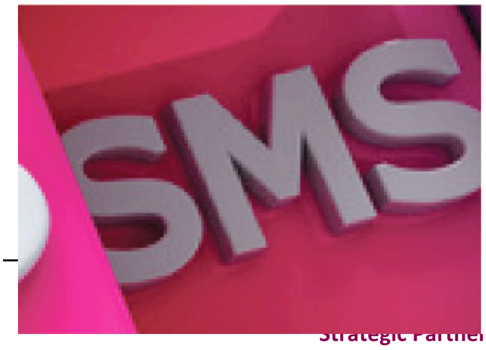
Module 1

PLANNING YOUR BUSINESS

7 classroom hours and 5 hours e-learning

SMART WOMEN



Erasmus+

Project website: www.smartwomenproject.eu

Strategic Partnerships for Vocational Education and Training
Smart Women
Project ID: 2016-1-MT01-KA202-015202

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In the framework of the Smart Women project, seven partners from European countries have created an innovative European Training Model, focused on women, aiming for **encouraging entrepreneurship** and putting business ideas into practice.

The Smart Women Model combines online learning using online learning platforms and face to face training based on project collaboration, peer-learning, guidance, coaching and counselling.

Project Partners: MCA (Malta), LIKTA (Latvia), Dedalo Fundacion (Spain), EOS (Romania), Cyprus Computer Society (Cyprus) and ALL DIGITAL (Belgium).

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DISCLAIMER

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Planning Your Business

Creating a business plan is a useful and versatile tool. It is a guide that can also be described as the businessman's best friend. In today's global and highly competitive business environment, enterprises, whether large or small, cannot hope to compete and grow without proper planning.

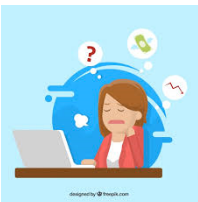
Learning Objectives

Having completed this module you will be able to:

- How to develop your business idea into a real business
- Making your business idea come to life by the SWOT analysis
- Define the market and the different kinds of competition that a business face
- The product life cycle
- The marketing mix
- An introduction to budgets

ANNOTATIONS

The following icons are used in the text with the meaning indicated.

Icon	Used as
	Concepts & Theory
	Resources & links the student can use for further reading
	Review Exercise
	Tasks to be performed by student individually
	Tasks to be performed by students in groups

MODULE OUTLINE

1.BUSINESS IDEA DEVELOPMENT AND EVALUATION BY SWOT ANALYSIS

Concepts

Who are we?

Individually, introduce yourselves by answering these four questions briefly to everyone in class:

1. What is your business idea?
2. What is your product?
3. Who is your product targeted at? (Who will your customers be?)
4. Where do you stand right now?

Example:

“My business idea is to start selling homemade products. I would like to specialise in sugar-free marmalades, targeted at people following low-sugar diets / diabetics. Right now I am preparing these marmalades for my relatives and friends, and sometimes as gifts.”

Now, let’s develop those ideas!

Brainstorming Tool

This will help you develop a wide range of ideas.

Start with one keyword and write down all the points/ideas you can think of.

Do not criticise any ideas (if you are doing it in a group)

Example:

Mind Maps

A Powerful Approach to Note-Taking

(Also known as Mind Mapping, Concept Mapping, Spray Diagrams, and Spider Diagrams)

Have you ever studied a subject or brainstormed an idea, only to find yourself with pages of information, but no clear view of how it fits together?

This is where Mind Mapping can help you.

Mind Mapping is a useful technique that helps you learn more effectively, improves the way that you record information, and supports and enhances creative problem solving.

By using Mind Maps, you can quickly identify and understand the structure of a subject. You can see the way that pieces of information fit together, as well as recording the raw facts contained in normal notes.

More than this, Mind Maps help you remember information, as they hold it in a format that your mind finds easy to recall and quick to review. Read on to find out more.

About Mind Maps

Mind Maps were popularized by author and consultant, Tony Buzan. They use a two-dimensional structure, instead of the list format conventionally used to take notes.

Mind Maps are more compact than conventional notes, often taking up one side of paper. This helps you to make associations easily, and generate new ideas . If you find out more information after you have drawn a Mind Map, then you can easily integrate it with little disruption.

More than this, Mind Mapping helps you break large projects or topics down into manageable chunks, so that you can plan effectively without getting overwhelmed and without forgetting something important.

A good Mind Map shows the "shape" of the subject, the relative importance of individual points, and the way in which facts relate to one another. This means that they're very quick to review, as you can often refresh information in your mind just by glancing at one. In this way, they can be effective mnemonics – remembering the shape and structure of a Mind Map can give you the cues you need to remember the information within it.

When created using colours and images or drawings, a Mind Map can even resemble a work of art!

Uses

Mind Maps are useful for:

- Brainstorming – individually, and as a group.
- Summarizing information, and note taking.
- Consolidating information from different research sources.
- Thinking through complex problems.
- Presenting information in a format that shows the overall structure of your subject.
- Studying and memorizing information.

Drawing Basic Mind Maps

To draw a Mind Map, follow these steps:

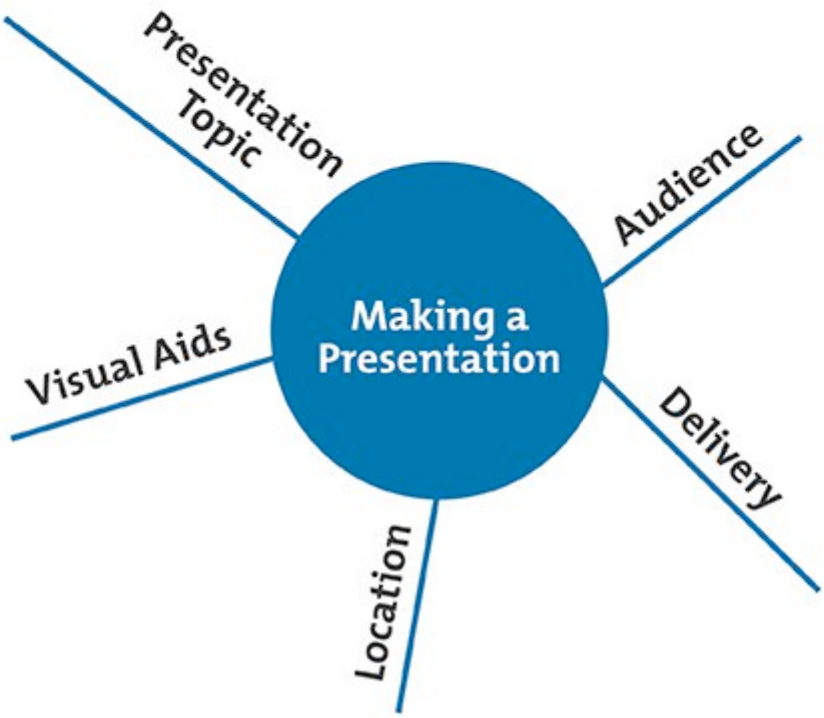
1. Write the title of the subject you're exploring in the center of the page, and draw a circle around it. This is shown by the circle marked in figure 1, below.

