environment.
- Expose business people to government policies regarding business activities in the country.
- Educate business people on how to use available resources to minimize costs and maximize profits.
- Expose people to other opportunities that exist in the import and export market.
- ***Trade promotion***

This is a government initiated and supported policy to encourage local business people to enter into business. This is aimed at increasing the volume and variety of goods and services traded in.

Trade promotion is classified as either **external trade promotion** or **internal trade promotion.**

- **External trade promotion**
- The purpose of external trade promotion is to encourage local business people to enter into the export market.
- It also intended to attract foreign investors into the country.
- In Kenya, external trade promotion is done through the department of external trade in the ministry of trade and industry.
- External trade promotion may also be done by ***Commercial attaches.***

Commercial attaches are officers sent by the country's government to work with the embassies in foreign countries as support staff in the field of

commerce. Their main duty is to look at the interests of their home countries' exports eg cash crops and manufactured goods.

Duties of commercial attaches

- Explore and identify new markets for more export opportunities.
- Research and analyze markets for exports from their home countries.
- Keep statistics of products such as volumes, packaging size and method of manufacturing.
- Attend meetings, seminars and workshops on trade patterns of the countries and keep data for new markets of exports.
- Publish and advertise their country's exports in business journals and magazines.
- Select buyers, agents and distributors of the home country's exports.
- Inform traders in their home countries of the standards required for exports.
- Assist sales missions from their home countries by organizing educational tours for them.
- Organize visits to trade fairs and exhibitions for business people from their home country.
- Make detailed reports on commercial activities that may help improve the exports of their countries.

To perform these duties, the commercial attaché needs to:

- Keep information on prices paid for exports and terms of payments(conditions to be filled before the payment is made)
- Be aware of the rules that govern payment in international trade.
- Be aware of the working of the regional organizations that operate in developing countries such as **the East African Community (E. A. C), Inter-Governmental Authority for Development (I.G.A.D), Common Market for Eastern and Southern Africa (COMESA), Economic Commission for Africa (E.C.A) and African Growth Opportunity Act (A.G.O.A).**
- **Internal trade promotion**

This is done by the government through the ministry of trade. The ministry carries out various activities

CONSUMER PROTECTION

Definition:

- ✓ These are measures by either, the government, NGOs or consumers to avoid exploitation of consumers by business people.

- ✓ It is the deliberate attempt to safeguard consumer against exploitation or malpractices in business.

Need For Consumer Protection

i. To protect them against sale of poor quality goods and services.

ii. To protect them against sale of goods and services under unhygienic conditions and environment.

iii. Protect them against sale of harmful goods and services.

iv. Protect them against breach of contract.

v. To protect them against overpricing of goods services.

vi. To protect them against hoarding of goods and services this may create artificial shortages.

vii. Protect them against cheating through misleading or false advertisements.

viii. To protect them against sale of underweight goods and inadequate services.

ix. Protect them against sale of socially unacceptable goods and services. For example, pornographic materials.

x. Protect them against dangers that arise due to contamination of the environment.

xi. Protect them from dangers that may arise from the use of unsafe building.

xii. Protect them against sale of illegal goods and services.

METHODS OF CONSUMER PROTECTION

Government initiated methods

i. Enactment of laws that safeguard interest of consumer such as:

- ✓ Kenya Bureau Of Standards (KEBS) Act to ensure standards of goods are maintained
- ✓ Trade Description Act to guard against false or misleading advertisement.
- ✓ Food And Drug Act to ensure that products are not harmful
- ✓ Public Health Act to ensure safety and health standards are met.
- ✓ Trade Licensing Act.

- ✓ Weight And Measures Act to ensure goods are of the right weight.
- ✓ Hire-Purchase Act to guard against unfair repossession of goods.

ii. Encourage **formation of consumer organizations** to cater for the interests of consumers.

iii. Encouraging businesses to **conduct their affairs in a way that is not detrimental to the interest of consumer.**

Consumer initiated methods

These are methods by the consumers to protect themselves from exploitation by business people by forming consumer associations.

Functions of consumer associations

- ✓ Deals with complaints on defective goods.
- ✓ Ensure regular supply of goods: no hoarding
- ✓ Ensure correct weight and measures of commodities.
- ✓ Ensuring availability of goods and services.
- ✓ Educating members on their rights as consumers.
- ✓ Ensure health and safety regulation are followed.

Limitations of consumer initiated methods

- ✓ Lack of government support
- ✓ Lack of capital to finance the associations
- ✓ Ignorance of consumers on their rights.
- ✓ Lack of initiative from consumers in checking trader's performance.
- ✓ Reluctance of many consumers to join these associations so that they may voice their complaints as a group.

Non-governmental Organisations (NGOs)

- ✓ Involve in consumer protection by informing consumers on their rights e.g right to true advertisement.
- ✓ Ensures standards are maintained by both producers and traders.

Emerging issues in business and government

- ✓ **Corruption –** this has lowered profit in that most firms affected perform poorly.

- ✓ **Market liberalization –** is the removal of protection policies and regulations so that the Kenyan market is open to all.
- ✓ **Privatization-** is the conversion of public enterprises. Privatization has enhanced efficiency of enterprises to make profit.
- ✓ **Dumping –** occurs when firms sell goods at lower prices overseas than in its home market. This affects local products by denying them market and capacity to survive and expand.
- ✓ **HIV/AIDS-** the government is losing a lot of competent trained manpower through HIV/AIDS

T0PIC 4

COMMUNICATION

Meaning of communication

- Communication is the transfer or conveyance of messages or information from one person to another.
- Communication is the process of sending and receiving meaningful messages, information and ideas between two or more people located at different points in space.

  Note: The space between the sender (s) and the receiver (s) maybe as narrow as when people are talking to each other or as wide as between the North Pole and the South Pole.

Effective communication is vital/important for business in that it serves the following purposes.

Importance of communication (purposes)

- ***To give and obtain information***

For an organization to run smoothly there should be proper flow of information within the business and also between the firm and outsiders e.g. the manager may inform members of staff about a planned meeting. Similarly the business may receive a letter of inquiry from a customer

- ***To clarify issues and points***

Through proper communication the organization is able to clarify confusing issues from within and without the firm for example in cases where there are many managers. It would be necessary to clarify the responsibilities of each manager.

- ***To enhance public relations***

  Good/efficient communication enables the business to create a more positive image and a favorable reputation of itself to outsiders and overcome prejudices and negative attitudes that people may have against the business.

- ***To start and influence Action***

  Proper communication enables the business to get new ideas make plans and ensure that they are implemented in the desired way.

- ***Improving customer service;*** Good communication helps in reducing errors providing customers with desired feedback and assisting in handling inquiries more efficiently

- ***Giving instructions;*** Through proper communication management is able to get work done by issuing instructions (procedures and orders)e.g. a supplier may be instructed when and where to deliver the goods ordered.
- ***To give Reassurance;*** Information is needed to reassure people that their performance is good e.g. an employee may feel better is he/she is served with a "will done"memo or a "customer of the year" award.
- ***Confirming arrangements;*** Through communication arrangements are confirmed for example confirmation of meetings conferences or details of transactions
- ***Co-ordinating departments of the firm;*** Charges in one department are communicated to other departments that have a direct bearing to those changes e.g. when sales increase the sales department informs the production department so as to increase production proportionality
- ***Modifying behavior of persons within or outside the organization;*** Through effective communication persons are trained and counseled and as a result their behavior knowledge and attitudes change

Communication process

Communication is a process that involves interchange of information and ideas between two or more people. Communication therefore is a circular process i.e communication may lead to some reaction which in turn may generate further communication

or feedback. This flow can be illustrated as below:

(2) Message

(3) Receiver

Message 3

Receivercdddd

- Sender

Sender

(4) Feed back

Feedback

- ***Sender*** –this is the person who writes, speaks or sends signs (symbols or signals) and is the source of the information.
- ***Receiver -*** this is the person to whom the information or the message is sent.
- ***Message –*** this is the information that is transmitted from the sender to the receiver. It may be spoken, written or in the form of symbols.
- ***Feed back –*** this is the response to the sender's message. A message is said to have been understood if the receiver provides the desired feedback.

Lines of communication

Communication can be classified according to either the levels of the communicating parties or according to the nature of the message.

- ***According to levels***-This can either be:

  I) Vertical

  ii) Horizontal

  iii) Diagonal

- ***Vertical communication***

This is where messages are passed between a senior and her/his juniors in the same organizations

Vertical communication can be divided into two parts

-Downward communication

-Upward communication

-Downward communication-This is a communication process which starts from the top manager to her/his juniors. This can be informed of:

- *Training juniors*
- *Evaluating performance*
- *Delegating duties*
- *Solving the problems facing workers*
- *Inspiring and motivating the juniors(giving rewards)*

-Upward communication-This is a communication process that starts from the juniors to the seniors and maybe in the form of:

- *Submitting reports*
- *Giving suggestion*
- *Submitting complaints a grievances*
- *Making inquiries*

ii) ***Horizontal communication (lateral communication)***

This is communication between people of the same level (rank) in the same organization e.g. departmental heads in an organization may communicate to achieve the following:

- Co-ordination and harmonization of different activities.

- To create teamwork within the department.
- To exchange ideas in order to develop human resources.
- To reduce goal blindness among different departments.
- To create a sense of belonging among department heads thus acting as a motivating factor.

One of the major characteristics of this type of communication is that there are less inhibitions. The people involved are more open and free with each other than in the case of people with different ranks.

iii) *Diagonal communication*

This is communication between people of different levels in different departments or different organizations e.g. an accounts clerk may communicate with a sales manager of the same organization or of different organizations. Diagonal communication enhances team work.

b) According to nature of message

This can either be;

i) *Formal communication*

ii) Informal communication

Formal communication

This is the passing of messages or information using the approved and recognized way in an organization such as official meetings, memos and letters. This means that messages are passed to the right people following the right channels and in the right form.

Formal communication is also known as official communication as it is the passing of information meant for office purposes.

Formal systems of communication are consciously and deliberately established.

Informal communication

This is communication without following either the right channels or in the right form i.e. takes place when information is passed unofficially. It is usually used when passing information between friends and relatives hence it lacks the formality.

Informal communication may also take the form of gossips and rumor-mongering.

Informal communication usually suppliments formal communication as is based on social relations within the organization.

Note: Both formal and informal communication is necessary for effective communication in an organization.

Essentials of Effective communication

For communication to be effective it must be originated produced transmitted received understood and acted upon. The following are the main essentials to effective communications.

i) ***The sender/communicator***

This is the person from whom the message originates. He/she encodes the message i.e. puts the message in the communicative form.

ii) ***Message***

This is the information to be sent. It is the subject matter of communication and may contain words, symbols, pictures or some other forms which will make the receiver understand the message

iii) ***Encoding;*** This is the process of expressing ones ideas in form of words, symbols, gestures and signs to convey a message

iv)***Medium/channel***; This refers to the means used in communicating. This could be in the form of letters, telephones and emails among others.

v)***The receiver***; This is the person for whom the message is intended. The receiver decodes the message for proper understanding.

vi)***Decoding;*** This is the process of interpreting or translating the encoded message to derive the meaning from the message

vii) ***Feed-back***; This refers to the reaction of the receiver of the message. This maybe a reply /response which the receiver sends back to the sender.

The above can be represented in a diagram as shown below;

Receiver (5)

Channel (4)

Encoding (3)

Message (2)

Decoding (6)

Sender (1)

Feedback (7)

FORMS AND MEANS OF COMMUNICATION

Forms; These are channels or ways of passing on messages. The four main forms are;

i) Oral communication

ii) Written communication

iii)Audio –visual communication

iv) Visual communication

Means; This is the device used to pass on information e.g. messages, letters, telephones e.t.c

- **Oral communication**

This is where information is conveyed by talking (word of mouth)

It is also known as ***verbal communication***

Means of communication

i) Face-to-face conversation

This involves two or more people talking to each other. The parties are usually near each other as much as possible to ensure effective communication.

It is suitable where subject matter of discussion require convincing persuasion and immediate feed-back.

It may be used during meetings, interviews, seminars, private discussions, classrooms e.t.c

It is the most common means of oral communication

Advantages of face-to-face communication

- Provides for immediate feedback
- Has personal appeal
- Body language can be easily expressed
- One can persuade or convince another
- It is the simplest communication to use
- It is direct i.e. does not pass through intermediaries
- Convenient for confidential messages.

Disadvantages of face-to-face communication

- No record for future reference
- Can be time consuming
- Messages can be distracted
- Not suitable when people are far apart

- Unsuitable for the dumb and deaf

ii)***Telephone***

This form of communication is commonly used in offices and homes. It is useful in sending messages quickly over short and long distances.

It is however not suitable for sending;

- *Confidential messages*
- *Long and detailed reports, charts and graphs*
- *Messages that would require reference or evidence*

In Kenya telephone services are mainly provided by Telkom Kenya Limited. The subscriber is required to purchase the telephone equipment from the post office or other authorized dealers before installation.

Installation is done on application by the subscriber (applicant).He/she pays the installation fee in addition; the subscriber is sent a monthly bill with the charges for all the calls made during the month.

The charges for calls depend on the time spent time of the day of the week and distance of the recipient from the caller e.g. it is cheaper to call at night than during the day. It is also cheap to make calls during public holidays and weekends than on weekdays.

There are also mobile phones which have no physical line connection to exchange and may be fixed to a vehicle or carried in pockets. In Kenya these services are provided by safaricom, Airtel, orange and Yu mobile communications.

Advantages of Telephones

- Relatively fast
- Has personal appeal
- Provides for immediate feedback
- One can persuade or convince another
- Suitable for long distance communication

Disadvantages of Telephone

- Can be expensive especially over long distances
- No record for future reference
- Lacks confidentiality
- Not convenient for dumb and deaf
- Can be time consuming

<u>Reasons why mobile phones have become popular</u>

- They are portable and can be conveniently carried around.
- It is not very expensive especially when making local calls.
- Relatively cheap to acquire.
- Some mobile phones can record conversations / calls thereby acting as evidence.
- Can be used to send short text messages (sms)
- Can be used anywhere since they are portable.

iii) Radio calls

This involves transmitting information by use of radio waves i.e. without connecting wires between the sender and the receiver

The device used is called a radio telephone. It is commonly used in remote areas where normal telephone services are lacking or where telephone services are available but cannot be conveniently used e.g. policemen on patrol in different parts of a town

Radio transmission is a one way communication system i.e. only one person can speak at a time. It is therefore necessary for the speaker to say'over' to signal the recipient that the communication is through so that the recipient can start talking. To end the conversation, the speaker says 'over and out'

The radio calls are commonly used by the police, game rangers, researchers, foresters, ship owners and hotels situated in remote areas. They are also used for sending urgent messages such as calling for an ambulance and fire brigade

Note; Radio calls are not confidential since they use sound frequencies that can be tapped by any radio equipment that is tuned to that frequency

Advantages of Radio calls

- Relatively fast
- Has immediate feedback
- Has personal appeal
- Provide room for one to persuade and convince another
- Suitable for remote areas
- Convenient for long distances

Disadvantages of Radio calls

- No record for future reference
- Lacks confidentiality
- Messages are sent one way at a time

- Can be expensive
- Cannot be used by dumb and deaf
- Can be time consuming.

iv) ***Paging***

This is a means of communication used to locate staff or employers who are scattered in an organization or who are outside and need to be located urgently

When within the organization portable receivers, lighted signals, bells, loudspeakers etc are used

When outside the organization employees are contacted using portable receivers (pocket-size) used to send messages through sms (short message services)

The paying system can only be used within a certain radius. When using a portable receiver, the caller will contact the subscriber by calling the post office which will then activate the pager.

The subscriber is then informed to contact the originator of the message.

Paging is mostly used in emergency cases

v)***Radio***

Usually messages intended for a wide audience can be transmitted through a radio more quickly and economically than by using other forms of communication.;`

Radio is used for different reasons apart from advertising e.g for formal notices, and venue for activities

Advantages of oral/verbal communication

- Very effective method of communication since the recipient can be persuaded/convinced
- It is relatively faster method of communication
- The sender can get immediate feedback
- It indicates some sence of regard hence more appealing.