(Our simple example shows someone brainstorming actions needed to deliver a successful presentation.)

Figure 1

2. As you come across major subdivisions or subheadings of the topic (or important facts that relate to the subject) draw lines out from this circle. Label these lines with these subdivisions or subheadings. (See figure 2, below.)

Figure 2



3. As you "burrow" into the subject and uncover another level of information (further subheadings, or individual facts) belonging to the subheadings, draw these as lines linked to the subheading lines. These are shown in figure 3.

Figure 3

4. Then, for individual facts or ideas, draw lines out from the appropriate heading line and label them. These are shown in Figure 4.

Figure 4

5. As you come across new information, link it in to the Mind Map appropriately.

A complete Mind Map may have main topic lines radiating in all directions from the center. Sub-topics and facts will branch off these, like branches and twigs from the trunk of a tree. You don't need to worry about the structure you produce, as this will evolve of its own accord.

Using Mind Maps Effectively

Once you understand how to take notes in Mind Map format, you can develop your own conventions for taking them further. The following suggestions can help you draw impactful Mind Maps:

- **Use Single Words or Simple Phrases** – Many words in normal writing are padding, as they ensure that facts are conveyed in the correct context, and in a format that is pleasant to read.

In Mind Maps, single strong words and short, meaningful phrases can convey the same meaning more potently. Excess words just clutter the Mind Map.

- **Print Words** – Joined up or indistinct writing is more difficult to read.

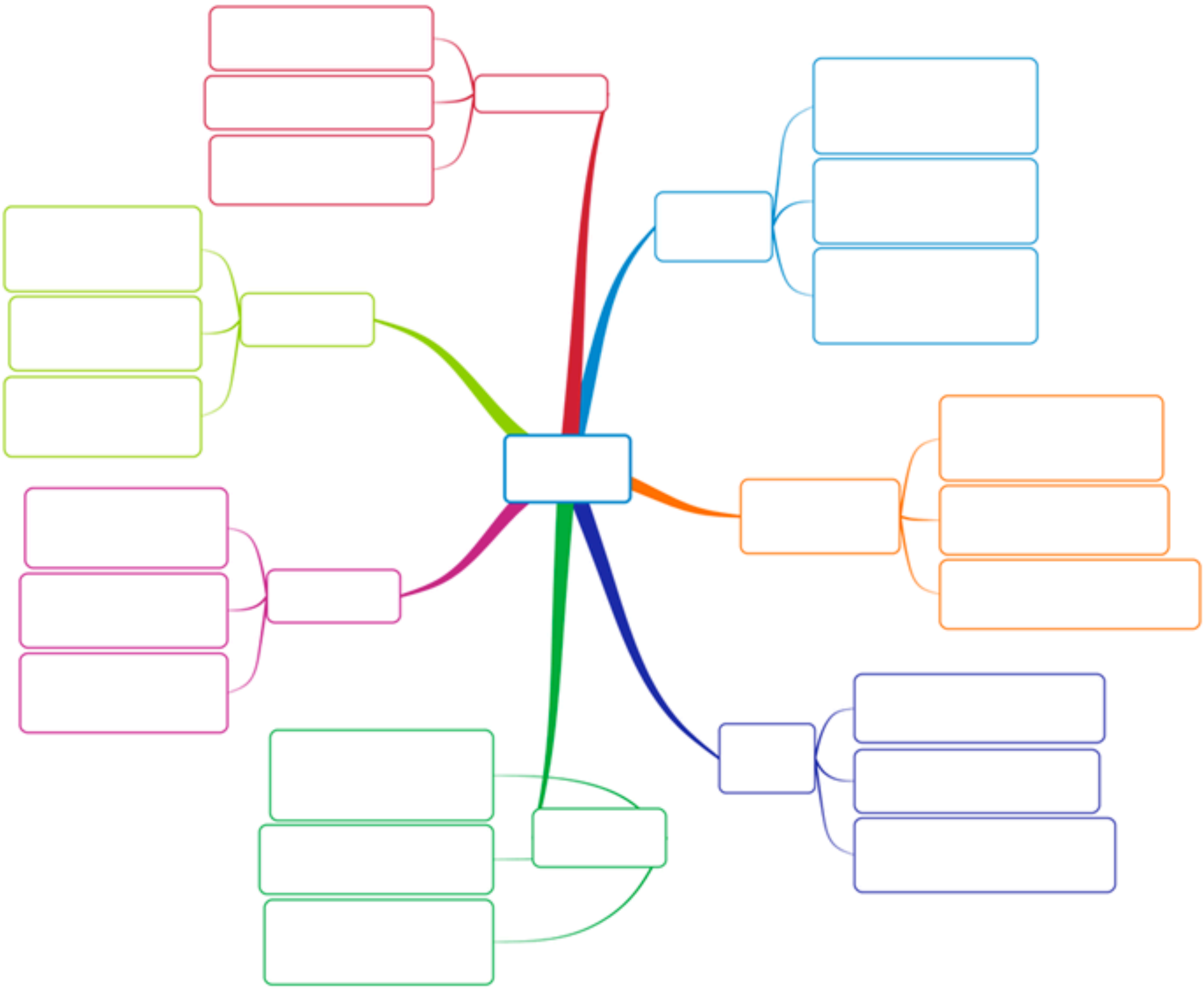
- **Use Colour to Separate Different Ideas** – This will help you to separate ideas where necessary. It also helps you to visualize the Mind Map for recall. Colour can help to show the organization of the subject.

- **Use Symbols and Images** – Pictures can help you to remember information more effectively than words, so, where a symbol or picture means something to you, use it.

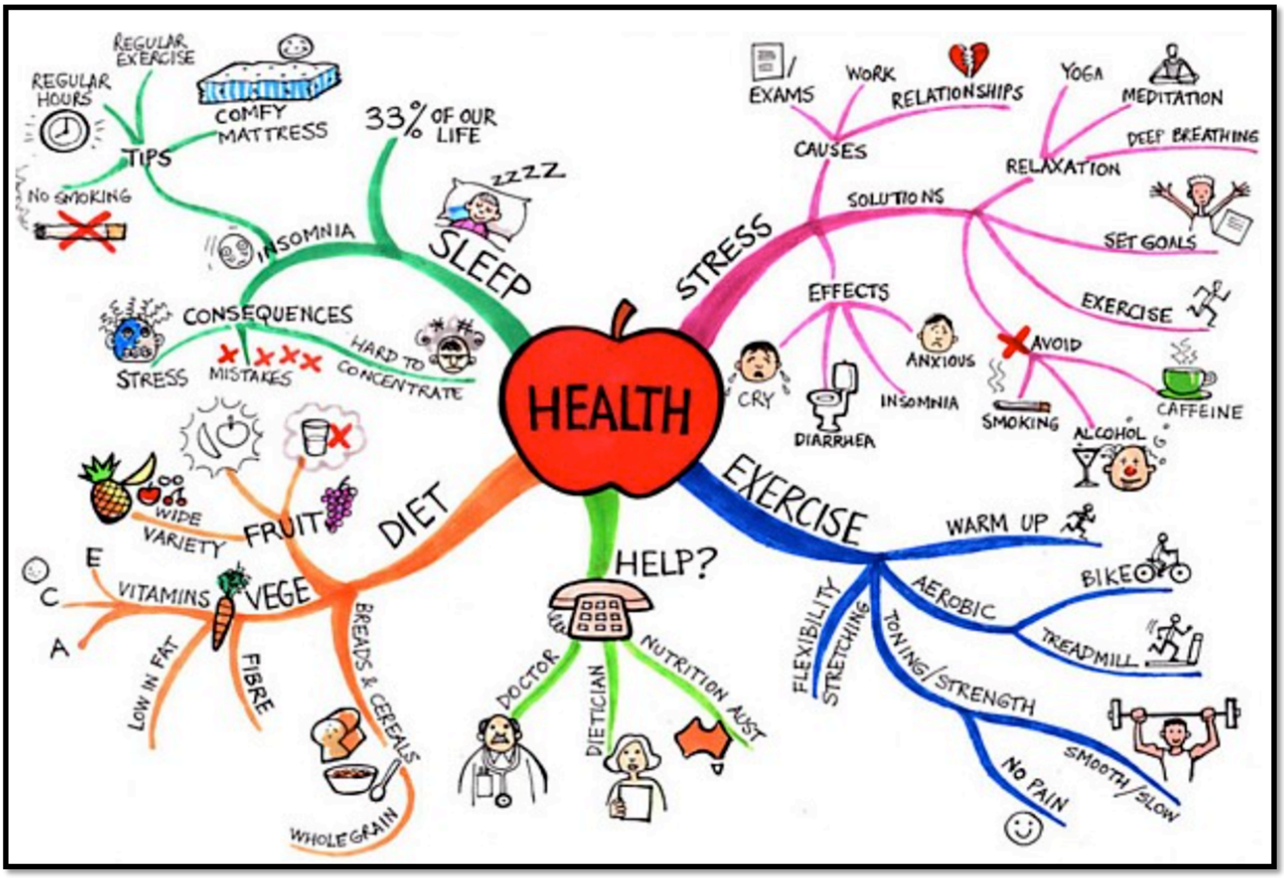
- **Using Cross-Linkages** – Information in one part of a Mind Map may relate to another part. Here you can draw lines to show the cross-linkages. This helps you to see how one part of the subject affects another.

 **Task**

Example: Let's mind-map the topic of 'Health'



Now let's take a look at how this could have come out



SWOT Analysis

Conducting a SWOT analysis of your business is a lot more fun than it sounds. It won't take much time, and doing it forces you to think about your business in a whole new way.

The point of a SWOT analysis is to help you develop a strong business strategy by making sure you've considered all of your business's strengths and weaknesses, as well as the opportunities and threats it faces in the marketplace.

What is a SWOT analysis?

S.W.O.T. is an acronym that stands for Strengths, Weaknesses, Opportunities, and Threats. A SWOT analysis is an organized list of your business's greatest strengths, weaknesses, opportunities, and threats.

Strengths and weaknesses are internal to the company (think: reputation, patents, location). You can change them over time but not without some work. Opportunities and threats are external (think: suppliers, competitors, prices)—they are out there in the market, happening whether you like it or not. You can't change them.

Existing businesses can use a SWOT analysis, at any time, to assess a changing environment and respond proactively. In fact, I recommend conducting a strategy review meeting at least once a year that begins with a SWOT analysis.

New businesses should use a SWOT analysis as a part of their planning process. There is no "one size fits all" plan for your business, and thinking about your new business in terms of its unique "SWOTs" will put you on the right track right away, and save you from a lot of headaches later on.

Looking to get started right away?

In this article, I will cover the following:

- How to conduct a SWOT analysis
- Questions to ask during a SWOT analysis
- Example of a SWOT analysis
- TOWS analysis: Developing strategies for your SWOT analysis

How to conduct a SWOT analysis

To get the most complete, objective results, a SWOT analysis is best conducted by a group of people with different perspectives and stakes in your company. Management, sales, customer service, and even customers can all contribute valid insight. Moreover, the SWOT analysis process is an opportunity to bring your team together and encourage their participation in and adherence to your company's resulting strategy.

A SWOT analysis is typically conducted using a four-square SWOT analysis template, but you could also just make lists for each category. Use the method that makes it easiest for you to organize and understand the results.

I recommend holding a brainstorming session to identify the factors in each of the four categories. Alternatively, you could ask team members to individually complete our free SWOT analysis template, and then meet to discuss and compile the results. As you work through each category, don't be too concerned about elaborating at first; bullet points may be the best way to begin. Just capture the factors you believe are relevant in each of the four areas.

Once you are finished brainstorming, create a final, prioritized version of your SWOT analysis, listing the factors in each category in order of highest priority at the top to lowest priority at the bottom.

Questions to ask during a SWOT analysis

I've compiled some questions below to help you develop each section of your SWOT analysis. There are certainly other questions you could ask; these are just meant to get you started.

Strengths *(internal, positive factors)*

Strengths describe the positive attributes, tangible and intangible, internal to your organization. They are within your control.

- What do you do well?
- What internal resources do you have? Think about the following:
    - *Positive attributes of people*, such as knowledge, background, education, credentials, network, reputation, or skills.
    - *Tangible assets of the company*, such as capital, credit, existing customers or distribution channels, patents, or technology.
- What advantages do you have over your competition?
- Do you have strong research and development capabilities? Manufacturing facilities?

- What other positive aspects, internal to your business, add value or offer you a competitive advantage?

Weaknesses *(internal, negative factors)*

Weaknesses are aspects of your business that detract from the value you offer or place you at a competitive disadvantage. You need to enhance these areas in order to compete with your best competitor.

- What factors that are within your control detract from your ability to obtain or maintain a competitive edge?
- What areas need improvement to accomplish your objectives or compete with your strongest competitor?
- What does your business lack (for example, expertise or access to skills or technology)?
- Does your business have limited resources?
- Is your business in a poor location?

Opportunities *(external, positive factors)*

Opportunities are external attractive factors that represent reasons your business is likely to prosper.

- What opportunities exist in your market or the environment that you can benefit from?
- Is the perception of your business positive?
- Has there been recent market growth or have there been other changes in the market that create an opportunity?
- Is the opportunity ongoing, or is there just a window for it? In other words, how critical is your timing?

Threats *(external, negative factors)*

Threats include external factors beyond your control that could place your strategy, or the business itself, at risk. You have no control over these, but you may benefit by having contingency plans to address them if they should occur.

- Who are your existing or potential competitors?
- What factors beyond your control could place your business at risk?
- Are there challenges created by an unfavourable trend or development that may lead to deteriorating revenues or profits?

- What situations might threaten your marketing efforts?
- Has there been a significant change in supplier prices or the availability of raw materials?
- What about shifts in consumer behaviour, the economy, or government regulations that could reduce your sales?
- Has a new product or technology been introduced that makes your products, equipment, or services obsolete?