Disadvantages of oral/verbal communication

- Has no records for future reference
- Is an expensive method especially if the two parties are far apart
- Is not good for confidential messages
- It is not suitable for confidential messages
- It may be time wasting especially where one needs to be convinced

Written Communication

This involves transmission of messages through writing. It is the most formal way of communication because the information is in recorded form and can be used for reference

Means of written communication

(i)Letters

Letters are the most commonly used means of communication.

There are two categories of letters;

a)Formal letters

b) Informal letters

a) Formal letters; These include business letters and official letters.

Business letters are written to pass messages and information from businessmen to customers and vice versa e.g. letters of inquiry and acknowledgement notes.

It can also be used between employees and employers in an organization e.g. a complimentary note.

Official letters are letters between people in authority and others that touch on the activities of the organization e.g. an application letter for an advertised vacancy in an organization.

Formal letters have a salutation clause which usually starts with “Dear Madam “or “Dear Sir”. It also bears the addresses of both the sender and the recipient, a subject heading and a complimentary clause ending with “Yours faithfully”.

b) ***Informal Letters;*** these are letters between friends and relatives

They are also known as ***Personal letters***

ii) Telegrams

This is a means of communication provided by the post office. The sender obtains the telegram form fro the post office and fills the message on it in capital letters and hand it over to the post office employees at the counter. Alternatively the sender may use a telephone to read the message to the post office. The post office then transmits the message to the recipient post office.

The charges of a telegram are based on the number of words used, the more the words used the higher the charges. However there is a standing charge.

Telegrams are used for sending urgent messages.

Note; Due to changing technology telegrams have lost popularity. Short messages can now be sent by cell phones (mobile phones) using the short messages services (sms)

iii) Telex

This is a means of communication used to send short or detailed messages quickly by use of a teleprinter. The service is provided by the post office on application.

A message is sent by use of two teleprinters one on the senders end and another on the recipients end. When sending information through a teleprinter which is a form of electric typewriter producing different electric signals, its keys are pressed and automatically the message is printed at the recipient's machine.

Telex saves time for both the sender and recipient as the messages are brief precise and received immediately. However it's an expensive means of communication

iv) ***Facsimile (Fax)***

This involves transmission of information through a fax machine. Both the sender and the receiver must have a fax machine. These machines are connected using telephone lines

Fax is used to transmit printed messages such as letters, maps, diagrams and photographs. To send the information, one dials a fax number of the required destination and then the document is fed into the sender's machine. The receiving machine reproduces the document immediately. It is used for long distance photocopying service.

v) Memorandum (Memo)

This is printed information for internal messages within an organization. It is normally used to pass information between departments or offices in an organization.

Memoranda have no salutation or complimentary clause. They are suitable for informing the officers within an organization of matters related to the firm.

A memo is pinned on the notice board of an organization if it is meant for everybody otherwise passed to the relevant staff.

vi) ***Notice***

This is a written communication used to inform a group or the public about past current or future events. It is usually brief and to the point. It can be placed on walls, in public places, on trees, in newspapers or on notice boards

viii) Reports

These are statements/within records of findings recommendations and conclusion of an investigation/research. A report is usually sent to someone who has asked for it for a specific purpose.

viii) Circulars

These are many copies of a single letter addressed to very many people when the message intended for each is the same.

ix) Agenda

This is an outline of the items to be discussed in a meeting. It is usually contained in a notice to a meeting sent in advance to all the participants of the meeting. The notice of the meeting contains;

- The date of the meeting
- The venue of the meeting
- Time of the meeting
- Items to be discussed

x) Minutes

These are records of the proceedings of a meeting. Keeping minutes of certain meetings is a legal requirements e.g companies

Keeping minutes for other meetings are for management purposes to ensure that decisions made at the meetings are implemented

Advantages of written communication

- It can be retained for future reference
- Some like letters are relatively cheap(can produce many copies)
- It is suitable for confidential messages
- Allows for inclusion of fine details
- It is not prone to distortion of messages
- Can be used as evidence
- Can be addressed to many people.

Disadvantages of written communication

- It lacks personal appeal
- It takes time to prepare and reach the recipient
- Suitable for the literate only
- Immediate feedback may not be possible
- Does not offer room for persuasion and convincing
- It may be expensive because it involves a lot of paperwork and time.

- Not suitable if the sender and the receiver do not share a common language.

3) Visual Communication

This is the process of passing information by use of diagrams, drawings pictures, signs, and gestures e.t.c

- ***Photographs***

  A photograph is an image (visual representation of an object as it appeared at the time when the photograph was taken

  Photographs are self-explanatory and may not be accompanied by any narration or explanation. The recipient is able to get the message at a glance.

  b) Signs

  Refer to marks, symbols, drawings or gestures whose purpose is to inform the public about such things as directions, distances, dangers and ideas.

  Examples; road signs, traffic lights and danger signs on electricity poles

  This means of communication can only be effective if the meaning of the sign used is understood.

  Graphs; These are used to show and illustrate statistical information

  Charts; These are diagrams which show or illustrate the flow of an idea e.g. an organization chart illustrates the whole organization structure indicating the chain of command

Advantages of visual communication

- It can be used to pass confidential information

The information may be obtained at once

Disadvantages of visual communication

- Can only be used by people who can see
- The information may be wrongly interpreted
- It may be an expensive method of communication
- Cannot be used for long distances

4) Audio-Visual communication

This is a form of communication in which messages are sent through sounds and signs .

This form of communication ensures that the receiver gets the message instantly.

It is suitable where both the sender and the receiver know the meaning of specific sounds and signs

Means of Audio-visual communication

- ***Television (TV);*** This is a device that transmits information inform of a series of images on a screen accompanied by sound. It is a very effective method of communication since it combines the advantages of image and sound

  A television can be a very suitable means of sending urgent messages especially when it gives live coverage of events.

- ***Siren;*** This is a device used to produce a loud shrill sound accompanied by a flashing light. It is commonly used by the police, ambulances, and the fire brigade and security firms to alert the public of the danger involved e.g. the ambulance siren conveys the message that somebody is seriously sick and therefore other motorists should give way.

Advantages of Audio-visual communication

- It reaches many people
- It is more appealing than other means of communication
- Reinforces verbal communication
- May have a lasting effect on the receiver
- Suitable where receivers are illiterate.

Disadvantages of Audio-visual communication

- It is suitable to those people who can interpret the messages correctly
- It is not suitable for confidential messages
- Preparation may take long.

5) Audio Communication

This is when the message is transmitted through sounds. Examples include

- ***A whistle;*** This is a device which is blown to produce a sharp shrill sound to alert or warn the public or employees in an institution. It is normally used by security guards when there is danger. In some organization, a whistle is used to announce change in shifts
- ***Horn;*** This is also an instrument that is used to produce sound which passes different information depending on the way it is blown.

  Other methods of audio communication include drums, alarms, and bells among others

Advantages of Audio communication

- Is a faster method of communication

- It can reach several people at once
- The message is received instantly

Disadvantages of Audio communication

- The message may be interpreted wrongly
- It can only be used within a certain radius at a time
- It distracts people's attention

FACTORS TO CONSIDER WHEN CHOOSING MEANS OF COMMUNICATION

- ***Speed;*** Speed is an important factor when the message is urgent. In such a case telex, fax, telephone, telegram or e-mail would be the most suitable means of communication. Otherwise ordinary mail would be used
- ***Cost;*** The cost incurred in using a means of communication vary from one means to another e.g. it is cheaper to send messages by ordinary mail than by telegram or telex
- ***Confidentiality;*** Some messages are quite confidential and are intended for certain person only. Where confidential messages are involved, appropriate means should be used e.g. registered mail or internal memo enclosed in an envelope
- ***Distance;*** The geographical gap between the sender and recipient is very important in determining the means of communication to be used. Some means are suitable for long distances while others are not.Paging and sirens are suitable for short distances. For long distances, fax letters, telephone.g,e-mail may be appropriate
- ***Evidence,*** Some means of communication do not provide record of the message communicated while others do. All means of written communication provide evidence of messages communicated.
- ***Reliability;*** This is the assurance (certainty) that the message will reach the intended person at the right time in the right form. Face-to-face communication is more reliable than other forms of communication because one can ask for clearly and get answers immediately. For some written information, courier service may be preferred
- ***Accuracy;*** This refers to the exactness of the message communicated as intended by the sender. Written messages are generally more accurate than other means of communication.
- ***Desired impression;*** The impression created upon the recipient of a message is very important e.g. a telegram or speed post mail will carry some sence of urgency, registered mail will create an impression of confidentiality while use of colourful and attractive letterheads would convey a good image of the business.

- ***Availability;*** One may want to telephone, for example, but the services are not there so the person would be forced to use alternative means e.g. letters or radio call.

BARRIERS TO EFFECTIVE COMMUNICATION

Communication is said to be complete only when the recipient gets the message the way the sender intends it to be. When information is not received the way it was intended then it has been distorted. Distortion of a message is brought about by some communication barriers which may exists in the path of the message between the sender and the recipient. Some of these barriers are;

- ***Language used***; the language used by the sender should be known (understood) by the recipient so that communication can take place

- ***Poor Listening***; the effectiveness of communication will depend on the willingness of the recipient to listen keenly .listening require careful attention and concentration. It may however be the task of the sender of the message to attempt to gain the attention of the listener. Through his/her choice of words and expression among others.

- ***Negative Attitude***; Attitude refers to the feelings of the communicating parties towards each other. It is important that there exists a mutual feeling of trust and respect between the parties concerned in order to avoid bias .If there is mistrust and prejudice then there may be deliberate or unintentional misunderstanding of the message involved.

- ***Poor Timing*** ; poor timing leads to breakdown in communication , therefore for effective communication to take place the message must be sent and received at an appropriate time, eg a message sent when one is in a hurry may not be properly received or delivered

- ***Wrong medium*** ; the medium used to communicate must be appropriate for the message being conveyed otherwise there may breakdown in communication eg one may not convey a confidential message over the telephone effectively

- ***Prejudgment*** ; our understanding of the message is often conditional by our earlier experiences and knowledge this may make one individual draw premature conclusion eg a student who always fail in a subject and this time round has improve may be failed by the teacher because he has always failed in the past .

- ***Ambiguities*** it occurs when the sender express in a manner which leads to wrong interpretation. When the rec eiver interprets the message differently it automatically leads to communication breakdown.

- ***Emotional responses***; emotional responses such as those resulting from hunger or excitement may lead to distortion of message.

- ***Unclear System within the organization*** ; if the channel of passing information in an organization are not clear then the message will not get to the right people for whom the messages intended

- ***Noise*** it refers to any disturbing sounds which interfere with concentration or listening ability of the recipient of the message the presence of noise may make it impossible for any message to be received in the right way.
- ***Unfamiliar Non verbal signals***; lack of understanding of non verbal sign may be a barrier to effective communication.

SERVICE THAT FACILITATE COMMUNICATION

Services that facilitate communication include;

- Mailing services
- Telephone services
- Broadcasting services

Mailing services

This refers to handling of letters and parcels. They are offered by organizations such as postal corporation of Kenya (P.C.K) securicorl courier and Document handling Limited (D.H.L)

Some of the services offered by the postal corporation include;

- ***Speed post;*** This is service offered by the post office to send correspondence and parcels to a destination in the shortest time possible. The post office uses the quickest means of transport available to deliver the mail.

  The sender pays the normal postage fee plus a fee for special service. An example of such a service is *Expedited Mail Service(*EMS) speed post

- ***Ordinary Mail***

These include surface mail and air mail.

Surface Mail; These include letters and parcels delivered by road, rail, water and hand.

Air Mail; This consists of letters and light parcels delivered by air.

- ***Express Mail;***

An express mail is/must be presented at the post office counter by the sender and the envelope clearly addressed and a label with the word "*express"* affixed. Normal postage plus an extra fee (commission) is charged

The mail is delivered to the receivers nearest post office from where the post office makes arrangements to deliver the mail to the receiver within the shortest time possible.

NOTE: For speed post special arrangements to deliver the mail start at the sender's post office whereas express mail, the arrangements start at the addressers post office.

- ***Poste Restante;***This is a service offered by the post office to travelers who may wish to receive correspondence right away from their post office box. The addressee has to inform those who may wish to correspond with him/her of the nearest post office he is likely to use at a particular time

  Under this arrangement when addressing the letter, the words poste Restante must be written on the envelope clearly. The addressee must identify himself/herself when collecting the correspondence from the post office.

  There is no additional charge made apart from normal postage charges. This service can only be offered for three months in the same town

- ***Registered Mail;***

This service is offered by the post office for sending articles of value for which security handling is required. A registration fee and a commission is paid. The commission depends on the weight of the article and the nature of registration. The sender is required to draw a horizontal and a vertical line across the faces of the envelope.

A certificate of registration is given to the sender. In case of loss,the sender may be paid compensation on production of the certificate of registration.

A green card is sent to the recipient. The card bears his name and the post office at which the mail was registered. The recipient will be required to identify himself before being allowed to posses the mail.

Items that may be registered include jewels, certificate, land title deeds e.t.c.

- ***Business Reply Service;*** This is a service offered by the post office to business firms on request. The firm pays some amount to the post office and an account is then opened from which posted charges are deducted.

  The service is useful/more common with firms which would like to encourage their customers to reply their letters. Customers are issued with reply card envelopes (or envelopes marked 'postage paid')

  They can send letters to the business by using these envelopes/the card. The customers then place the card/envelope in the post box and the firms post office branch will deduct postage charges from the lump some amount.

- ***Courier Services***

These are services where a service provider receives transports and delivers parcels or important documents to destinations specified by customers in return for payment of fees or charges.

Examples; Akamba bus service, Securicor courier services e.t.c

ii)Telephone services

- Landline/fixed line services
- Cellular (mobile)phone services
- ***Land(Fixed)line services***

Telkom Kenya, through the post office, provides telephone services which offer direct contact between people who are far apart. It makes conversation between people at any distance possible, as long as there are transmission facilities between them. Urgent matters can be discussed and consultations can take place so that instant decision or actions are taken. The telephone assists organizations to establish a fast and convenient machinery for its internal and external communication network.

- ***Cellular(mobile)phone services***

These are hand held telephones with digital links that use radio waves. They are sometimes called cell-phones since they use power stored in a dry cell

In Kenya mobile phone services are provided by safaricom Ltd.(a subsidiary of Telkom Kenya)and Airtel communications Ltd(formally Kencel Communication Ltd)which is a joint venture between a French company and a Kenyan company, yu mobile services and Orange mobile services . This sector therefore greatly benefits from foreign investment to improve services.

The use of this service is popular. Apart from the provision of telecommunication service, cell phones have different attractive features or services such as short messages service (sms) whereby a caller can send a written message. Recent models of mobile phones enable the user to access the internet and send e-mail messages

Advantages

- They are portable
- Written messages can be transmitted easily and cheaply through the short message service(sms)
- Enables both local and international communication.
- The cost of acquiring the equipment is relatively affordable
- Direct feedback is possible
- Has memory for storing written messages
- Has got e-mail capability

Disadvantages

- Some kinds of mobile phones are expensive to buy

- Maintenance expenses of a mobile phone are high. They are also susceptible to damage and repair can be very costly
- Users are greatly inconvenienced in case there is no network coverage
- A special facility where the callers identity is known(displayed on screen)can be abused where recipient does not wish to answer the call
- Mobile phones are a security problem. They are easy targets for thieves
- There is a danger of the radio active rays or emissions negatively affecting the users health, if such emissions are not adequately controlled

iii) Broadcasting services

Communication commission of Kenya is a regulatory body that receives applications and issues licences for radio and television broadcasting stations.

- ***Radio stations***

Radio broadcasting is a very important mode of giving news and information to people in the whole world.