Examples of a SWOT analysis

For illustration, here’s a brief SWOT example from a hypothetical, medium-sized computer store in the United States:

Strengths	**Weaknesses**
• **Knowledge:** Our competitors are pushing boxes. But we know systems, networks, programming, and data management. • **Relationship selling:** We get to know our customers, one by one. • **History:** We've been in our town forever. We have the loyalty of customers and vendors.	• **Price and volume:** The major stores pushing boxes can afford to sell for less. • **Brand power:** We can't match the competitor's full-page advertising in the Sunday paper. We don't have the national brand name.
Opportunities	**Threats**
• **Training:** The major stores don't provide training, but as systems become more complex, training is in greater demand. • **Service:** As our target market needs more service, our competitors are less likely than ever to provide it.	• **The larger price-oriented store:** When they advertise low prices in the newspaper, our customers think we are not giving them good value. • **The computer as appliance.** Volume buying of computers as products in boxes. People think they need our services less.

TOWS analysis: Developing strategies from your SWOT analysis

Once you have identified and prioritized your SWOT results, you can use them to develop short-term and long-term strategies for your business. After all, the true value of this exercise is in using the results to maximize the positive influences on your business and minimize the negative ones.

But how do you turn your SWOT results into strategies? One way to do this is to consider how your company's strengths, weaknesses, opportunities, and threats overlap with each other. This is sometimes called a **TOWS analysis.**

For example, look at the strengths you identified, and then come up with ways to use those strengths to maximize the opportunities (these are strength-opportunity strategies). Then, look at how those same strengths can be used to minimize the threats you identified (these are strength-threats strategies).

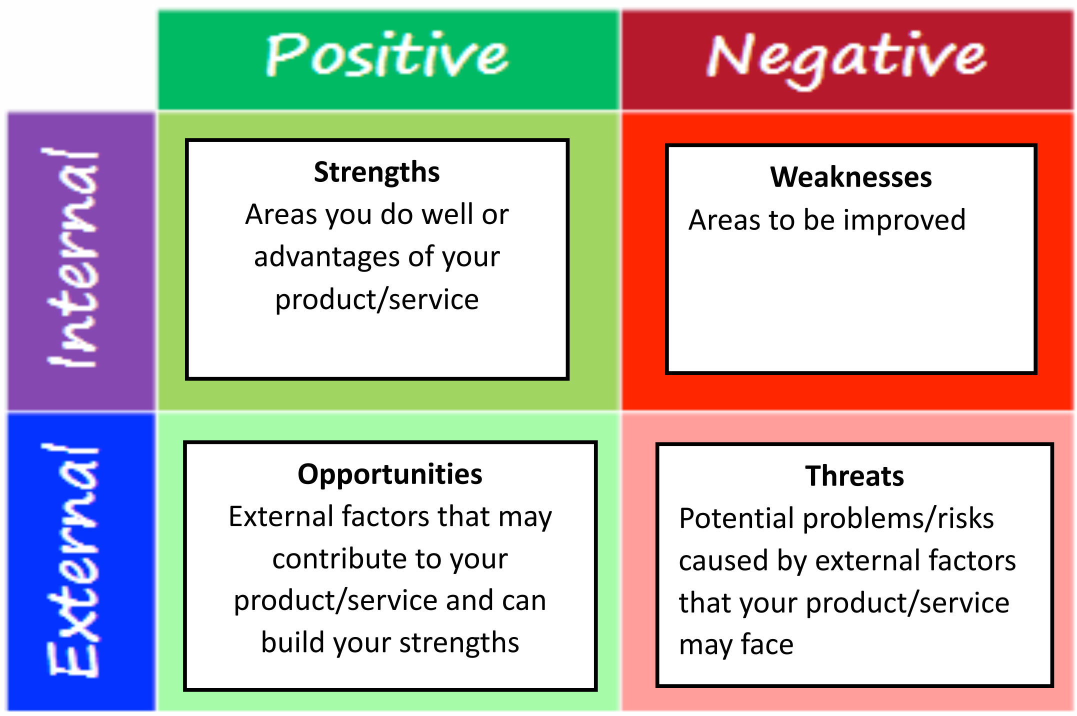
Continuing this process, use the opportunities you identified to develop strategies that will minimize the weaknesses (weakness-opportunity strategies) or avoid the threats (weakness-threats strategies).

The following table might help you organize the strategies in each area:

	Opportunities (external, positive)	**Threats** (external, negative)
Strengths (internal, positive)	**Strength-Opportunity strategies** Which of the company's strengths can be used to maximize the opportunities you identified?	**Strength-Threats strategies** How can you use the company's strengths to minimize the threats you identified?
Weaknesses (internal, negative)	**Weakness-Opportunity strategies** What action(s) can you take to minimize the company's weaknesses using the opportunities you identified?	**Weakness-Threats strategies** How can you minimize the company's weaknesses to avoid the threats you identified?

Once you've developed strategies and included them in your strategic plan, be sure to schedule regular review meetings. Use these meetings to talk about why the results of your strategies are different from what you'd planned (because they always will be) and decide what your team will do going forward.

SWOT Summery



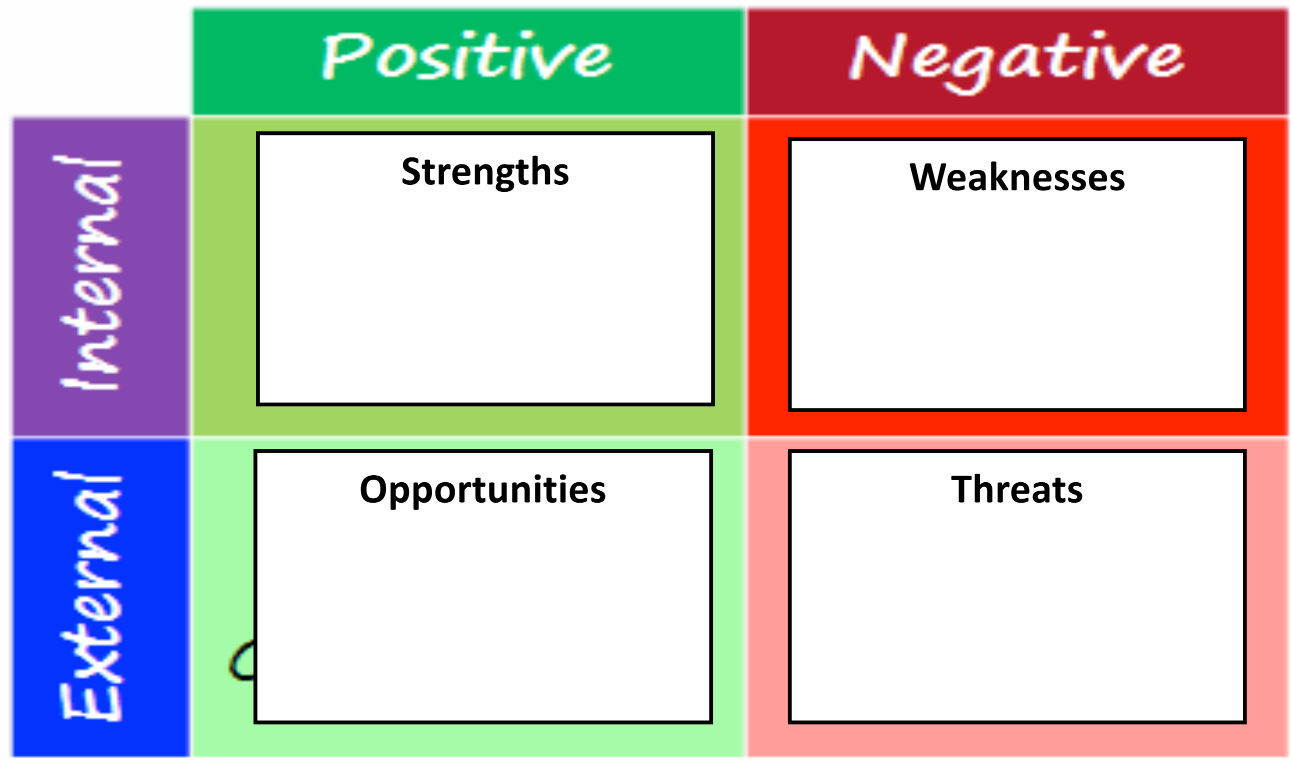
Worked Example

Coca cola is a brand which is present in households, shops, hotels, offices, etc. You name it, and the place would have heard of Coca cola. Coca cola has many products in its arsenal. Here is the SWOT analysis of Coca cola.

	Positive	Negative
Internal	**Strengths** Brand value is over $77 billion World's largest beverage company Strong marketing and advertising	**Weaknesses** Reliance on carbonated drinks Lack of diversification Negative publicity
External	**Opportunities** Growth in beverage consumption Increasing bottled water demand Reduced price of production material	**Threats** Changing customer demand Increased competition for carbonated drinks Local brands in different countries

 **Task**

You are now encouraged to carry out your own SWAT analysis according to your own business idea.



1.2 DEFINING THE MARKET

Concepts

There are various factors one should consider before introducing their product/service to the market.

These factors include:

- Geographic segmentation
- Customer segmentation
- Competition
- Maturity of the market

What is Geographic Segmentation?

Geographic segmentation is when a business divides its market on the basis of geography. There are several ways that a market can be geographically segmented. You can divide your market by geographical areas, such as by city, county, state, region, (like the West Coast), country, or international region, (like Asia). You can also divide the market into rural, suburban, and urban market segments. And, you can segment a market by climate or total population in each area.

Advantages of Geographic Segmentation

So what are the advantages of geographic segmentation? Let's look at some.

- It's an effective approach for companies with large national or international markets because different consumers in different regions have different needs, wants, and cultural characteristics that can be specifically targeted.
- It can also be an effective approach for small businesses with limited budgets. They can focus on their defined area and not expend needless marketing dollars on approaches ill-suited for their target geographic segment.
- It works well in different areas of population density. Consumers in an urban environment often have different needs and wants than people in suburban and rural environments. There are even cultural differences between these three areas.
- It's relatively easy to break your market down to geographic segments.

Customer Segmentation

Segmenting a market is sound practice. It enables you to develop a deeper understanding of your customers and discover what makes them tick. When you're communicating a message, it will be more effective if the recipient of the message finds it relevant.

Segmentation is simply a way of arranging your customers into smaller groups according to type. These distinct sub-groups or segments should be characterised by particular attributes. Now you can target specific, relevant marketing messages at each group.

And it's not just about what you say. How you communicate is also vital, and segmentation often requires a carefully structured marketing mix. That's because some customers may prefer the direct approach, such as telephone marketing, while others respond better to a local advertising campaign.

First steps to customer segmentation

Segmentation doesn't have to be complex. For a small company, it could be about recognising that you have two or three distinct customer types with different needs. My philosophy is to always start with the simple question: Who do we want to talk to? The answer could be simple - customers. Segmentation principles can then add several layers of intelligence, based on key differentials, such as:

- spending patterns;
- gender;
- where they live;
- age;
- socio-economic group.

What is important is not surface differences, but those differences that actually affect buying behaviour. What triggers each person to buy? If you run a hairdressing salon, for example, the type of offers you might make to customer groups would certainly differ on gender and age lines. If you own a mail order business, you might be better off analysing buying patterns and splitting customers into groups according to how much they spend, how often they buy or what products they are most interested in.

Targeted selling

By increasing your understanding of what your customers are buying, you can also maximise opportunities for cross-selling or up-selling. I'm reminded of the builders merchant who sells a tonne of bricks but doesn't cross-sell by selling the sand and cement. By grouping together all the customers who regularly buy certain products, you can target them with relevant offers encouraging them to increase their spend.

Not only is a relevant marketing message more effective as a sales tool, it is also about good customer service. A piece of communication that acknowledges what you bought and when is much more impactful than a one-size-fits-all message. What's more, if you are a regular customer, a targeted message shows that you are appreciated and valued. Conversely, a general message, which doesn't acknowledge previous custom, could well make you feel unloved and taken for granted.

Competition

The Four Types of Market Structures

There are quite a few different market structures that can characterize an economy. However, if you are just getting started with this topic, you may want to look at the four basic types of market structures first. Namely perfect competition, monopolistic competition, oligopoly, and monopoly. Each of them has their own set of characteristics and assumptions, which in turn affect the decision making of firms and the profits they can make.

It is important to note that not all of these market structures actually exist in reality, some of them are just theoretical constructs. Nevertheless, they are of critical importance, because they can illustrate relevant aspects of competition firms' decision making. Hence, they will help you to understand the underlying economic principles. With that being said, let's look at them in more detail.

Perfect Competition

Perfect competition describes a market structure, where a large number of small firms compete against each other. In this scenario, a single firm does not have any significant market power. As a result, the industry as a whole produces the socially optimal level of output, because none of the firms have the ability to influence market prices.

The idea of perfect competition builds on a number of assumptions: (1) all firms maximize profits (2) there is free entry and exit to the market, (3) all firms sell completely identical (i.e. homogenous) goods, (4) there are no consumer preferences. By looking at those assumptions it becomes quite obvious, that we will hardly ever find perfect competition in reality. This is an important aspect, because it is the only market structure that can (theoretically) result in a socially optimal level of output.

Probably the best example of a market with almost perfect competition we can find in reality is the stock market. If you are looking for more information on perfect competition, you can also check our post on perfect competition vs imperfect competition.

Monopolistic Competition

Monopolistic competition also refers to a market structure, where a large number of small firms compete against each other. However, unlike in perfect competition, the firms in monopolistic competition sell similar, but slightly differentiated products. This gives them a certain degree of market power which allows them to charge higher prices within a certain range.

Monopolistic competition builds on the following assumptions: (1) all firms maximize profits (2) there is free entry and exit to the market, (3) firms sell differentiated products (4) consumers may prefer one product over the other. Now, those assumptions are a bit closer to reality than the ones we looked at in perfect competition. However, this market structure will no longer result in a socially optimal level of output, because the firms have more power and can influence market prices to a certain degree.

An example of monopolistic competition is the market for cereals. There is a huge number of different brands (e.g. Cap’n Crunch, Lucky Charms, Froot Loops, Apple Jacks). Most of them probably taste slightly different, but at the end of the day, they are all breakfast cereals.