The liberalization of the communications sector in Kenya in 1999, Kenya has witnessed a mushrooming of F.m Stations which are owned by private sector operators e.g. Kiss Radio, Easy fm,Classic fm,Family fm,Kameme e.t.c

They have helped to spread news and information countrywide. Before liberalization, Kenya Broadcasting corperation (KBC) radio was operating as a state owned monopoly.

- ***Television Stations***

Television broadcasting (telecasting) does not reach as wide an audience as radio broadcasting in Kenya. It however serves the same purpose of relaying news and information to Kenyans. Both radio and television stations are widely used for advertising purposes.

The T.V subsector has been liberalized since 1999 and a number of privately owned stations have emerged e.g Kenya Television Network (KTN) Nation Television, Family T.V etc. Prior to that time KBC television was in operation as a state owned monopoly.

Other services that facilitate communication

- Telex
- Facsimile
- Paging
- E-mail

Current trends and Emerging issues in communication

With the advancement of information technology (I.T) there has been a lot of revolution in communication.

The following are some of the current trends and emerging issues in communication;

- ***Telephone Bureaux(Bureaus)***

  These are privately owned kiosks where telephone services are sold. The owner of the kiosk must get authority from the service provider in order to run the bureau. The individual wishing to use the services of the bureau makes payments to the owner of the service. Other services offered by the bureau include selling of scratch cards for mobile telephones and credit cards for landline telephone services.

- ***Mobile phones (cell phones)***

  These are hand held telephones with digital links that use radio waves. They have become an important business and social tool. This is because most people and traders want some flexibility to be able to communicate whenever they are.

  Other reasons that have led to the popularity of cell phones include:

  - Pre paid services which enable the owners to control communication costs.
  - Most cellular phones now allow the owners to browse the internet, check and send mail. This allows business people to communicate research and even place orders.
  - Cellular phones have short message services (sms) which enables the owners to send written messages.

- **E- mail (Electronic Mail)**

  This is a service provided through the internet for sending messages.

  It is similar to sending a letter through the postal system only that it is done electronically.

  -Messages can be sent to anyone on the network, anywhere in the world. For this to take place, computers have to be connected to each other to form a network.

  -To communicate, one is required to have an email address e.g raeform2 @ yahoo.com. Messages arrive at the e – mail address immediately they are sent.

  -It is only the addressee of the message who can retrieve the message since a password is required to access the mailbox.

  -E – mail can also be used to send documents and photographs like certificates by scanning and attaching.

- More and more businesses are using e- Mail to communicate with other businesses, their customers and suppliers.

*** QUESTION: OUTLINE THE ADVANTAGES OF USING E- MAIL AS A MEANS OF COMMUNICATION.**

iv) Internet

The internet links computers all over the world. Written and oral information is transmitted on the internet through the use of telephone wires, fibre- optic cables and wireless devices.

The internet has changed the way people communicate in the following ways;

- Increased use of electronic mail (e-mail)
- Quick access to information from all over the world.
- Development of home offices and remote offices.
- Use of teleconferencing and video conferencing.
- Development of e-commerce.
- **Move towards a paperless office**

The future office will rely largely on computers. Most of the communication will be done through computers. This may result in less use of paper, hence the use of the term “the paperless office”.

Vi) Decline in the use of postal services

Decline in the use of postal services is a result of the impact of the internet. E-mail has become a popular and preferred mode of communication since it is fast and cheap. However, ordinary mail/ use of postal services may not be completely phased out since the government, businesses and people do not regard an e-mail as a binding or formal communication.

Vii) Transformation of language

The language used to pass and receive messages has evolved through time.e.g the youth have adopted the use of “sheng” in exchanging messages. such language is largely understood by its youthful users. There is also the use of cell phones to send short text messages; which are highly abbreviated and may use slang whose meaning is only known to the users e.g ‘av a gr8 day’.

COMMUNICATION REVESION QUESTIONS

1. Define the term communication

-Communication is the process by which information is passed from one person or place to another.

2. Outline the role played by communication in any given organization

- It is used to give instructions on what should be done at work and during work.
- It enhances good relations among workers thereby promoting and enhancing their efficiency.
- Through communication most organizations have been able to improve their image, for example through advertising.
- It used to improve the relationship between the organization and the customer or clients.
- For co-ordinating purposes, communication is used to ensure all departments work in harmony.
- The feedback got from the clients or customers helps to improve an organization's reliability and quality of goods and services offered.
- Communication is used as a tool for management.
- Good decisions are made as communication helps one understand all the necessary matters.

3. Briefly explain the following levels of communication

(a) Vertical communication

Involves the flow of information either downwards or upwards, for example, from a senior employee to a junior employee

(b) Horizontal communication

Is also referred to as lateral communication which is passing of information between people of the same rank or status, for example from one departmental manager to another departmental manager

(c) Diagonal communication

Is communication of different people in different levels of management or departments for example a receptionist communicating to a production manager.

4. Distinguish between formal and informal communication

Formal communication is official and documented and follows certain rules for example a worker writing an official letter to an organization's seniors. Informal communication does not conform to any time, for example communicating to friends and relatives.

5. State the essential elements in communication.

- The sender who is the source of the information being communicated
- The receiver(or recipient) of information
- The message being communicated
- The channel (or medium) through which the message is passed on

- Feedback which is the response or reaction of the recipient.

6. Highlight the various types of verbal communication

- Face-to-face communication
- Telephone conversation
- Radio calls conversation.

7. State the advantages and disadvantages of verbal communication

Advantages

- A large number of people can receive the information at once for example when addressing in a meeting.
- There is immediate feedback
- Clarification can be made easily and immediately
- This is personal appeal
- It can be very convenient and persuasive
- It is fast since the intended information reaches the recipient immediately.

Disadvantages

- It is not easy to know if the message or information has been received particularly if the receivers are many
- It is prone to outside interference due to noise and other forms of disruptions
- In case of incorrect pronunciation of words, there could be distortion of the information
- There is no record for future reference.
- The method is not effective for recipients with learning problems.
- Can take a lot of time to pass intended information.

8. Outline the various barriers to effective communication

- Noise may hinder effective communication
- The emotional state of both the sender and the recipient
- Use of the wrong channel to communicate
- Breakdown of a channel used to communicate

- Illiteracy of the recipient particularly for written communication.
- The attitude of the recipient towards the sender and the information being communicated
- Use of difficult vocabulary or words by the sender
- Lack of concentration on the part of the recipient may affect communication
- Poor timing by the sender.

9. Highlight reasons that would make an organization use cell phones for communication within and outside the organization.

- One gets immediate feedback
- It is fast and can be used to send urgent messages
- There is personal appeal
- The sender has a great opportunity to convince and persuade the recipient.
- It is not very expensive particularly for making calls for a short duration of time
- It can be used even when both the sender and the recipient are far apart

10. State the various types of written communication.

- Written
- Memorandum(memos)
- Reports
- Notices
- Telegrams
- Circulars
- Minutes

11. State the reasons why an organization would use written communication instead of verbal communication.

- Written communication provides evidence which may not be there in verbal communication
- Written information can be stored for future reference unlike verbal which cannot be stored and depends on the recipients memory
- It is not prone to distortions and therefore more accurate than verbal communication

- Written communication can be in form of diagrams, illustration and maps which is not possible for verbal communication
- Some written communication such as letters would be cheaper and time saving than verbal communication, for example making long telephone calls.
- Written communication can be used for confidential messages, for example registered mails.

12. State the disadvantages of written communication

- Written is not very persuasive or convincing
- There is no personal touch
- It can only be used by literate
- It can be slow where letters take time to reach the recipient
- It takes time to get a feedback from the recipient
- Messages cannot be enhanced by gestures, that is, body language or face expressions
- It can be expense to file all the written communication

13. Outline the various means of visual communication

- Charts
- Photographs
- Gestures, which may include signs and symbols
- Slides

14. State the advantages and disadvantages of audio-visual of communication

Advantages

- Information is more attractive and appealing
- Can reach many people at once
- It can be used even for those who cannot read and write
- Immediate feedback is received from the way the recipient behave
- Can be entertaining

Disadvantages

- Can be misinterpreted, for example if the receiver does not understand the signs or gesture
- Not suitable for passing confidential information

- It is not possible for the recipient to give a feedback
- Gesture and signs are only suitable to those who can understand them
- The initial cost of preparing these forms of communication may be high for the sender
- It may take a lot of time to prepare these forms of communication

15. Outline the various service that facilitate communication

- Registered mail, for sending valuable or confidential information.
- Speed post services offered by the post office to send letters parcels using the quickest means possible
- Poste restante, usually used by those without postal addresses
- Business reply service which enables customers and clients to reply to a business without having to pay for postage stamps
- Broadcasting services through various radio stations
- Print media such as the various newspapers, magazines and journals
- Internet services which connect one to the world wide website
- Telephone services

16. State the various trends in communication

- Mobile or cell phone use
- Internet which uses inter linked computers to the world wide website
- Fax, which can be used to send written messages very fast
- Information and telephone bureaus where one can make local and international calls
- Move towards a paperless office.
- Transformation of language.

17. Highlight the factors to be considered when choosing a means of communication.

- The cost because some are more expensive than others
- Availability of the means
- Reliability or assurance that the message will reach the recipient
- The distance between the sender and the recipient.
- The literacy level of both the receiver and the recipient

- The confidential nature of the information being sent
- The urgency of the message
- If there is need for evidence or need for future reference
- The desired impact of the means upon the recipient.

18. Advice Mary Wakio why she should not use telex to communicate to her friends

- Her friends may be illiterate and may be unable to read the message received
- Her friends may not have a receiving machine and will be unable to get the information
- It can be expensive to use as the sender pays a subscription fee and rental fee while he and the recipient pays for the sent message
- It can be expensive to buy the teleprinters used in receiving and sending information
- Telex may only send written messages but cannot be used to send maps, diagrams and charts

19. State circumstances when sign language can be the most appropriate form of communication

- When communicating to someone who has a hearing problem
- If one wishes to pass a secret or coded message
- If both the receiver and the sender are far apart but can see each other
- It can be used in case there is a language barrier
- In an environmental where there is a lot of noise or physical interference to other forms of communication, sign language may be used
- It can be appropriate where both the recipient and the sender understand the signs.

20. Explain four factors that have led to the popularity of mobile phones as a means of communication.

TOPIC 3:

TRANSPORT

TOPIC OBJECTIVES

By the end of the lesson, the learner should be able to:

- Explain the meaning and importance of transport to business.
- Explain the essential elements of transport.
- Describe the modes and means of transport.
- Discuss the advantages and disadvantages of each means of transport.
- Discuss the factors that influence choice of appropriate means of transport.
- Discuss trends of transport.

MEANING OF TRANSPORT

Transport is the physical movement of people and goods from one place to another. It helps bridge the gap between producers and consumers hence creating **place utility.**

Importance of Transport to Business

- ***Bridging the gap between producers and consumers/ linking consumers to producers-***Transport links consumers to producers which enable the consumers to obtain the goods they need.

- ***Employment creation-***Transport helps in solving unemployment problem by creating job opportunities. For example, people may be employed as drivers, pilots, mechanics and road constructors.
- ***Promotes specialization-***Transport enables people to specialize in jobs they are best at. For example; producers would concentrate in production only while other people carry out distribution.
- ***Making goods and services more useful-***Through transport goods are moved from a place where they are least required to a place where they are most required thereby making them more useful.
- ***Improving people's standard of living-***It enables consumers to get a variety of goods and services thereby improving the standards of living.
- ***Availing a wide market for products-***It helps producers to widen the markets for their products by enabling them access to areas they would otherwise not have accessed
- ***Increased production/ facilitates mass production-***Due to the wider market created through transport, producers are able to increase the volume of goods produced.
- ***Avoiding wastage-***Transport makes it possible for surplus goods to be disposed of by taking them to areas where they are required. Perishable goods such as flowers, fruits and vegetables can also be transported fast hence minimizing/ avoiding wastage.
- ***Promoting development of industries-***Through transport, raw materials can be taken to manufacturing industries and also finished goods to the market. Similarly, it promotes development of service industries such as tourism.
- ***Adds value to goods and services-*** creates utility in goods by moving them from the point of production to where they are needed thereby adding their value.
- ***Leads to the opening of new markets-*** Goods and services can be taken to new areas with ease.
- ***It facilitates the movement of labour-*** people can easily move from where they stay to where they work

ESSENTIAL ELEMENTS OF TRANSPORT

In order for a transport system to function efficiently it should have certain basic elements. These elements are:

- **Unit(S) of carriage**
- **Methods of propulsion**
- **Ways**
- **Terminals(terminus)**

Unit(S) of carriage

This refers to anything i.e. vessel that is used to transport goods and people from one place to another. Units of carriage include: ships, trains, aeroplanes, motor vehicles, bicycles and carts. Units of carriage are also referred to as means of transport**.**

Methods of propulsion

This is the driving force (source of power) that makes a unit of carriage to move.The power for most vessels may be petroleum products, electricity, human force or animal power.

Ways

It refers to either the route or path passes by the vessel. The route can be on land, on water or through air. Examples of ways are roads, railways, paths, canals, seaways and airways. The ways can be classified into either natural ways or manmade ways.

- **Natural ways-**As the name suggests, natural ways are the ways that are provided by nature. They are therefore free to acquire. They include airways and seaways**.**
- **Man-made ways-These are ways that are made available by human being. They include roads, canals and railways. Manmade ways are usually expensive to construct and maintain.**

Terminals (terminuses)

The vessel used to carry goods and people starts from one destination and ends up at another. At these destinations the loading and off-loading take place respectively. The loading and off-loading places are referred to as terminals or terminus. Examples of terminuses are bus stations, airports and seaports**.**

MODES OF TRANSPORT

Mode refers to the manner in which transport is carried out. There are three modes of transport namely**:**

- **Land transport**
- **Water transport**
- **Air transport**

Land transport

This mode of transport involves movement of goods and people using units of carriage that move on dry land. The various means under this mode includes:

- **Human Porterage**

This involves human beings carrying goods on their heads, shoulders or backs. Human Porterage as a means of transport is the oldest kind of transport and is still very common in our society. The means is suitable for transporting light luggage over short distances. It is also appropriate where other means of transport are not available or convenient.

Advantages of Human Porterage

- Could be the only means of transport available
- Compliments other means of transport
- Flexible as it has no fixed time table or routes
- May be a cheap means compared to other means of transport
- Readily available when required
- Convenient over short distances

Disadvantages of human Porterage

- Not suitable for long distances
- They add onto congestion on roads
- Not suitable for transporting heavy and bulky goods
- It is relatively slow
- Relies on human energy which is exhaustible

Carts

Carts are open vessels usually on two or four wheels that are pushed or pulled by either human being or animals such as oxen and donkeys. The carts pushed or pulled by human beings are referred to as hand carts or mikokoteni. The ones pulled by animals, on the other hand, are called animal driven carts. Carts are used to carry relatively large quantities compared to human porterage. Like human porterage, they are not suitable for long distances. Types of goods that are transported using this means include, agricultural produce, water and animal feeds**.**

Advantages of carts

- Compliments other means of transport
- Relatively cheap to hire
- Initial buying and maintenance cost is low
- Appropriate in remote areas where other means are not available
- Readily available for hire
- Can carry fairly heavier and bulky goods
- Convenient for transporting goods over short distances

Disadvantages of carts

- May not be suitable for transporting heavy and bulky goods
- Cause traffic jams on roads leading to congestion and accidents
- Not suitable for transporting goods over long distances

Vehicles

These are means (units of carriage) of transport that ferry goods and people on roads. Vehicles are the most commonly used means of transport.

Vehicles are either passenger or goods carriers. Passenger carriers may be buses, matatus, taxis and private cars while goods are transported using Lorries, pick-ups, tankers and trailers. Vehicles are expensive to acquire and maintain. The convenience of vehicles may depend on the nature of the road on which they travel.