Oligopoly

An oligopoly describes a market structure which is dominated by only a small number firms. This results in a state of limited competition. The firms can either compete against each other or collaborate. By doing so they can use their collective market power to drive up prices and earn more profit.

The oligopolistic market structure builds on the following assumptions: (1) all firms maximize profits, (2) oligopolies can set prices, (3) there are barriers to entry and exit in the market, (4) products may be homogenous or differentiated, and (5) there is only a few firms that dominate the market. Unfortunately, it is not clearly defined what a «few» firms means exactly. As a rule of thumb, we say that an oligopoly typically consists of about 3-5 dominant firms.

To give an example of an oligopoly, let’s look at the market for gaming consoles. This market is dominated by three powerful companies: Microsoft, Sony, and Nintendo. This leaves all of them with a significant amount of market power.

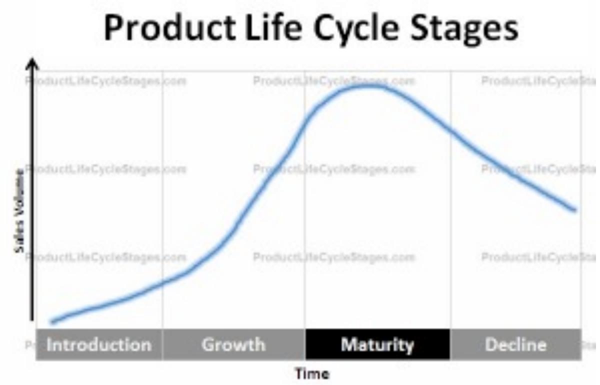
Monopoly

A monopoly refers to a market structure where a single firm controls the entire market. In this scenario, the firm has the highest level of market power, as consumers do not have any alternatives. As a result, monopilists often reduce output to increase prices and earn more profit.

The following assumptions are made when we talk about monopolies: (1) the monopolist maximizes profit, (2) it can set the price, (3) there are high barriers to entry and exit, (4) there is only one firm that dominates the entire market.

From the perspective of society, most monopolies are usually not desirable, because they result in lower outputs and higher prices compared to competitive markets. Therefore, they are often regulated by the government. An example of a real life monopoly could be Monsanto. About 80% of all corn harvested in the US is trademarked by this company. That gives Monsanto an extremely high level of market power. You can find additional information about monopolies our post on monopoly power.

Maturity



After the Introduction and Growth stages, a product passes into the Maturity stage. The third of the product life cycle stages can be quite a challenging time for manufacturers. In the first two stages companies try to establish a market and then grow sales of their product to achieve as large a share of that market as possible. However, during the Maturity stage, the primary focus for most companies will be maintaining their market share in the face of a number of different challenges.

Challenges of the Maturity Stage

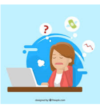
- **Sales Volumes Peak**: After the steady increase in sales during the Growth stage, the market starts to become saturated as there are fewer new customers. The majority of the consumers who are ever going to purchase the product have already done so.
- **Decreasing Market Share**: Another characteristic of the Maturity stage is the large volume of manufacturers who are all competing for a share of the market. With this stage of the product life cycle often seeing the highest levels of competition, it becomes increasingly challenging for companies to maintain their market share.
- **Profits Start to Decrease**: While this stage may be when the market as a whole makes the most profit, it is often the part of the product life cycle where a lot of manufacturers can start to see their profits decrease. Profits will have to be shared amongst all of the competitors in the market, and with sales likely to peak during this stage, any manufacturer that loses market share, and experiences a fall in sales, is likely to see a subsequent fall in profits. This decrease in profits could be compounded by the falling prices that are often seen when the sheer number of competitors forces some of them to try attracting more customers by competing on price.

Benefits of the Maturity Stage

- **Continued Reduction in Costs**: Just as economies of scale in the Growth stage helped to reduce costs, developments in production can lead to more efficient ways to manufacture high volumes of a particular product, helping to lower costs even further.
- **Increased Market Share Through Differentiation**: While the market may reach saturation during the Maturity stage, manufacturers might be able to grow their market share and increase profits in other ways. Through the use of innovative marketing campaigns and by offering more diverse product features, companies can actually improve their market share through differentiation and there are plenty of product life cycle examples of businesses being able to achieve this.

Product Life Cycle Management in the Maturity Stage

The Maturity stage of the product life cycle presents manufacturers with a wide range of challenges. With sales reaching their peak and the market becoming saturated, it can be very difficult for companies to maintain their profits, let alone continue trying to increase them, especially in the face of what is usually fairly intense competition. During this stage, it is organizations that look for innovative ways to make their product more appealing to the consumer that will maintain, and perhaps even increase, their market share.



Task

Each participant analyses own target market according to own business idea, in terms of the mentioned factors by answering the following questions:

1. What is your business idea (product/service)?
2. What is the geographic segment that you intend to target your product/service at? Why did you choose this particular segment?
3. What will be the characteristics of your customers?
4. What means of communication do you intend to use to reach your customers?
5. Which of the four types of competition does your business fall in?
6. How would you differentiate your product/service when it reaches the maturity stage?

1.3 THE MARKETING MIX – PRODUCT AND PLACE

Concepts

What is marketing?

A “simple” definition that many marketers give to this word is
“Putting the right product in the right place, at the right price, at the right time.”

It sounds simple however a lot of hard work needs to go into:

- finding out what customers want,
- identifying where they do their shopping,
- figuring out how to produce the item at a price that represents value to them, and
- Getting it all to come together at the critical time.
- The **marketing mix** is used to describe the different choices that organisations could opt for to be able to bring their product or service to the market.
- The **4Ps** is a good way to do this.

These are:

- **Product (**or **Service)**
- **Price**
- **Place (**also called **Distribution)**
- **Promotion**

- Getting one of the 4Ps wrong could result in a disaster.

*During this session we are going to discuss **Product** and **Place** **(Distribution).***

The Production Process

- This is a process that transforms a range of inputs into those outputs (products) that are required by the market.
- This involves two main sets of resources:
    - the transforming resources, and
    - the transformed resources
- The transforming resources include the premises,
  machinery, computers and people that carry out
  the transforming processes.
- The transformed resources are the raw materials and components that are transformed into end products.
- Any production process involves a series of links in a production chain.
- At each stage **value** is added in the course of production. This makes a product more desirable to a consumer so that they will pay more for it.
- Adding value is not just about **manufacturing**, but also in the **marketing process** (advertising, promotion and distribution) that make the final product more desirable.
- It is very important for businesses to identify the processes that add value, so that they can enhance them for the benefit of the business.

There are three main types of processes:

1. **Job production**
2. **Batch production**
3. **Flow production**

Job Production

Job production is the creation of single items by either one operative or a team of peratives, e.g. producing a chair.

It is possible for a number of identical units to be produced in parallel under job production, e.g. several chairs of a similar type.

Smaller projects can also be seen as a form of job production, e.g. hand knitting a sweater, painting a room, cutting and styling hair, etc.

What are the benefits of job production?

The job is a unique product, which exactly matches the requirements of the customer, often from as early as the design stage.