Some roads are impassible especially when it rains while others are usable throughout the year (all weather roads).Of special concern in road transport is the matatus. These are privately owned passenger vehicles which were introduced to supplement the existing mainstream transport companies that were inadequate at independence. They got their name from the amount of fare they used to charge originally that is, mapeni matatu. The operators have to obtain the relevant documents such as insurance cover in order to be allowed to operate. Their owners may form associations which take care of their interests along given routes or in certain areas**.**

Advantages of matatus

- They supplement regular bus companies, especially in remote areas where they are the only means.
- They fill up faster than buses hence save time
- They are more flexible since they can change routes easily depending on demand
- They reach out into the interior of rural areas where big buses cannot access
- They are more flexible with the fares they charge
- They are easier to hire as most of them are readily available
- They are cheaper to acquire as compared to buses

Disadvantages of matatus

- Some Matatus are poorly maintained to the extent of being roadworthy
- Most drivers are reckless as they rush to compete for customers. They pick or drop passengers anywhere
- In some cases, touts use impolite language when dealing with passengers
- They may cause noise pollution such as unnecessary hooting and loud music

- They may cause congestion in towns unnecessarily because of careless driving and parking
- Uncalled for sudden increase in fares at peak hours, during the night and on public holidays
- Their operation is concentrated on peak hours, rarely operating at night.
- They at times unexpectedly change their route hence causing breach of contract**.**

Advantages of vehicles

- Most readily available means of transport
- Relatively fast compared to carts and human Porterage
- Relatively cheaper over short distances
- Flexible as it can offer door to door service
- Vehicles may be available for transporting special goods
- Roads are widely spread thereby making many areas accessible.

Disadvantages of vehicles

- Acquisition and maintenance costs are high
- May not be suitable for transporting heavy and bulky goods over long distances as compared to railways
- Traffic jams in roads may cause delays
- Vehicle transport is prone to accidents which may lead to loss of goods and life
- Some roads may be impassible especially during the rainy seasons.

Trains

Trains are vessels that transport goods and people on rails hence the term railways.

The terminuses of trains are the railways stations. Therefore; the goods to be transported by trains have to be taken to the railway station. Railway transport is suitable for heavy and bulky goods as well as passengers. There are two types of trains: *cargo and passenger train.*

Advantages of Trains

- Relatively secure as cases of theft and accidents are rare
- Enables a transporter to plan for the transport of his/her goods as trains follow a fixed time table
- Economical for transporting heavy and bulky goods over a long distance

- Trains may have facilities for carrying special types of goods e.g. gas, petrol and vehicles
- Where shunting facilities are available trains may deliver goods up to or from the owner's premises

Disadvantages of Trains

- Not flexible as trains follow a strict time table
- Railway lines are expensive to construct and to maintain
- Not all areas are served by railway lines
- Not suitable for transporting urgently required or perishable goods as it is slow
- Unsuitable for transporting goods over short distances
- Trains are expensive to acquire and maintain

Pipeline Transport

This is the movement of liquids and gases from one place to another through a pipe. Products transported through pipes include water, gases, petrol and diesel. Solids that cannot be dissolved or damaged by water may also be transported through pipes as suspension. Examples coffee berries from machines to drying places. The pipeline is both a vessel and a way.

Products flow by the force of gravity or pressure from an original station. If the original terminal is at a higher level than the receiving terminal, the force of gravity is adequate to move the product. But if the receiving terminal is at a higher level than the original than the originating terminal, then power is required to pump the product uphill. For example, petroleum from Mombasa which is at sea level needs pressure to pump it to all the receiving stations**.**

Advantages of pipeline Transport

- It is labour saving as it requires minimal manpower
- It is environmentally friendly since it is free of noise or smoke
- It may be constructed in areas where it is difficult to construct roads or railway lines. For example, over rugged terrain
- Pipelines allow continuous flow of the goods being transported
- It ensures that road damage is reduced as the number of tankers is reduced on roads
- It helps to reduce accidents that may be caused by tankers on roads
- It reduces delays arising from congestion on roads
- Maintenance costs are reduced as it relies on gravitational force and booster stations along the way

- It may not be affected by adverse weather conditions

Disadvantages of pipeline Transport

- A leakage not detected in good time may lead to high losses
- Initial construction cost is high
- Accidents leakages may lead to environmental pollution
- It is unidirectional that is, travels only in one direction
- It can transport only one product at a time
- It is not flexible since once a line is laid, it cannot be adjusted according to transport patterns or demands
- Generates comparatively fewer job opportunities as it is capital intensive
- It is vulnerable to sabotage by enemies**.**
- Once laid, it is difficult to re route or re locate.

Water Transport

It is a mode of transport where the units of carriage transport goods and people on water. Water in this case includes; navigable rivers, lakes, seas and oceans. The means of transport which are the units of carriage or vessels using this mode include; ships, dhows, boats, steamers and ferries. Water transport can be divided into inland waterways and sea transport.

Inland waterways

This is transport carried out on lakes, rivers and inland canals. The Lake Victoria facilitates transport among the three east African countries i.e. Kenya, Uganda and Tanzania. Ferries also connect the mainland to islands such as Rusinga Islands, found in Lake Victoria.

Water hyacinth has however been a threat to transport on the lake. Most rivers in Kenya are not navigable due to reasons such as:

- Too small
- Presence of rapids and waterfalls
- Too shallow
- Most are seasonal
- High gradient

Sea Transport

This is where goods and people are transported in seas and oceans. All types of water vessels may be used in sea transport. Sea transport is important as it connects continents of the world thereby facilitating international trade. Kilindini in Mombasa

provides a good natural harbor facilitating sea transport between Kenya and other countries of the world. Ferries also connect the island of Mombasa and the mainland.

Types of Water vessels

- **Ships**

A ship is a large vessel that transports people or goods through water. Their sizes however vary depending on quantity of goods and passengers they carry. Ships help in connecting countries or places which borders the sea. They load and offload in terminals referred to as *harbors* found at sea ports. For example, the Kilindini harbor is found in the port of Mombasa.

Ships that transport people are referred to as *passenger ship* while those that transport goods are referred to as *cargo ships.* Cargo ships are c are convenient for carrying heavy and bulky goods.

Ships may also be classified as either liners or tramps.

Liners

These are ships that are owned and operated by shipping companies called *conferences*. Each conference is responsible for specifying the route on which each liner would operate the rates to be charged and setting the rules and regulations to be followed by the members.

Characteristics of liners

- Have fixed routes
- Follow a fixed time table
- Charges are fixed
- Call at specified ports along the route at specified intervals
- Travel at regular intervals

Tramps

These are ships that do not follow a regular route or time table. Their routes therefore depend on demand. During times when demand is high, they charge higher rates and when demand is low they lower their rates. Tramps can therefore be likened to matatus. Tramps may be owned by either individuals or firms**.**

Characteristics of tramps

- Do not have a fixed rate. They therefore move to wherever there are goods or passengers to carry.
- Have no set time tables. They therefore move according to demand
- Their fares change according to demand.
- Their travelling patterns are irregular and therefore cannot be relied upon

NB: Liners and tramps owners are in constant competition business. Traders therefore need to choose the type of ships to hire. Liners are however more popular than tramps among traders because of their reliability.

When a trader hires an entire ship to transport goods to a given destination, he/she and the ship owner signs a document called a ***charter party***. This document shows the terms and conditions under which the goods would be transported.

Other information included in the agreement are destination, nature of the goods and freight charges. When the ship is hired to carry goods for a given journey the document signed is referred to as ***voyage charter***. On the other hand, if the ship is hired to transport goods for a given period of time, the document signed is called ***time charter***.

Ships may be specially built to carry special commodities. These may include tankers specially built to transport petroleum products and other liquids. Refrigerated ships may also be available to transport perishable commodities such as meat, fish and fruits.

- ***Boats and Ferries***

These are water vessels used in transporting goods and people over short distances. They are therefore found in both inland water transport and also the sea transport e.g. the Likoni ferry in Mombasa carries people from and to the island of Mombasa and the main land.

Advantages of water transport

- Sea transport is economical to the owner as the number of employees to carriage volume ratio is less compared to road transport
- Suited for transporting heavy and bulky goods
- It is cheap as the way is natural and free
- Connects countries of the world which border the sea
- Special types of ships are available for transporting goods
- Large volume can be carried thereby reducing cost per unit
- Not affected by traffic congestion.
- Some ships can be very luxurious for passengers and may even provide swimming pools.
- At the port/dock, there are many depots for storage of goods.

Disadvantages of water transport

- Sea-sickness, sea-pirates and storms may occur
- They are slow therefore not suitable for transporting perishable and urgently required goods
- It is expensive to construct and maintain artificial harbors

- Unfavorable weather conditions may affect water transport
- Sea transport is not accessible to land locked countries
- Lack of loading and off-loading facilities may lead to delay
- Cost of acquiring and maintaining ships is high.
- Theft of cargo and other valuables may occur during loading and offloading.
- **Air Transport**

This refers to the movement of goods, people and documents by aircrafts. Aircrafts/ aeroplanes are the units of carriage and air the way. The terminals include airports and airstrips.

Aeroplanes are fast compared to other means of transport i.e. they are the fastest means of transport. They are therefore suitable for transporting urgently required goods like drugs and perishable goods Such as flowers over long distances.

Aircrafts may be classified as either **passenger planes** or **cargo planes**. Passenger planes transport people from one place to another. On the other hand, cargo planes transport light cargo to the required destinations. Aeroplanes may be fitted with special facilities for handling special goods. Aeroplanes are expensive to acquire and to maintain. Their operations may also be affected by weather conditions**.**

Advantages of Air Transport

- There is less handling of goods on the way since aeroplanes may move direct to the final destinations.
- The way does not require construction or maintenance as it is natural and free.
- Planes can move through places where other means cannot, such as over the earth poles and across high mountains/ planes are not hampered by physical barriers.
- Have efficient interconnections between airlines all over the world which makes it convenient
- Suitable for long distance travelers especially from one continent to another
- Very fast therefore suitable for transporting perishable and urgently required goods.
- Chartered planes can be used to reach remote areas.
- The movement of aircrafts is smooth therefore suitable for transporting fragile goods such as glassware and eggs.
- Passengers are given the highest degree of comfort and personal attention making it the most comfortable means of transport.

Disadvantages of Air Transport

- Causes noise pollution

- Air fields are not available in all places
- Cannot be conveniently used to carry heavy and bulky goods
- Expensive to acquire and maintain aircrafts
- Requires highly trained manpower e.g. air traffic controllers, pilots e. t. c
- Unfavorable weather conditions such as fog, mist and heavy rains smay cause delay
- It is an expensive means of transport in terms of freight charges
- Not suitable for transporting inflammable goods such as cooking gas and petrol
- In case of accidents results are catastrophic/ accidents are rare but fatal.
- Has limited carrying capacity which should not be exceeded.
- It is not flexible.
- Most air fields/ terminals are located some distance away from town/ city centers and therefore require transport or railway links that are affected by jams occasionally causing delays.
- Recent hijackings by terrorists have made air transport an insecure means especially for transporting valuables.

Containerization

This is a recent development in transport. It refers to the packaging of goods in standardized 'box like' containers designed for use in transporting cargo. The containers are mainly made of metal though a few are made of wood. They can either be hired or bought from firms that provide them. The hired containers are returnable to the owner after the goods have been transported.

Containers are designed in a way appropriate to transport goods by ships, train, lorry or by air. To safeguard the goods against risks such as theft and unfavorable weather conditions the containers are sealed immediately after goods have been packed. The sealed containers are then transported up to the final destination where they are off-loaded. The consignee can then break the seal.

Goods can be transported in containers as **Full Container Load (F.C.L)** or as **Less Container Load (L.C.L**).Full container load applies where the container is filled with goods belonging to one person. In FCL, goods are delivered to the consignee intact. On the other hand, less than container load applies where a container is filled with goods belonging to several consignors. This may be the case where a single consigner does not have enough goods to fill a container. When such a container reaches the destination, it is opened and the various consignees take their goods.

There are special handling facilities for loading and offloading containers onto and from the units of carriage.

Apart from the container depot at Mombasa, Kenya Ports Authority (K.P.A) has established inland container depots referred *dry ports.* An example of a dry port is

found at Embakasi in Nairobi. The establishment of dry ports aims at relieving congestion at the sea port. It also aims at making handling of cargo easier and efficient for inland importers and exporters.

When containers are off loaded from ships at Mombasa, they are loaded into special container trains called *railtainer* which transports them by railway to the inland container depot at Embakasi. Containers can also be transported by specially designed trucks between the ports or from the port to consumer's destination.

Advantages of containerization

- Minimizes the risks of loss or damage of goods as containers are sealed at source
- Containers are lifted with devices which make movement and handling easy
- Saves time and labour in loading and off-loading due to use of machines
- Containers sealed at source in presence of customs officials may not be opened until they reach their final destination. This reduces delay.
- Special containers are available for goods requiring special attention like chemicals.
- Insurance costs are relatively low as risks are less
- Space is saved when containers are used as opposed to when individual items are packed in the carrier.
- Can carry large quantities of cargo if packed well.
- Containers are tough structure, which offer protection to sensitive and fragile goods.

Disadvantages of containerization

- They are expensive and this increases the cost of transporting goods
- Contributes to unemployment since it is capital intensive
- Not suitable for transporting small quantities of goods.
- Requires special handling equipment which may be expensive
- May not be suitable for goods with irregular shapes.
- Training labour force is long and expensive.
- They may be used to smuggle illegal goods.
- The large trucks used on the road increase road damage and may increase accidents.

Factors that influence the choice of appropriate means of transport

- ***Cost;*** The cost of transporting a good should be reasonable; except where other factors should be considered such as need for quick delivery. Otherwise should be proportional to the value of goods transported.
- ***Nature of goods;*** The nature of goods should be considered when choosing a means of transport. For example, perishable goods require a fast means. Similarly, heavy and bulky goods require a means of transport convenient for such goods e.g. trains and ship.
- ***Reliability;*** The means chosen should be able to deliver the goods to the required place at the right time and in the right form.
- ***Urgency;*** For goods that are urgently required, the fastest means available should be chosen**.**
- ***Safety and Security;*** The means chosen should ensure that the goods on transit are secure against loss, theft or physical damages.
- ***Distance;*** Some means of transport are suitable for long distances while others are suitable for short distances. If goods are to be transported for long distances, air, sea or railway transport would be appropriate, otherwise roads would be suitable for short distances.
- ***Availability of means;*** The means of transport to be selected should be based on its availability. For example, where there is only one means of transport, it would be the only one to be chosen**.**
- ***Flexibility;*** This is the ability of means of transport to be manipulated to suit the convenience of the transporter. Where flexibility is required, then the means that would provide such should be chosen. For example a matatu is usually more flexible than an aeroplane**.**
- ***Terminals;*** Some means of transport may have their terminals near the transporter than others. In this case, the transporter should choose the means whose terminals are conveniently accessible to facilitate loading and offloading of goods.
- **Value of goods to be transported-** goods of high value require special handling and high security during transportation.

<u>Trends in transport</u>

- Pipeline and containerization
- Electric trains are replacing diesel engines
- Underground tunnels for trains are being used to ease congestion on the surface
- Dual-carriage roads are being developed in various parts to ease congestion and minimize accidents
- Development of planes with larger carrying capacity and speed is a major feature in the transport industry

- Use of bicycles commonly known as bodaboda are a common feature in towns, bus terminals and rural areas, supplementing other means of transport to ferry people and cargo to their destinations. The bicycles are being modified to make them more convenient. It is not unusual to find a bicycle (bodaboda) which has been fitted with facilities such as:
    - Motors to increase their speed and reduce energy applied by the cyclist.
    - Music systems to entertain passengers and More comfortable seats.

  Motor cycles are also being used as *bodabodas* in various areas. Similarly, the three wheeled vehicles commonly known as 'Tuk Tuk' is a major feature in cities and most towns.

- Private personal vehicles with less carrying capacity e.g. four-seater vehicles are being used as matatus. The vehicles are convenient to the passengers as they:
    - Fill up within a shorter time compared to larger vehicles
    - May accommodate each of the customers interests.
    - Passenger vehicles are being fitted with radios, music systems and videos to entertain customers as they travel. However, some forms of entertainment may not be conducive to all.

END.

REVISION QUESTIONS ON TRANSPORT

KCSE PAST PAER 1

- 1996 State four circumstances under which a businessman would choose to transport goods by air? (4mks).
- 1997 Outline four reasons why a school in Kisumu may prefer to transport its sixty students to a music festival in Nairobi by train rather than by bus. (4mks).
- 1999 Give five reasons why a manufacturing firm would be located in an area well served by good road network.(4mks).
- 1999 Outline four limitations of containerization. (4mks).
- 2000 State four reasons why road transport is popular in Kenya.(4mks).

- 2001 State four ways in which the nature of goods would influence the choice of transport.
- 2002 Outline four reasons why a transporter of goods from Mombassa to Nairobi may prefer rail transport to road transport. (4mks).
- 2003 State the unit of carriage for each of the following modes of transport. (5mks)

  Mode of transport Units of carriage

  - Portage
  - Sea
  - Road
  - Cartage
  - Air
- 2004 list four ways in which transport promotes growth of trade. (4mks)
- 2000 State four reasons why road transport is popular in Kenya. (4mks)
- 1995 Give 3 disadvantages of railway transport in Kenya. (4mks)
- 1998 List 4 disadvantages of using containers to transport goods. (4mks)

KCSE PAST QUESTIONS PAPER 2

- 1995 Explain five reasons that may account for continued use of hand carts as a mode of transport in Kenya. (12mks)
- 1996 The oil pipeline has recently been extended from Nairobi to western Kenya.
- Explain five benefits that may be accounted to the country from the extension. (10mks).
- 1997 Explain five ways in which an efficient road transport system may promote trade within a country.(10mks).
- 1998 Discuss five factors that have hindered the expansion of railway transport in Kenya.
- 1999 Explain five features of an efficient transport system (8mks).
- 2000 Explain the advantages of pipeline as a mode of transporting oil products. (12mks).
- 2002 Outline five factors that should be considered when choosing a means of transport.
- 2003 Explain six advantages of containerization as a mode of transport. (10mks)

- 2004 Discuss six factors that may discourage the use of pipeline as a means of transporting petroleum products in a country.(12mks).
- 2005 Discuss 5 circumstances under which a trader may choose to transport goods by rail.

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TOPIC 5

WAREHOUSING

Warehouse; This is a building or a part of a building where goods are received and stored until need arises for them.

-Other terms used to refer to a warehouse are *depot, a go down or a silo.*

Warehousing; This is the process of receiving goods into a warehouse, protecting such goods against all types of hazards and releasing them to users when need arises for them

-There are three distinct stages in warehousing process namely:

- Receiving goods into a warehouse
- Storing them
- Releasing them to users

Importance of warehousing to Business

- ***Steady/continuous flow of goods;*** Producers can produce and store goods awaiting demand through warehousing e.g. agricultural products that are produced seasonally are made available throughout the year
- ***Stability in prices;*** Warehousing ensures that there is no surplus or shortage of goods. It ensures that goods are stored when in plenty and released to the market as their need arises. This helps to keep their prices fairly stable
- ***Security;*** Warehousing ensures that goods are protected against physical damage and adverse weather conditions. This also ensures that the quality of the goods is maintained until they are demanded. Goods are also protected from loss through pilferage and theft.
- ***Bridging the time lay/difference between production and consumption;*** many goods are produced in anticipation of demand. Such goods must be stored until their demand arises e.g. gumboots, umbrellas and sports equipment are needed seasonally but are manufactured in advance and stored in a warehouse so as to be released to the users when need arises for them.
- ***Continuous/uninterrupted production schedules;*** Manufactures are able to buy raw materials in large quantities and store them awaiting their need to arise. This prevents interruption of the production process because of lack of raw materials
- ***Preparation of goods for sale;*** While in the warehouse, goods can be prepared for sale e.g. they can be blended, packed, graded or sorted out.
- ***Sale of goods;*** Goods may be sold while still in the warehouse. If sold while still in a bonded warehouse, duty passes to the buyer
- ***Specialization;*** Warehousing encourages specialization in production and distribution. Producers concentrate on producing while distributors store the goods for sale to the customers.
- ***Unexpected demand can be met;*** The government collects agricultural goods e.g. cereals and stores them as buffer stocks to be used in times of disaster or serious shortages.
- ***Clearance of goods;*** Warehousing helps in clearance of goods i.e. goods entering the country can be inspected by the customs officials.

- Warehousing helps to improve the quality of goods e.g. goods like tobacco and wine mature with time.
- Warehousing enables buyers to inspect the goods before they buy them.
- Wholesale warehouses may also operate as showrooms for traders.

Essentials of a warehouse

These are the features and resources a warehouse should have in order for it to function effectively.

These include;

- ***Ideal location;*** A warehouse should be located at a suitable place to facilitate receipt and issue of goods e.g. a manufactures warehouse should be located near his/her factory.
- ***Proper building;*** A warehouse should have proper buildings which are suitable for different types of goods to be stored.
- ***Equipment;*** A warehouse should be equipped with appropriate facilities for handling goods such as fork-lifts conveyer belts e.t.c.It should also be well equipped with necessary storage facilities e.g. provision of refrigerated or cold storage for perishable goods such as meat and fruits.
- ***Accessibility;*** A warehouse should be accessible to its users. It should therefore be linked with good and appropriate transport system to facilitate movement of goods in and out of the warehouse.
- ***Safety and security;*** It should have/be fitted with safety equipment or facilities necessary for protection of goods against damaged caused by such things like water, fire or sunshine as well as for the protection of the personnel.
- ***Communication;*** A warehouse should have a good communication network or system for easy contact with its clients and suppliers
- ***Qualified personnel;*** A warehouse should have well trained and efficient staff/personnel for proper management and efficient functioning of the warehouse.
- ***Recording system;*** There should be a proper recording system in a warehouse to ensure that all movement of goods is properly monitored.
- A warehouse should be spacious enough to allow easy movement and accumulation of goods and personnel.

Types of warehouses

Warehouses can be broadly classified into three namely:

- Private warehouses
- Public warehouses
- Bonded warehoused

Private warehouses

These are warehouses that are owned by private individuals/organizations for the purpose of storing their own goods only. They include;

- Wholesalers warehouses
- Producers warehouses
- Retailer's warehouses.

a) Wholesalers warehouses

These are warehouses for storing the wholesalers' goods as they await distribution or sale. They need warehouses because they buy goods in bulk from producers and store them until they are needed by retailers.

-The wholesalers warehouses also act as showrooms i.e. they display their goods in the warehouse.

-These warehouses also enable the wholesalers to prepare their goods for sale e.g. branding, blending, packing and sorting may be carried out in the warehouse

b) **Producers warehouse**s;

-These warehouses are owned by producers and they are for storing goods prior to their demand.

-The producers may be manufactures of finished goods or farmers

-Such warehouses are built near the manufactures factories or the farmers production points.

-Manufactures who export may locate some warehouses near ports through which they export e.g Mumias sugar warehouse, Bamburi Portland cement warehouse e.t.c

c) **Retailers warehouses**

Some large-retailers such as chain stores and supermarkets own warehouses for storing their large stores

-It becomes necessary for such business to have warehousing facilities due to their large and bulky purchases dictated by the nature of their business

-Goods are distributed from their warehouses to the retail outlets or to the branches

Advantages of private warehouses

- The owner has full control over its operation and may make major decisions without having to consult anyone.
- The warehouse is designed to suit the specific needs of the organizations

- It enables special handling, storage and protection of goods by having special facilities which may not be available in a public warehouse
- The owner is not tied down by procedures of receiving and issuing goods unlike in public warehouse.
- The owner does not incur the cost of hiring space unlike with a public warehouse
- The operation can be easily automated because the goods to be received stored and dispatched are already known.

Disadvantages of private warehouses

- The initial construction cost of a warehouse is high
- Under-utilization of personnel and facilities may occur especially in times of low volumes
- They may not employ qualified management personnel and are consequently disadvantaged in dealing with management problem.
- Risks arising from dangers such as fire,pests,theft or damage are not spread

Public warehouses

These are warehouses owned by individuals or organizations who do business by renting space. To those traders who are in need of storage facilities to store goods temporarily. They have the following characteristics;

- Are owned and operated by individuals or companies who do not use them for storing their own goods.
- Are open to any member of the public who wish to rent storing space for their goods
- The customers pay on the basis of space rented and the period of time required to store the goods.
- They are often situated near terminals as airports, sea-ports and railway station and industrial areas. This facilitates the movement of goods in and out of the warehouse.
- The rent paid includes charges for insurance and other services i.e. goods are insured against loss or damage as a result of fire or theft while they are still in the warehouse.
- They provide other services apart from storing the goods e.g. grading,packaging,preparing export samples, preparing market reports and clerical documents
- Imported goods can be sold while they are still in the public warehouse. If such a transaction takes place the goods may change ownership without being physically moved out of the warehouse. This becomes possible if the importer has signed a document called ‘**a warehouse-warrant’** (which is a negotiable

instrument out of order), it is issued by the new owner after the transaction has taken place.

Advantages of a public warehouses

- A public warehouse serves a number of customers that deal with the same product. It assembles the small orders from these customers and places one order for all of them. This enables them to enjoy economies of large scale buying and delivery of goods to a warehouse.
- Goods stored in a public warehouse may be sold without their physical movement from the warehouse.
- Traders can rent space to store their goods
- Traders do not have to construct their own warehouses/do not have to tie up capital in storage buildings and handling equipment.
- Goods are insured against risks such as damage by fire and theft
- A trader may get a short term loan from the warehousing firm by using the goods held as collateral security.
- Apart from the handling, sorting and documentation of goods additional services such as bottling, bagging and repairs of damaged goods can be offered by public warehouses.
- Sharing equipment and machinery enables the users to reduce handling costs
- Inspection, re-packaging and labeling services provide users of public warehouses the expertise they themselves may not have.

Disadvantages of public warehouses

- The hirer is denied the opportunity to physically handle the goods and is forced to compete for attention with other hirers of the warehouse. If the hirer had his/her own warehouse, he/she would have absolute authority on the goods and therefore enjoy individual attention.
- The hirer may lose contact with his/her customers since they get goods from a rented warehouse, away from the hirers premises
- The hirer may get poor services or miss space altogether during peak seasons due to stiff competition for the same facility.
- Documentation involving receipt and release of goods in a public warehouse is likely to be a long and complicated procedure due to the large number of clients involved.
- Continued renting of space can even be more expensive than constructing one’s own warehouse in the long run
- Public warehouses are sometimes situated far away from the hirer’s premises unlike private ones which are usually within the vicinity of the owner’s premises.

- The operations of a general merchandise public warehouse are difficult to automatic because different kinds of goods need different methods and equipment to handle them.

Bonded warehouses

These are public warehouses for keeping imported goods until customs duties have been paid against them. They are mainly located at the points through which goods enter a country

-Imported goods are kept in this type of warehouses if the owner has not paid customs duties. Such goods are said to be "**goods under bond"**or **"goods in bond"**

-Bonded warehouses are so called because the owners of such warehouses give a **'bond'** to the customs authorities i.e. a sum of money as guarantee that they will not release goods from the warehouses until customs duties have been paid.

-The importer may withdraw the goods either in part or in full after the customs duties have been paid for the goods he/she intends to collect.

-If the goods are sold while still in a bonded warehouse, the new owner of the goods pays the duty before taking them out of the warehouse.

-If the goods re-exported to another country while still in a bonded warehouse, the importer does not have to pay the customs duties e.g an importer may import some goods and further prepare them for sale inside a bonded warehouse and can then re-export them without having paid the customs duties

-When the importer pays the duties to the customs officials, a "**release warrant"** is issued. This is a document that enables the importer to have his/her goods released from a bonded warehouse

-Bonded warehouses have resident customs officials who monitor the movement of goods in and out of a bonded warehouse.

Features of a bonded warehouse

- Goods are bonded until customs duty is paid
- Goods can be re-exported while in the warehouse
- Storage charges are made on all goods stored in the warehouse
- Goods can be sold while still under bond
- Goods can be inspected and prepared for sale i.e. they can be repacked, branded and blended while in the warehouse
- Goods are released only on the production of a release warrant

Advantages of bonded warehouse to the importer

- While in bond, goods can be prepared for sale
- The owner can look for the market for the goods before paying the duty

- Some goods lose weight while in the warehouse so the duty paid becomes lower if based on weight.
- If goods are sold while still in the bonded warehouse, the duty passes to the buyer
- The importer has more time to arrange for payment of customs duty.
- Security is provided for the goods, so the importer is relived of the task of providing security for his/her goods
- Some goods improve in quality while in a warehouse for example, wine and tobacco.

Advantages of Bonded warehouse to the Government

- The government gets revenue by levying duty on the goods
- The government is able to control the entry of harmful goods
- The government is able to verify the documents for goods in transit
- The government is able to check on the quantity, quality and the nature/type of goods imported.
- The government is able to check on illegal goods entering the country.

Disadvantages of a bonded warehouse

- The importer may eventually fail to pay customs duties. This forces the customs authorities to auction the bonded goods in order to recover the duties.
- When the importer withdraws goods from a bonded warehouse he/she ends up paying a higher duty if he/she had paid the duty at once.
- The importer incurs costs in hiring a bonded warehouse as opposed to if he/she had a private warehouse

Free warehouses

These are warehouses in which tax-free goods are kept awaiting sale or collection by owners

-Goods stored in these warehouses can be either locally produced, requiring no taxation or imported goods for which customs duties have already been paid.

NOTE: i) All warehouses apart from bonded warehouses are free warehouses since goods held in them are not subject to control by customs authorities. This includes all private and public warehouses

ii) Locally produced goods are stored in free warehouses since no custom duties are paid for them.

Advantages of free warehouses

- Owners of goods stored need not to pay any taxes, thus the goods cannot be auctioned for failure to pay customs duties
- It is cheaper to store goods in free warehouses as compared to bonded warehouses since there are no customs duties levied.
- Clearence of the goods from the warehouse is simple since a “release warrant” to prove payments of duties is necessary
- These warehouses are located at places that are convenient to users

Disadvantages of free warehouses

- The Government does not benefit since no customs duty is levied on the goods stored
- Some unscrupulous traders might use them to store durable goods so as to evade tax.
- Checking and security of goods is more relaxed hence the possibility of storing illegal goods.

Current trends and emerging issues in warehousing

Warehousing technology is undergoing important changes in both building design and handling in storage equipment. These may include;

- **Warehousing design-**In modern times, there is an increasing emphasis on high ceiling warehouses to permit storage of more goods and to make it possible for the movement of fork lift trucks and stuck-cranes
- **Handling of goods-**Handling includes the steps involved in moving of goods to and from storage. There is widespread use of modern machines in most warehouses such as conveyer belts, tracks, forklifts and stuck cranes. The use of automated stucker cranes which more by remote control in a fixed path on guide rails, is a new development in warehousing

  Computerization has also greatly helped in monitoring the movement of stock in and out of storage. This has eased the handling, especially in loading and unloading of goods.

- **Storage of goods-**Storage is the condition of the goods at rest in their assigned areas of the warehouse. Most warehouses are currently using storage racks that permit replacement or retrieval of goods without disturbing neighbouring goods.

- **Environmental pollution-**Goods that expired or spoilt while in the warehouse are sometimes discarded in a manner or in areas that may cause pollution to the environment e.g. expired chemicals are sometimes thrown into rivers and oceans thereby endangering the marine life.

-Other times they are burned causing air pollution with toxic gases. Some goods when thrown on land are dangerous to human life

-To avoid the effects of improper disposal of expired or spoilt goods the warehouse owners should come up with methods that are environmentally friendly such as

recycling of these goods. They should also be socially responsible for whatever goes out from their warehouses.

TOPIC 6

INSURANCE

Insurance-This is an undertaking or contract between an individual or business and an insurance an occurrence of risk(s) (i.e. against events whose occurrences are unforeseen but causes financial losses or suffering to the affected parties.