Example:
Someone baking and decorating cakes will first discuss with a customer the sort of cake s/he would like.

A sketch would then be produced, according to the customer's demand.
Once the type of cake and the design are approved, the cake will be baked and decorated. The finished product is then given to the customer who will pay for a unique product.

As the work is concentrated on a specific unit, supervision and inspection of work are relatively simple.

Specifications for the job can change during the course of production to meet the customer's changing needs.

Example:
A printing company producing a menu for a cafeteria can easily modify the prices on customer's request before printing.

Working on a single unit job, coping with a variety of tasks and being part of a small team working towards the same aim would provide employees with a greater level of satisfaction.

Example:
Aircrew working for an airline would treat each flight as a specific job, with passengers requiring individual attention to their specific needs, e.g. for vegetarian dishes, wheelchair access to the flight, etc.

Batch Production

Batch production refers to a process in which products are manufactured in groups instead of individually.

The manufacture of products may go through several stages and requires that all products in a batch must be completed before moving to the next stage.

As one batch finishes, the next one starts.

Batch production is usually irregular (depending on the demand, season, availability of raw material, etc.)

Can you think of any examples of batch production?

Examples:

- In a bakery, a number of cookies may be baked at the same time in order to ensure supply is steady and that costs are minimised.

- Production of newspapers also requires batch production, since all the newspapers contain the same content and would be too expensive and time consuming to produce individually.

What do you think are the benefits of batch production?

The benefits of batch production are:

- It is ideal for a wide range of almost similar goods, which can use the same machinery on different settings.

Example: An insurance company sending out a batch of letters to customers.

- The range of machinery/equipment needed would not be too vast.
- Since purchasing of material and production are made in bulk, this would save money.
- It is an efficient process when compared to job production, therefore it saves time.
- It is ideal for seasonal products.
- It makes costing easy and provides a better information service for management.

Flow Production

- Flow production is a continuous process of parts and sub-assemblies passing on from one stage to another until completion.
- Units are worked upon in each operation and then passed straight on to the next work stage without waiting for the batch to be completed.
- The production line must work smoothly, with all stages up to their standards.
- For flow production to be successful there needs to be a continuity of demand. If demand varied, this could lead to a constant overstocking of finished goods.
- Although with modern robotics it is possible to create variations in products being produced through continuous flow techniques, typically such products will be relatively standardised.

- Achieving a smooth flow of production requires considerable pre-production planning to make sure that:
    - raw materials are purchased and delivered just-in-time,
    - sufficient labour is employed, and
    - there is continuous attention to quality throughout the production process.

What are the benefits of flow production?

The benefits of flow production are:

- Labour costs will be reduced due to the use of robotics.
- Deviations in the line can be quickly spotted through ongoing quality control techniques.
- Less waste due to less defected products.
- Production is continuous as there is no rest between operations.
- The need for storage space is minimal as raw material is used straight away and there is no resting time between operations.
- The physical handling of items is minimal.
- Investment in raw materials and parts are quickly converted into sales.
- Monitoring and control is relatively easy to carry out.

Key resources to start your business

- Starting a business is always a challenge; being properly prepared would help facing competition.
- However a strong business plan on its own is not enough.
- There are five resources that contribute to the success of a new enterprise:

1. **Financial resources**

- This is one of the most important elements to start a business.
- Even the most basic home business incurs start-up costs, including registration, business cards, and any required equipment/material.
- Funds can be obtained from:
  - personal accounts,
  - loans,
  - grants from financial institutions,
  - friends and relatives,
  - private investors, and
  - possibly the government.

1. **Human Resources**

The success of an organisation relies heavily on the skills and competences of its employees.

The hiring of experienced individuals with track records of excellence within their area of expertise ensures that work will be carried out efficiently and professionally.

Strong team members can be recruited using a variety of methods, namely:

Through recruitment companies, which could help with finding the right candidates

Through referrals from individuals whose judgment is trusted

3. **Educational Resources**

Gaining as much knowledge as possible prior to establishing a new business is crucial.

This would help the individual with:

- understanding the competition,
- gaining in-depth knowledge of the industry, and
- making smart decisions regarding the firm when necessary.

4. **Physical Resources**

- Whether a small home business or a retail operation with multiple locations, every organisation must have the appropriate physical resources to survive.

- This includes a proper workspace, working communication device, adequate information systems and effective marketing materials.

- This aspect of business planning can be one of the costliest.

- Hence, it is important for an entrepreneur to realistically assess his/her needs before making any purchases.

5. Emotional Resources

Starting a business can be extremely stressful for an entrepreneur to undertake.

To stay calm and motivated, it is important to have a support team that can give the person inspirations and guidance as needed.

This team may be composed of friends and family as well as a mentor or professional group.

 **Task**

Can you relate these resources to your business idea?

Concepts

Distribution

- Distribution is the process of making a product or service available for the consumer.

- This can be done directly by the producer or service provider, or using indirect channels with intermediaries.

- Before deciding on a distribution system his/her product/service, s/he needs to determine various factors, such as the type of product (especially if it is perishable), the market served, and the geographical segment.

- There are three main approaches to distribution:

1. Mass distribution
2. Selective distribution
3. Exclusive distribution

1. **Mass distribution**

- The producer's products are stocked in the **majority of outlets**.
- The marketer will seek out **plenty of intermediaries** to broad his/her market base.
- *Example:* Selling snack foods and drinks via a wide variety of outlets including supermarkets, convenience stores, vending machines, cafeterias and others.
- This is suitable for large businesses.

2. **Selective distribution**

- The producer relies on a **few intermediaries** to carry their product.
- This strategy is commonly observed for **more specialised** goods that are carried through specialist dealers.
- *Examples:* A brand of orthopaedic shoes, a range of appliances.
- Some prestige brands, like cosmetics and skincare, insist that sales staff are **trained** to use the product range.

3. **Exclusive distribution**

- The manufacturer chooses to deal with **one or very few intermediaries** only.
- The manufacturer therefore retains greater control over the distribution process.
- The distributor usually works closely with the manufacturer and adds value to the product through service level, after sales care or client support services.
- Example: Luxury goods retailers such as Gucci.

The Marketing Channels

- Some business operations may manufacture and sell products on a retail basis directly to consumers.
- Other manufacturers have established business relationships with wholesalers, distributors and retailers to sell their products to consumers.

Agents:

- Represent manufacturers on a commission basis.
- May sell to wholesalers, retailers, government agencies, hospitals, schools, etc.
- May represent several companies who produce compatible, but not competitive, products.
- *Example:* An agent may represent one company which manufactures skis, another which makes ski boots, and others which make sunglasses, caps, gloves and other clothing for the skier.

Brokers:

- Similar to agents but requiring additional certification and licensing.
- Need to have a greater knowledge of the industry and the various products available from the different companies in the market.
- Give customers different options and suggest the best products depending on their needs.
- A broker does not represent a single company like an agent, but serves the best interests of the customer, so they can make an informed decision.
- *Examples of agents and brokers:* insurance, real-estate

Distributors:

- Frequently have a business relationship with manufactures that they represent.
- Maintain buying agreements that enable them to cover a certain territory.
- Become the manufacture's direct point of contact for prospective buyers.
- Sell a manufacture's goods to wholesalers and retailers, rarely to customers.