Risks are also referred to as **contingencies, hazards or perils and include:**

-Fire outbreak

-Accidents

-Thefts

-Deaths

-Disabilities

-Risks are real and unforseen.Methods to eliminate such risks has achieved very little and thus has necessitated the need for insurance.

Importance of insurance

- **Continuity of business**

Every business enterprise is exposed to a variety of risks e.g. fire, theft e.t.c.The occurrence of such risks often result in financial losses to the business. Insurance provides adequate protection against such risks in that, if a trader suffers losses as a result of insured risk, she/he is compensated, thus he/she is able to continue with business operations.

- **Investment projects**

Insurance enables investors to invest in profitable yet risky business projects that would otherwise avoided.

Not all the money received as premiums (by the insurance companies) is used up for compensation to those who have been exposed to risk and suffered losses. The rest of the money is invested in other businesses to earn profits.

- **Creation of employment**

Insurance does provide employment opportunities to members of the public.

- **Government policy**

The profits earned are a source of revenue for the government i.e. insurance companies are profit-making organizations which generate revenue to the government through payments of taxes

- **Credit facilities**

The insurance industry have also established credit or lending facilities which the business community uses by borrowing. Loans are made available to the public for different investment projects in different sectors of the economy and also for personal requirements.

- **Development of infrastructures**

The insurance industry plays a crucial role in the development of urban facilities in major towns. Both residential and office buildings have been developed by insurance firms. The firms also participate in development projects in the areas where they operate. They contribute to development of a region by constructing and infrastructural facilities

- Life policies can be used as security for loans from either the insurance company or other financial institutions.

- Provision of life and general insurance policies encourages Kenyans to plan ahead for their dependants thereby reducing the number of needy future students.

- **Loss prevention-**The insurance companies encourage the insured not to cause accidents thus channeling the unclaimed resources into the economy.

THE THEORY OF INSURANCE

The insurance business relies on the law of large numbers in its operations. According to this law, there should be a large group of people faced with similar risks and these risks spread over a certain given geographical area.

Every person in the group contributes at regular intervals, small amounts of money called premium into a “common pool”. The pool is administered and controlled by the insurance company.

- The fact that risks are geographically spread ensures that insurance does not have a concentration of risks in one particular area.
- The law of large numbers enables the insurance to accurately estimate the future probably losses and the number of people who are likely to apply for insurance. This is done in order to determine the appropriate premiums to be paid by the person taking out insurance.

Pooling of risks

The insurance operation is based on the theory that just a few people out of a given lot may suffer a loss. There is therefore a “pooling of risks” i.e the loss of the unfortunate few is spread over all the contributors of the group, each bearing a small portion of the total loss. This is why the burden of loss is not felt by the individuals because it is “shared” by a large group.

Benefits of the “pooling of Risks” to insurance company

- Pooling of risks enables an insurance company to create a common pool of funds from the regular premiums from different risks.
- It enables the insurance company to compensate those who suffer loss when the risks occur
- The insurance company is able to spread risks over a large number of insured people
- Surplus funds can be invested in for example, giving out loans or buying shares in real estates
- It enables the insurance company to meet its operating costs by using the pool funds
- It enables the insurance company to calculate to be paid by each client
- It enables the company to re-insure itself with another insurance company.

Terms used in Insurance

Insurance

This is a written contract that transfers to an insurer the financial responsibility for losses arising from insured risk.

Premium

This is the specified amount of money paid at regular intervals by the insured to the insurer for coverage against losses arising from a particular risk.

Risk

These are perils or events against which an insurance cover is taken. It is the calamity or problem a person or business faces and results into losses.

Note: The calculation of premiums depends upon the type of risk insured against. The higher the probability of the risk occurring, the higher the premium. The more the risks the business or person is exposed to the more the premiums payable.

Pure risk

This is a risk which results in a loss if it occurs and results in no gains if it does not occur. For example, if a car is involved in an accident, there will be a loss and if the accident does not occur there will be no gain or loss

Speculative risk

This is a risk which when it occurs, may result in a loss or a profit. For example, a person may buy shares at ksh.50 each, one year later the shares may be valued at ksh40 each meaning a loss of ksh.10

Alternatively, their value might not have changed or might have increased to ksh.45 each. Speculative risk lures people to venture into business in the first place.

Insured

This is the individual or the business that takes out the insurance cover and therefore becomes the policy holder

The insured pays premiums to the insurance company to be compensated should the risk insured against occur or cause loss.

Insurer

This is the business company that undertakes to provide cover or protection to the people who suffer loss as a result of occurrence of risks

Actuaries

These are people employed by an insurance company to complete expected losses and calculate the value of premiums.

Claim

This is a demand by the insured for payment from the insurer due to some loss arising from an insured risk.

Policy

This is a document that contains the terms and conditions of the contract between the insurer and the insured. Its issued upon payment of the first premium.

Information contained in a policy includes;

- Name, address and occupation
- Policy number of the insured
- Details of risks insured
- Value of property insured
- Premiums payable
- Other special conditions of the insurance, for example nominees

Actual value

This is the true value of the property insured

Sum insured

This is the value for which property is insured, as stated by the insured at the time of taking the policy.

Surrender value

This is the amount of money that is refunded to the insured by the insurer incase the former(i.e. the insured) terminates payment of the premiums before the insurance contract matures. The policy holder is paid an amount less than the total amount of the premium paid.

Grace period

This is term allowed between the date of signing the contract and the date of payment of the first premium. During this period the insurance contract remains valid. This period is usually a maximum of thirty (30) days.

Proposer

This is a person wishing to take out an insurance cover (prospective insured)

Cover note (Binder)

This is a document given by the insurance company to an insured on payment of the first premium while awaiting for the policy to be processed. It is proof of evidence that the insurer has accepted to cover a proposed risk.

Annuity

This is a fixed amount of money that an insurer agrees to pay the insured annually until the latter's death. It occurs when a person saves a lumpsum amount of money with an insurer in return for a guaranteed payment which will continue until he/she dies.

Consequential loss

This is loss incurred by a business as a result of disruption of business in the event of the insured risk occurring.

Assignment

This is the transfer of an insurance policy by an insured to another person. Any claims arising from the transferred policy passes to the new policy holder called an assignee

Beneficiaries

These are people named in a life assurance policy who are to be paid by the insurer in the event of the insured

Nomination

This is the act of designing one or more people who would be the beneficiaries in the event of death of the insured. These people are called nominees

Average clause

This clause is usually included in policies to discourage under-insurance. The clause provides that the insured can only recover such proportions of the loss as the value of the policy bears on the property insured. It is usually included in marine or fire insurance policies.

The amounts recoverable are arrived at using the following formulae:

$$\text{Compensation} = \frac{\text{value of the policy} * \text{loss}}{\text{Value of property}}$$

Example:

If a house worth kshs.800,000 and insured against fire for kshs.600,000 was damaged by fire to the tune of kshs.400,000,the insured would be compensated;

Compensation= $\frac{600{,}000 \times 400{,}000}{800{,}000}$ ($\frac{\text{value insured} \times \text{Actual loss}}{}$)

Double insurance

This is taking of insurance policies with more than one company in respect to the same subject matter and the risk. It is significant because if one of the insurers is insolvent at the time the claim arises the insured can enforce his/her claim against the solvent insurer or if both insurers are solvent then they share compensation.

(Insolvency is a state where a business is not able to pay all its liabilities from its existing assets)

Co-insurance

This is an undertaking by more than one insurance company to provide insurance cover for the same risk for an insured. This will usually occur for properties that have great value and face great risk exposures that an insurer cannot successfully make compensation for e.g. value of aeroplanes, ships e.t.c

Co-insurance help spread risks to several insurers, each insurer covering only a certain proportion of the total value. The insurance company with the largest share is called the “leader” and acts on behalf of all the participating insurance companies’ e.g. in collecting premiums from the insured and carrying out documentation work, making claim after collecting each insurers premium contribution e.t.c

Note: Co-insurance is different from double-insurance in that in co-insurance company approaches another insurance company to help in covering the insured property while in double-insurance; it’s the insured who decides to approach different insurance companies to insure the same property against the same risk.

Re-insurance

‘Re-insurance’ means insuring again. This is a situation where an insurance company insures itself with a bigger insurance company called **le-insurer** for all or part of the risks insured with it by members of the public

Re-insurance indirectly insure an individuals risks.Re-insurance helps to reduce the burden on an insurance company when the loss is too high for a single insurer. When such losses occurs, the claim is met by both the insurer and re-insurer(s) proportionately (according to agreed percentages)

Note: Re-insurance deal with the protection of insurance companies only, while insurance companies protect individuals and business organizations.

Factors that may make it necessary for an insurance company to Re-insure

- **Value of property-**When the value of property is great, such as ship, the risk is too high to be borne by a single insurer
- **High risk of loss-**When chances of loss through the insured risks are high, it becomes necessary to re-insure.
- **Number of risks covered-**When the insurance company has insured many different risks, it would be too costly to compensate many claims at once, hence the need for re-insurance
- **Need to spread the risk-**When the insurance company wishes to share liability in the event of a major loss occurring
- **Government policy-**The government may make a legal requirement for an insurance company to re-insure

Under-insurance

This occurs when the sum insured as contained in the policy is less than the actual value of the property e.g. A property of shs.500, 000 can be offered for insurance as having a value of shs.400, 000

Over-insurance

This is a situation where the sum insured is more than the correct value of property e.g. a person insures property of shs.300,000 for shs.600,000.If total loss occurs, he is compensated the correct value of the property i.e. that which he has lost

Agents

These are people who sell insurance policies on behalf of the insurance company. They are paid on commission that is dependent upon the total value of policies sold

Insurance Brokers

These are professional middlemen in the insurance process. They connect the people wishing to take insurance with the insurers. They act on behalf of many different insurance firms, unlike agents. Their activities include:

- Examination of insurance market trends
- Correspondence between the insured and his clients
- Advising the insured and would be policy holders on the best policies for their property e.t.c.

  He receives a commission (reward) known as **brokerage.**

  PRINCIPLES OF INSURANCE

Principles of insurance provide guidance to the insurance firms at the time they are entering into a contract with the person taking the cover. These insurance principles include:

- Help to determine whether a valid insurance contract exists between the two parties at the time claims are made.
- Provide checks and controls to ensure successful operations of insurance for the benefit of both the parties

  It is therefore important that a prospective insured (person wishing to take insurance policy) has basic knowledge of these principles as stated in the insurance law.

The insurance principles include;

- **Insurable Interest**

  This principle states that an insurance claim cannot be valid unless the insured person can prove that he has directly suffered a financial loss and not just because the insured risk has occurred.

  Going by this principle one cannot insure his parents or friends or other people’s property since he/she has no insurable interest in them. If such properties are damaged or completely destroyed, he/she will not suffer any financial loss.

  For example, Mr.x has no insurable interest in the property of his neighbours.He does not suffer any financial loss should they be destroyed. This principle ensures

that people are not deliberately destroying other people's properties/life in order for them to receive compensation.

In life insurance (life assurance) it is assumed that a person has unlimited interest in his/her own life. Similarly it is assumed that one has insurable in the life of spouse and children e.g. a wife may insure the life of her husband, a father the life of his child because there is sufficient insurable interest.

- **Indemnity**

The essence of this principle is that the insurer will only pay the "replacement value" of the property when the insured suffers loss as a result of an insured risk.

This principle thus puts the insured back to the financial position he enjoyed immediately before the loss occurred.

It is therefore not possible, then, for anybody to gain from a misfortune by getting compensation exceeding the actual financial loss suffered as this will make him gain from a misfortune.

This principle does not apply in life assurance since it is not possible to value one's life or a part of the body in terms of money. Instead, the insurance policy states the amount of money the insured can claim in the event of death.

- **Utmost good faith (uberrima fides)**

In this principle the person taking out a policy is supposed to disclose the required relevant material facts concerning the property or life to be insured with all honesty. Failure to comply to this may render the contract null and void hence no compensation.

e.g.

-A person suffering from a terminal illness should reveal this information to the insurer.

-One should not under-insure or over-insure his/her property.

- **Subrogation**

This principle compliments the principle of indemnity. It does so by ensuring that a person does not benefit from the occurrence of loss.

According to this principle, whatever remains of the property insured after the insured has been compensated according to the terms of the policy, becomes the property of the insure.

Example

Assuming that Daisy's car is completely damaged in an accident and the insurance compensates for the full value of the loss, whatever remains of the old car (now scrap), belongs to the insurance company

Scrap metal can be sold for some values and should Daisy take the amount she would end up getting more amount than the value of the car which will be against the principle of indemnity.

Note: This principle cannot be applicable to life assurance since there is nothing to subrogate.

- **Proximate cause**

This principle states that for the insured to be compensated there must be a very close relationship between the loss suffered and risk insured i.e. the loss must arise directly from the risk insured or be connected to the risk insured.

Example

- If a property is insured against fire then fire occurs and looters take advantage of the situation and steal some of the property, the insured will suffer loss from 'theft' which is a different risk from the one insured against, so he/she will not be compensated.

  However if the property burns down as a result of sparks from the fire-place, the proximate cause of the loss is sparks which are directly related to fire. So the insured is entitled for compensation.

CLASSES OF INSURANCE

Insurance covers are mainly classified into two,

- Property (non-life) general insurance
- Life assurance

1. Life Assurance

The term assurance is used in respect of life contracts. It is used to mean that life contracts are not contracts of indemnity as life cannot be indemnified i.e. put back to the same financial position he was in before the occurrence of loss.(life has no money value, no amount of money can give back a lost or injured life)

Life insurance (assurance) is entered by the two parties in utmost good faith and the premiums payable in such life contracts depend on:

- **Age;** The higher the age the higher the premiums as the age factor increase the chances of occurrence of death.
- **Health condition;** A person with poor health i.e. sickly person pays higher premiums as opposed to one in good health.
- **Exposure to health risks;** The nature of a person's occupation can make him susceptible to health problems and death.

Types of policies

- **Whole life assurance -** In whole life assurance, the assured pays regular premiums until he/she dies. The sum assured is payable to the beneficiaries upon the death of the assured.

  -Whole life assurance covers disabilities due to illness or accidents i.e. if the insured is disabled during the life of the policy due to illness or accidents, the insurer will pay him/her for the income lost.

ii) Endownment policy/insurance

This is whereby the insured pays regular premiums over a specified period of time. The sum assured is payable either at the expiry of the period (maturity of policy) or on death of the insured, whichever comes first.

The insured, at expiry of policy is given the total sum assured to use for activities of his own choice.(ordinary endownment policy)

-Where the insured dies before maturity of contract, the beneficiaries are given these amounts.

Note; The assured person may be paid a certain percentage of the sum assured at intervals until the expiry of the policy according to the terms of contract. Such an arrangement is known as **Anticipated Endowment policy.**

Advantages of Endowment policies

- They are a form of saving by the insured, for future investments
- Premiums are payable over a specified period of time which can be determined to suit his/her needs e.g. retirement time
- Where the assured lives and time policy matures, he receives the value of sum assured.
- Policy can be used as security for loans from financial institutions.

Differences Between a whole life policy and an Endowment policy

Whole life	**Endowment**
• Compensation is paid after the death of the assured	• Compensation is paid after the expiry of an agreed period
• Premiums are paid throughout the life of the assured	Premiums are paid only during an agreed period
• Benefits go to the dependants rather than the assured	The assured benefits unless death proceeds the expiry of the agreed period
• Aims at financial security of dependants	Aims at financial security of the assured and dependants

iii) Term insurance

The insured here covers his life against death for a given time period e.g. 1yr, 5yrs e.t.c.

If the policy holder dies within this period, his/her dependants are compensated.

If the insured does not die within this specified period, there is no compensation. However, a renewal can be taken.

IV) Education plan/policies

This policy is normally taken by parents for their children's future educational needs.

The policy gives details of when the payments are due.

v) Statutory schemes

The Government offers some types of insurance schemes which are aimed at improving/providing welfare to the members of the scheme such as medical services and retirement benefits.

A member and the employer contribute, at regular intervals, certain amounts of money towards the scheme.

Examples

- N.S.S.F
- N.H.I.F
- Widows and children pension scheme (W.C.P.S)
- **Annuity**

Characteristics of life Assurance

- It is a cover for life until death or for a specified period of time
- It may be a saving plan
- It is normally a long term contract and does not require an annual renewal
- It has a surrender value
- It has a maturity date when the assured is paid the sum assured bonuses and interests.
- A life assurance policy can be assigned to beneficiaries
- The policy can be any amount depending on the assureds' financial ability to pay premiums
- The policy can be used as security for a loan

2. General insurance (property insurance)

This type of insurance covers any form of property against the risks of loss or damage. A person can insure any property he has an insurable interest in

General insurance is usually divided into;

- Fire insurance/department
- Accident insurance/department
- Marine insurance/department
- **Accident insurance**

  This department covers all sorts of risks which occur by accident and includes the following;

- **Motor policies**

-These provide compensation for partial or total loss to a vehicle if the loss results from an accident.

-The policy could either be **third party or comprehensive.**

-Third party policies cover all damages caused by the vehicle to people and property other than the owner and his/her vehicle. This includes pedestrians, fare-paying passengers, cows, fences and other vehicles

In Kenya, a motor-vehicle owner is required by law to have this policy before the vehicle is allowed on the roads. One can also take a third party, fire and theft policy.

Comprehensive policy covers damages caused not only to the third party but also to the vehicle itself and injuries suffered by the owner. Comprehensive policies include full third party, fire, theft and malicious damage to the vehicle.

- **Personal accident policy**

-These policies are issued by insurance companies to protect the insured against personal accidents causing;

- Injury to the person
- Partial or total physical disability as a result of the injury
- Loss of income as a result of death

-If death occurs due to an accident, the insured's beneficiaries are paid the total sum assured.

In case of a partial or total disability as a result of accident, the insured can be paid on regular periods, e.g. monthly as stipulated in the policy.

Compensation for injuries where one loses a part of his/her body can be done on a lump sum basis.

The insured is also paid the value of hospital expenses incurred if hospitalized as a result of an accident.

- **Cash and / or Goods in Transit policies**

These are policies that specifically provide cover for loss of cash and goods in transit between any two locations.

E.g. Goods and cash moved from business to the markets, from suppliers to business e.t.c

d) Burglary and Theft policies

These policies cover losses caused by robbers and thieves

Burglary policies are enforceable only if the insured has met the specified safety and precautionary measures for protection of the insured items.

E.g.-How much money should be maintained in different kinds of safety boxes

-Positioning of each of the cash boxes is also an important precautionary measure.

NB: The control measures are aimed at reducing both the extent and probability of loss occurring

e) Fidelity Guarantee policies

These policies cover the employers against loss of money and/or goods caused by their employees in the cause of duty.

-The losses may be as a result of embezzlement, fraud, arithmetical errors e.t.c

-The policies may cover specified employees or all the employees

7) Workmen's compensation (Employer's Accident liability)

These policies provide compensation for employees who suffer injuries in the course of carrying out their duties.

The employer insures his employee against industrial injuries i.e the employer is only liable for the compensation of workers who suffer injuries at work.

f) Public liability

This insurance covers injury, damages or losses which the business or its employees cause to the public through accidents.

The insurer pays all claims from the public upto an agreed maximum

g) Bad debts

This policy covers firms against losses that might result from debtor's failure to pay their debts.

iii)Marine Insurance

This type of insurance covers ships and cargo against the risk of damage or destruction at the sea. The main risks sea vessels are exposed to include; fire, theft, collision with others, stormy weather, sinking e.t.c

Types of Marine Insurance policies

The marine insurance covers are classified as Hull, cargo, freight and ship owners' liability.

- **Marine Hull**

This policy covers the body of the ship against loss or damage that might be caused by sea perils.

Included here are any equipment, furniture or machinery on the ship.

A special type of marine hull is the part policy, which is for a specified period when the ship is loading, unloading or at service.

- **Marine Cargo**

This type of policy covers the cargo or goods carried by the ship

The policy is taken by the owners of the sea vessels to cover the cargo being transported. It has the following sub-divisions.

- **Voyage policy-**Here cargo and ship are insured for a specific voyage/journey. The policy terminates automatically once the ship reaches the destination.
- **Time policy-**Here insurance is taken to cover losses that may occur within a specified period of time, irrespective of the voyage taken
- **Fleet policy-**This covers a fleet of ships,i.e several ships belonging to one person, under one policy.
- **Floating policy-**This policy covers losses that may occur on a particular route, covering all the ships insured along that route for a specified period
- **Mixed policy-**This policy provides insurance for the ship and cargo on specified voyages and for a particular period of time. No compensation can be made if the ship was on a voyage different from the ones specified even if time has not expired
- **Composite policy-**This is where several insurance companies have insured one policy of a particular ship especially when the sum insured is too large to be adequately covered by one insurer.
- **Construction policy/builders policy-**This covers risks that a ship is exposed to while it is either being constructed, tested or being delivered.
- **Freight policy-**This is an insurance cover taken by the owner of the ship for compensation against failure to pay hiring charges by a hirer of the ship.
- **Third parties liability-**This is an insurance policy taken by the owner of the ship to cover claims that might arise from damage caused to other people's property.

Description of marine losses

The following are some of the losses encountered in marine insurance.

- **Total loss,**

This occurs where there is complete loss or damage to the ship and cargo insured. Total loss can be constructive or actual.

In **Actual total loss,** the claims are as a result of the ships and/or cargos complete destruction. It could also occur;

-When a ship and its cargo are so damaged that what is salvaged is of no market value to both the insurer and the insured.

-When a ship is missing for a considerable period of time enough to assume that it has sunk.

-**Constructive total loss occurs** when the ship and/or cargo are totally damaged but retrieved. It may also occur;

-Where a ship and its cargo are damaged but of market value. This could be as a result of decision to abandon the ship and cargo as the probability of total loss appears imminent.

-If the cost of preventing total loss may be higher than that of the ship and its cargo when retrieved e.g many lives may be lost in the process of trying to prevent total loss.

- **General average-**This is a loss that occurs as a result of some of the cargo being thrown into the sea deliberately to save the ship and the rest of the cargo from sinking. The losses made are shared by the ship owners and the cargo owners proportionately as the effort was in the interest of both.

- **Particular average-**This occurs where there is a partial but accidental loss to either the ship or the cargo. When this happens each of the affected party is soldy responsible for the loss that has occurred to his property. A claim can, however be made if the loss incurred amounts to more than 3% of the value insured.

  Fire insurance-This type of insurance covers property damage or loss caused by accidental fire. Cover is offered to domestic commercial and industrial premises, plant and machinery, equipment, furniture fittings stock e.t.c

  In order to claim for compensation as a result of loss by fire, the following conditions must be fulfilled;

  - Fire must be accidental
  - Fire must be immediate cause of loss
  - There must be actual fire.

There are several types of types of fire insurance policies. These include;

- **Consequential loss policy;(profit interruption policy)**

This covers or compensates the insured for the loss of profit suffered when business operations have

It is offered to protect future earnings of an enterprice after fire damage.

- **Sprinkler leakage policy-**This provides cover against loss or damage caused to goods or premises by accidental leakages from fire fighting sprinklers
- **Fire and Related perils policy-**This covers buildings which include factories, warehouses, shops, offices and their contents. The policy does not cover loss of profit arising from fire damage.

CHARACTERISTICS OF GENERAL INSURANCE

- It’s a contract of indemnity
- It cannot be assigned even to ones relatives

- The insured must have an insurable interest in the property to be insured
- Premiums charged depends on the degree of risk, the higher the premium charged.
- Compensation for loss can only be upto a maximum of the value of the insured property or the sum insured in case of under insurance.
- It has no surrender value
- It's normally a short term contract which can be renewed periodically, usually after one year.

Factors to be considered when Determining Premiums to be charged

- Health of the person
- Frequency of occurrence of previous losses
- Extent of the previous losses
- Value of the property insured
- Occupation of the insured
- Age of the person or of the property in question
- Location of the insured(address and geographical location)
- Period to be covered by the policy
- Residence of the insured.

Procedure for taking a policy

- Filling a proposal form
- Calculation of the premium to be paid
- Issuing of cover note (Binder)
- Issuing of the policy

Insurance	**Gambling**
-The insured must have insurable interest	-A gambler has no insurable interest
-Reinstates the insured back to the financial position just before loss	-Aims at improving the winners financial position
-The insured is expected to pay regular premiums for the insurance cover to remain in force	-Gambling money is paid only once
-Insurance involves pure risks	-Gambling involves speculative risks
-The event of loss might never occur	-The event of bet must happen to determine the winner and the loser.

Procedure of claiming compensation

- **Notification to the insurer-**The insurer has to be notified about the occurrence of any incident immediately.
- **Filling a claim form-**The insurer provides the insured with a claim form which he fills to give details of the risk that has occurred
- **Investigation of the claim-**The insurer arranges to investigate the cause of the incident and to assess the extent of the loss incurred. The insurer is then able to establish whether the insured is to be compensated and if so, for how much.
- **Payment of claim-**On receipt of the report of the assessor, the insurer pays the due compensation to the insured. (Payment of the compensation shows that both the insurer and the insured have agreed on the extent of the loss and the payment is the settlement of the claim)

INSURANCE AND GAMBLING

In most cases, insurance is erroneously taken to be the same as gambling in that small amounts are contributed by many people into a common fund which later benefits just a few people. They are however different and their differences include;

PAST KCSE QUESTONS

1.1995 Describe the procedures that should be followed when taking an insurance policy. 10mks)

2.1996 explain four ways in which the insurance industry promotes the growth of business enterprises. (5mks)

3.1997 Explain four ways in which the insurance industry contributes to the development of Kenya's economy. (10mks)

4.1998 Discuss various insurance policies under which an insurance company would not compensate the insured in the event of the loss. (10mks)

5.1999 Discuss various insurance policies that the owner of a supermarket may find it useful for the business. (12mks)

6.2000 Explain four benefits of the 'pooling of risks' to an insurance company. (8mks)

7.2001 Explain the factors that may make it necessary for an insurance company re-ensure.

8.2002 Explain the meaning of the following terms as used in insurance (10mks)

i) Uberrimae fidei

ii) Indemnity

- Third party motor vehicle insurance

iv) Contribution.

v) Subrogation

9.2003 Discuss four circumstances under which an insurance contract may be terminated. (8mks)

10.2004 Explain five benefits that could be enjoyed by a person who decided to take out an endowment policy. (10mks

TOPIC
PRODUCT PROMOTION

Product is an item or service offered to the consumers at a price. Therefore, product promotion is the communication or any activity undertaken to inform the consumers, persuade and remind them to buy the product from the market.

The purpose/Importance of product promotion

- It informs the customer of the availability, price, and where to obtain the product to satisfy their wants
- It persuade the buyer to buy their products a head of their competitors products in the market
- It reminds the customers of the continued existence of a given product in the market
- It educate the consumers of the usage of the product to satisfy their needs fully
- It informs them on any improvement that has been made on the product
- It stimulates the demand of the product being promoted in the market
- It brings out the positive features of the product
- It opens new market for the product in the environment

Methods of product promotion

Product promotion may be carried out in the following ways:

- Personal selling
- Advertising
- Sales promotion
- Publicity

Personal selling

This is a method of promotion where there is an oral presentation in the conversation with the prospective customer. It is done by with the use of salesmen who informs the prospective buyer of all the aspects of the product

Methods of personal selling

Personal selling can be carried out in the following ways;

- Through sales person approaching the customers

A case where the sales person approaches the prospective customers after drawing their attention, explaining details of the product and even demonstrating how the product works in order to persuade the customer to buy.

Steps involved in personal selling through sales person

- Identify prospective customers who could possibly require the product
- Preparing the presentation by gathering all the possible information about the product , as well as designing an appropriate methods that he will be used to present to the customer
- Establishing the customers contact, as well as choosing an appropriate time to meet the customer to be. That is the time when the customer may receive him
- Arousing the consumers interest in the product by attracting his/her attention through approach and languages, as well as making the prospective customer develop interest in the product
- Dealing with the objections on the product which may have been brought about by the customer to be
- Closing the sale by inquiring whether the prospective customer will be interested in the product or not. This should be done in a polite manner
- Offering after sale service to the customer on the product that has been sold

Shows, trade fairs and exhibitions

This is where the manufacturer of a given product gets a chance to display publicly to the prospective customer to inform them about the product. The prospective customers' attention is then drawn to the product and more information is given to him about the product at the point where it is displayed.

Advantages of shows, trade fair and exhibitions

- It gives the customer an opportunity to compare various products before making a decision on what to buy
- It gives the sales person an opportunity to explain in fine details the features of the product to the prospective customers
- The manufacturers of the product gets a chance to receive immediate feed back from their customers through interactions during the shows
- The number of people visiting their stall to asses their products will help them determine their potential market size for the product

Disadvantages of shows, trade fairs and exhibitions

- It is expensive to hire a stall for the exhibition of the product
- The sales person may have to explain over and over again for the prospective customers as they may not enter into the stall at the same time
- The trade fairs are not frequently organized, therefore an organization rely on it as the only means of product promotion may not succeed

Showrooms

These are large rooms where goods are displayed, especially bulky and durable goods like cars, furniture's, etc for the customer to see and be informed about them to stimulate their interest in them

The room allows the customer to get more information about the product from the sales person in the showroom

Advantages of showrooms

- They enables the seller to get immediate feed back on the product
- They enable the customers to get clarification on the product they need to purchase
- It is a cheap method of production
- It provides an opportunity for the usage of goods to be demonstrated
- The information the prospective customer get from the show room is more reliable

Disadvantages of showrooms

- They are usually located away from the town centers, making them not be accessible by many
- It is expensive to hire showrooms
- They require security to protect the goods inside them which may be very expensive
- Some prospective customers may tamper with goods in the room while trying to operate them

Free Gifts

A gift is an item given to the customer free of charge after buying a product which it is pegged on or buying products of a given value. The gift may not necessarily be the same as the product bought, but they are meant to encourage the customer to buy more or give the customer opportunity to explore the product given as a gift.

Advantages of free gifts

- It enable the customer to enjoy the product given as a gift without paying for it
- It persuades the customer to buy more of the product in order to get the gift
- It is an additional product, and therefore increases the customers satisfaction
- It may help in creating loyalty in the product being promoted

Disadvantages of free gifts

- It makes the customer buy including products they didn't require in order to the said gift
- The cost of the product may be very expensive for he customer
- Some middlemen may remove the gift and keep or even sell to the customer to maximize profit

Free Sample

This is a product on trial given to the customers freely to influence their demand towards the product. It mainly used when the product is new and the customer may have not known about the existence of the product

Advantages of free sample

- It enables the customer try the product before making a decision to buy it
- The customer is able to enjoy the product that otherwise he may have not enjoyed
- The organization is able to get immediate feedback from the customer about their new product
- It enables the organization to acquire more customers for their product

Disadvantages of free sample

- Some of those receiving the sample may not come back to buy
- It may be an expensive method of promotion especially where many samples are to be given
- Goods given for free may reduce the value of goods that may have been sold to earn profit
- It is not suitable for expensive products

Circumstances under which personal selling is appropriate

- When launching a new product in the market which requires a lot of awareness to the prospective customers to enable them make a choice
- When a product is tailored to meet the customer's needs, as different consumers have different needs, taste and preferences to be addressed.
- When demonstration is required on how the product works, especially the technical products
- When the organization has the capacity to finance the sales force carrying out the personal selling.
- Where the market is concentrated within a given region that can easily be accessible by the task force.

Advantages of personal selling

- It is more flexible than any other method for the marketer is able to meet the needs of different people
- It enable the prospective customer to know more details about the product before making a decision
- The sales person is able to demonstrate the use of the product
- The seller is able to get immediate feedback on the product
- The seller is able to obtain the personal contact of the prospective buyer
- It gives the buyer an opportunity to negotiate the terms of purchase
- It takes care of both literate and illiterate prospective customer
- The seller is able to persuade the prospective buyer to buy the product

Disadvantages of personal

- It is labour intensive and therefore very expensive when the area to be covered is wide method
- It is time consuming as it involves explanation and demonstration
- It may only target a particular group of people
- The seller has to meet the travelling and other expenses involved which may be very expensive
- Salespersons may misuse the resources allocated for them, making the target not to be achieved

- The process may inconvenience the prospective buyer's program
- It may only cover a given region which may not be wide enough

Advertising

This is the presentation of information about a product through public media such as news papers, radios, billboards, etc

Types of Advertising

- **Product advertising**: - this is a form of advertisement meant to promote a given product or a particular brand of product
- **Institutional advertising**: - this is a form of advertisement meant to improve the image of the institution or organization and not a particular product. It is meant to create confidence in the customers about the institution
- **Primary demand advertising**: - a form of advertisement meant to a new product that has been introduced in the market for the first time. It is mainly to create awareness of the existence of that particular product
- **Celebrity advertising**: - a form of advertisement where a famous/popular person is used to promote a particular product. It is meant to convince those who identify themselves with that personality to buy the product
- **Informative advertising**: - a form of advertisement meant to give the customer more information about the product to enable them make an informed decision
- **Competitive/persuasive advertising**: - a form of advertisement carried out with organizations producing similar product to persuade the customers to buy their products ahead of their competitors
- **Corrective advertising**: - a form of advertising meant to correct a misleading information that may have been given out about the product
- **Reminder advertising**: - a form of advertising meant to remind the customers that the product still exists in the market and is still capable of satisfying their needs.

Advantages/Importance of advertising to the business

- It maintain the sales of an already existing product
- It create awareness in the customers about a new product in the market
- It informs the customers about the changes that may have been made in the product
- It helps in building image or reputation of the selling organization
- It may increase the volume of the existing sales of a product
- It reaches peoples who may have not been reached by the sales person
- It compliments the effort of the sales person to enable them achieve their sales objectives
- It clears the customers misconception and prejudice about the product
- It opens up new markets for the products.

Disadvantages of advertising to the business

- It may be costly to the business in terms of money and other resources
- It leads to increase in cost of production if at all it has to be done frequently
- The cost of the advertisement will always reduce the profit margin of the business
- Poorly planned advertisement may negatively affect the business
- Misleading advertisement may reduce the level of business operation

Advantages of advertising to the customer

- They educate them on the usage of the product
- They inform them on the products availability
- They guide them on where to get the product
- The outlines all the features about the product including prices to the customer
- Competitive advertisement may lead to improved quality of goods to benefit the customer
- Information on different prices through competitive advertisement makes the customer to benefit from the reduced prices

Disadvantages of advertising to the consumer

- The advertisement may not disclose the side effect of the product
- The advertising cost may be passed to the consumers through increased price
- Some advertisement may persuade customers to buy what they do not require leading to impulse buying
- Some customers may buy substandard goods due to misleading advertisement

Advertising media

These are channels or agents through which an advertisement message is conveyed to the target group. They includes both the print and electronic media which includes; newspapers, journals, magazines, posters, bill-boards, brochures', radio, television, neon signs, etc

- **Newspaper**

These are daily or regularly publications which contains advertisement. They includes, Daily nation, Standard, Taifa Leo, citizen, star, etc

Advantages of newspaper

- The can reach areas that other means may not reach
- Many people can afford them as they are relatively cheap
- They cover a wider geographical area, leading to a wider market
- The message on the news paper can last for a longer period of time, making it to reach more customers
- The advertisement appearing in the newspaper is readily acceptable by the reader
- Colored print makes the advertisement to be more attractive to the reader who in turn gets the information

Disadvantages of the newspaper

- Many of them are written in English or Kiswahili, making them to only target those who can read and understand the language
- It discriminate against the illiterate group who can not read the information
- They have short lifespan as they may be read only on the day it is circulated
- It can not be used to focus on a specific target as they are read by almost everybody
- Some of the prospective customers are always in a hurry to read the newspaper and may not pay attention to the advertisement

- **Magazines and Journals**

These are periodic publications meant to target a particular class or group of people. They may be published monthly, quarterly, annually, etc. The information reaches the targeted group as they read them

Advantages of magazines and Journals

- The specific information for the targeted people can be published
- They can be read and re-read before the next publication may the information to last longer and plead with the prospective customer

- Their publication is of high quality and colourful, making them to draw the attention of their targeted group easier and passing the information to them
- The quality material they are made of makes them to last longer and can be accessed even by those who may have not been around during their publication

Disadvantages of magazines and journals

- If the time gap between the publication time and circulation time is wide, the advertisement may fail
- They are a bit expensive which makes some of the potential customers not to afford them
- The cost of advertising on them may be expensive for the organization
- Their circulations may be limited to a small geographical region
- The publications may not be available in the vernacular language to reach those who are not able to read either English or Kiswahili

Posters and Billboards

A form of advertising that may contain the information about the product either in words, pictures or both for the customer to see and read.

Advantages of posters and billboards

- They are able to convey the information to the large audience, as they are placed in strategic position
- Posters are cheap and easy to prepare
- The use of different colors makes them to be more attractive and appealing to more audience
- It can be used by both literate and illiterate group
- The message may last for a longer period of time
- Billboards are conspicuous and hence attractive to the audience

Disadvantages of posters and billboards

- May be affected by adverse weather condition, especially rain
- If not placed strategically, it may not reach the targeted group
- Incase destroyed by the passersby, the information may not meet the targeted group
- Bill boards are expensive to make and maintain

Transit/transport advertising

A form of advertisement whereby vehicles such as trailers, matatus, buses, etc are used to carry and convey the advertisement message

Advantages of transit advertisement

- The message reaches most of the people in the environment
- They message last long as the paints always last on the vehicle
- Transit vehicles may carry the message a long way to their final destination
- It is captivating to the members of the public especially the promotion convoy, hence can easily reach the target

Disadvantages of transit advertisement

- During the rush hour, the crowd may hinder some from getting the information
- It mainly relay the information to those served by the vehicles

- The noise produced by the promotion convoy may be a nuisance to some members of the public

Brochures
These are small pamphlets carrying message and pictures about product being advertised.

Advantages of Brochures
- They are easy to carry around as they are small in size
- They are effective in meeting the targeted group
- Their cost of production is not very high
- They can be distributed at different places to meet the targeted group
- Can be made attractive by the use of different colours
- They have a long life and therefore can be used repeatedly
- They can be used to direct others on where to get the product

Disadvantages of Brochures
- The information may not reach the illiterate group
- They may be ignored by the intended users
- They may require frequent updating if many changes are made on the product making it expensive

- **Radio**

This is a channel that allows for the advertised messages to be conveyed through sound to the listeners, with some background music accompanying the message

Advantages of Radio
- Different languages may be used to reach different people
- It is accessible even to the remote areas that is not covered by other media
- One can choose the time to advertise to reach the targeted group
- Able to serve many people at the same time
- It can be used for both literate and illiterate members of the group
- The advertisement can be repeated over and over again according to the advertisers needs
- The music accompaniment may attract many people to listen to the information
- Can reach even the blind as they are able to hear
- The message can be conveyed in different languages

Disadvantages of Radio
- Their advertisement does not have any reference
- It may be more expensive than the print media
- Poor timing may make the message no to reach the targeted group
- It may interrupt some programmes to the annoyance of the listener
- It short and brief advertisement may be missed by the listeners
- It is difficult for the listener to visualize the product

Television (T.V) and Cinema
Television is a form of media advertisement where the written words are combined with motion pictures and sound to pass the information
Cinema is where the advertised messaged is conveyed during film shows in the cinema halls. It may be before or after the movie.

Advantages of Television (T.V) and Cinema

- It appeals to most people as it is entertaining
- It makes it possible for the demonstration of the use of the product
- It is able to reach both the literate and illiterate viewers
- The advertisement can be aired over and over again to meet the targeted group
- The advertisement may be modified when need arise
- It has wide appeal to many people
- The message can be conveyed in different languages

Disadvantages of Television (T.V) and Cinema

- The cost of advertising through this media is high
- The television sets are expensive to acquire, hence many people may not have them
- Their uses are limited to places with electricity
- The advertisement may not last longer
- The time for airing the information may not suit the targeted audience

Neon Signs

This is a form of advertisement where the message is passed to the public through the use of electrical signals transmitted through neon lights. They are usually common in the banks, airlines, jewel shops, etc

Advantages of Neon Signs

- The use of different colours makes them very attractive and catch attention of different people
- They can be put strategically making them to be visible to many people
- Can be used both at night and day
- They direct the customer on where the goods are to be found

Disadvantages of Neon Signs

- Can only be used where there is electricity
- They are expensive to buy and maintain
- The message may not easily reach the illiterate

Advertising Agencies

These are businesses that specialize in advertising work and are hired to carry out the functions for other businesses. They are paid a commission for this

Functions of Advertising Agencies

- They help the organizations in designing their trade marks, logos and advertising materials
- They book space and airtime for their clients in various media
- They offer advisory services to their client on selling techniques
- They advertise on behalf of their clients
- They choose on behalf of their clients the appropriate media to be used

Publicity

This is the mentioning of the product or the organization in the mass media to make it be known to many people. There two types of publicity, that is free publicity (where

the payment is not required) and Special featured publicity (where there is payment, for example sponsoring an event in the public)

Advantages of Publicity

- It saves the organization money incase of free publicity
- It is likely to cover a wider region as the publicity is in the media
- The organization may earn credibility due to positive publicity
- The information may be received positively by the customers as the message is likely to be more objective
- It may improve the competitiveness of the firm

Disadvantages of Publicity

- Unfavourable information about the organization may reach the public especially in free publicity
- It is irregular and short lived
- Might require special occasion or event in order to attract the mass media
- The firm does not have control on how the information will appear in the media and the extend of the coverage

Public relations

A process of passing information with an intention of creating, promoting, or maintaining good will and a favourable image of the organization in the public. It involves informing the public about the firm's achievement and how it is contributing to the community welfare and development, to get more approval of the public

Advantages of public relations

- May be used to correct the dented image of the firm
- It informs the public about the activities of the firm
- Assist in upholding the good image of the firm
- It improves the relationship between the firm and its customers

Disadvantages of public relations

- It is costly in terms of time and finance involved
- The customer may make premature buying arising from the picture created by the firm
- Effects may take long before they are actually realized
- It may be difficult to evaluate the impact of the message, since the customers are not obliged to respond to it

Point of purchase (Window) display

This is where the items are arranged in the shops strategically, allowing the customers to see them easily. The arrangement is meant to attract the customer's attention and induce them to buy goods as they pass close to the shop

Advantages of Point of purchase display

- May induce the customer to buy the product due to their arrangement
- As the customers get in to the shop, they are likely to buy including the other goods that were not being displayed
- The customers are able to determine the features of the product with ease
- It is relatively a cheaper method of promotion

Disadvantages of point of purchase

- The method only work well with the potential customers who are near the shop and not far away
- They may also attract thieves especially if the product displayed is of high value
- In case the arrangement does not appeal so much to the customers, they may not get into the shop
- It may be expensive setting up the display area

Direct mail Advertisement
A form of advertisement which is sent to the potential customers directly in the form of a mail, for example the pricelist being sent to the potential customers

Advantages of direct mail advertisement
- It is able to reach the targeted group as they are sent to the potential customer directly
- The message may be made to suit the requirement of the specific customer to be
- There may be an immediate respond on the message
- The potential customers incurs no cost to acquire the information

Disadvantages of direct mail advertisement
- Some mails may not get to the intended customers in time
- The prospective customer may ignore the advertisement
- May not be effective where the customer needs to examine the product
- This method may be expensive especially in terms of material and money
- It may only appeal to the literate group only

Catalogue
A booklet that gives information about the product that the organization deals in. It gives the description about the product, the picture as well as the prices of the product.

Advantages of catalogue
- It may be used to advertise all the products in the organization
- The owner/organization has the total control over the catalogue
- It gives detailed information about the product
- Its colourful nature makes it an attractive promotion tool

Disadvantages of catalogue
- It is expensive to produce increasing the cost of production
- Change in price may affect the whole catalogue

Guarantee (warranty issue)
An assurance given to the customer that the product will serve as expected if used according to the instructions given by the manufacturer. For the guaranteed period the seller will be willing to maintain repair or replace the product for the customer

Advantages Guarantee
- The confidence built in the customer by the guarantee to the customers makes them to buy more products.

- It may create the customers loyalty to the product of the firm
- The fact that the product can be replaced if it gets spoilt within the period is an advantage to the customer

Disadvantages of guarantee

- Repairing or replacing the product may be very costly to the organization
- The method may only be suitable for the durable goods
- The customer may be tempted to mishandle the good during this period

Discount

This is a reduction in price of the commodity, allowing the buyer to pay less than what he would have paid the goods.

Types of discount

- Quantity discount: - Allowed by trader to encourage him/her to buy more quantity of the product being offer
- Trade discount: - Allowed to another trader who is buying products for resale to the consumers
- Cash discount: - Allowed to the customer to enable him pay promptly for the goods bought

- Loss leader: - Selling the price below the market price to entice the customer to buy
- Psychological selling: - Playing with the customers psychology in terms of pricing by quoting odd prices such as 999, 199, 99, etc to convince the customer that the price has been reduced
- Credit facilities: - where the customer is allowed to take a product for his consumption and pay for it later. This entices the customer to buy more of the product
- After sales service: - these are services offered to the buyer after the goods have been bought. They may be in terms of packaging, transportation or installation which may be offered to the customers free of charge. This makes the customer to buy more goods with confidence

Sales promotion

These are activities carried out to increase the sales volume of a business. They are activities out of the ordinary routine of business that is carried out by the seller to increase his sales volume.

The methods of carrying out sales promotion includes all the methods of carrying out product promotion as discussed earlier, that is, shows and trade fair, showrooms, free gifts, free sample, personal selling, advertisement, window display, credit facilities, after sales services, etc

Factors to consider when choosing a promotion method

- The cost of the promotion that is whether the company can afford it or not, for some promotion methods are very expensive that may not be easily affordable to the company.
- The nature of the product being promoted especially whether it requires demonstration or not. Products which requires demonstration are best promoted through personal selling

- The targeted group for the advertisement, on whether they can be reached by that method or not. The promotion method must reach the targeted group, if it has to be effective
- The objective that the firm would like to achieve with the promotion, and whether the method is helping them to achieve that particular objective
- The method used by the competitor in the market to enable them choose a method that will enable them compete favourably
- The requirement of the law concerning product promotion, to enable them not use what the law does not allow

Ethical issues in product promotion

These are rules and regulations to be followed when carrying out promotion to avoid violating other people or businesses right. They include;

- Cheating on performance of the product to attract more customers by given them wrong and enticing information about what the product can do.
- Cheating on the ingredients of the product by telling them that the product contains a suitable type of ingredient which does not exist just to lure them to buy the product
- Not telling them the side effects of the product which may affect them should they continuously use the product due to fear of loosing customer
- False pricing, especially a case where they overprice their and later on reduce them slightly just to lure the customer, yet exploit them
- Not caring about the negative effect of the product on the environment, which may includes littering of the environment by the posters used for advertisement
- Social cultural conflict, especially putting up some forms of advertisement which are considered a taboo buy the community leaving around, such as hanging a billboard of a female advertising inner wears next to a church

Trends in product promotion

The following are some changes that have taken place to improve the product promotion activities

- Use of website/internet to advertise product world wide, which has increased the coverage
- Encouraging gender sensitivity and awareness in product promotion to bring about gender balance
- Use of electronic billboards in advertisement to increase their visibility even at night
- Intensifying personal selling by the business to reach more customers
- Development of promotion convoys to move from one place to the other with music and dancers to attract more prospective customers
- Catering for the rights of the youths when carrying out product promotion and even involving them in carrying out the promotion
- Catering for the interest of those with special needs when carrying out advertisement
- Advertisement through mobile phones by sending them s.m.s about the product