Wholesalers:

- Generally buy a large quantity of products at discounted prices directly from distributors.
- Their goods are destined for retailers.

Retailers:

- Consist of small and large businesses selling products directly to consumers.
- To make profit, retailers search for products that coincide with their business objectives and find suppliers with the most competitive pricing.
- Generally buy products from distributors or wholesalers.
- *Example:* A retail merchant who wants to purchase a dozen lamps can contact lighting distributors to inquire about pricing.

Task

Ask yourself these questions to find out the distribution options for your product/service:

- *Where do buyers look for your product or service?*
- *If they look in a store, what kind?*
  A specialist boutique or in a supermarket, or both?
  Or online? Or direct, via a catalogue?
- *How can you access the right distribution channels?*
  Do you need intermediaries to reach your customers?

- *Do you need to use a sales force? Or attend trade fairs? Or make online submissions? Or send samples to catalogue companies?*

- *What do your competitors do, and how can you learn from that and/or differentiate?*

1.4 The Marketing mix – price and promotion

Concepts

The Marketing Mix

- As discussed in the previous session, the marketing mix is used to describe the different choices that organisations could opt for to be able to bring their product or service to the market.
- The 4Ps were mentioned, which are:

- Product (or Service)
- Price
- Place (also called Distribution)
- Promotion

During this session we are going to discuss Price and Promotion, but first watch these 2 commercials… What makes them powerful?

- Edeka commercial: https://www.youtube.com/watch?v=V6-0kYhqoRo
- iPhone commercial: https://www.youtube.com/watch?v=XB4cjbYywqg

Pricing Strategies

- Pricing is one of the most important elements of the marketing mix, as it is the only element of the marketing mix, which **generates a turnover** for the organisation.

- The other 3 elements of the marketing mix are the variable cost for the organisation:

- Product - It costs to design and produce your products.
- Place - It costs to distribute your products.
- Promotion - It costs to promote your products.

- Therefore price must support the other elements of the marketing mix.
- Pricing is challenging and must reflect **supply and demand** relationship.
- Pricing a product too high or too low could mean lost sales for the organisation.
- Companies may use a variety of pricing strategies, depending on their own unique marketing goals and objectives:

1. **Premium Pricing**
2. **Market Penetration Pricing**
3. **Economy Pricing**
4. **Price Skimming**
5. **Psychological Pricing**
6. **Bundle Pricing**

1. **Premium Pricing**

- Premium pricing strategy establishes a price **higher than the competitors**.
- It can be effectively used when:

- there is something **unique** about the product, or
- when the product is **first to market** and the business has a distinct competitive advantage.

- *Examples:*

- In farming, crops such as grapes could be of a high quality, produced on carefully cultivated land.
- Luxury brand selling leather goods, perfumes, etc
- Consultants

2. **Market Penetration Pricing**

- This strategy is designed to capture market share by entering the market with a price **lower than the competitors** to attract buyers.

- The idea is to **raise awareness** and get people to try the product.
- Even though this may initially create a loss for the company, the hope is that it will help to generate word-of-mouth and create awareness.
- *Examples:*

- Many new food companies give packages of their products away by sponsoring events and providing sample packs to attendees.
- Buy 2, get 1 free – the free one could be the new product, where the manufacturer does so in the hopes of creating interest in the new product.
- Giving out freebies with new products

3. **Economy Pricing**

- Companies take a **very basic**, **low-cost** approach to marketing.
- Nothing fancy, just the bare minimum to keep **prices low** and attract price-conscious consumers.
- Used mostly by food suppliers.
- With this strategy, businesses minimise the costs associated with marketing and production in order to keep product prices down.
- Very effective for large companies, but can be dangerous for small businesses due to the small profit on items.
- *Examples:* Walmart, Target, Lidl, Aldi

4. **Price Skimming**

- This involves setting rates **high during the introductory phase** of new products and services.
- The company then **lowers prices gradually** as competitor goods appear on the market.
- This allows businesses **to maximise profits on early adopters** before dropping prices to attract more price-sensitive consumers.
- It helps a small business recover its development costs and creates an illusion of quality and exclusivity when the new product or service is first introduced to the market.
- *Examples:* Apple, Samsung, PlayStation, GoPro

5. **Psychological Pricing**

- This refers to techniques that marketers use to encourage customers to respond on **emotional levels rather than logical ones**.
- *Example:* Setting the price of a watch at €199 is proven to attract more consumers than setting it at €200, even though the true difference here is quite small.
- One explanation for this trend is that consumers tend to put more attention on the first number on a price tag than the last.
- The goal of psychology pricing is **to increase demand by creating an illusion** of enhanced value for the consumer.

6. **Bundle Pricing**

- With bundle pricing, small businesses **sell multiple products for a lower rate** than consumers would face if they purchased each item individually.
- This is an effective way of **moving unsold items** that are taking up physical space
- Moreover, it can also **increase the value perception** in the eyes of the customers, since they are being given something for free.
- *Examples:*

- With a booking of five facials at a beauty salon, the customer is given a manicure treatment.
- A restaurant can includes a dessert with every main course and drink sold on a particular day of the week.

- Small businesses should keep in mind that the profits they earn on the higher-value items must make up for the losses they take on the lower-value product.

 **Task:**

Which pricing strategy do you think is best for your business idea?

Determining the right price for your product or service

Concepts

Cost-Plus Pricing

- Setting a price too high or too low for your target market can lead to lower sales and loss of profit.
- The exact strategy used depends on your company's marketing and profit objectives.
- Cost-plus pricing is useful when the production costs of a product or service are not clear in advance.
- In cost-plus pricing, the company first needs to determine the **break-even price** for the product.
- This is done by calculating **all the costs involved in the production, marketing and distribution** of the product.

Then a mark-up is set for each unit, based on:

- The profit the company needs to make,
- Its sales objectives, and
- The price it believes customers will pay.

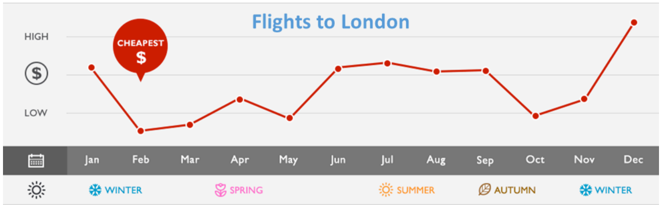
Worked example:

If the company needs a 15% profit margin and the break-even price is €10, the price will be set at €11.50 (€10 x 1.15).

Demand-based Pricing

- As the name indicates, there is no fixed price for the product or service, as the price depends on the market demand.
- If there is great demand for a particular food item, this means that there are many people purchasing or wanting to purchase the item.
- Prices increase when there is a high demand, and drop when the demand is low.

- *Example:* In the hospitality industry – Hotel rooms have higher rates in peak seasons as the demand is high. The same room would cost much less when the demand is low.
- *Other examples include:* flights, tickets for concerts/ shows/football matches, theme parks, ferry passes, parking fares, etc.



Competitive Pricing

- Competitive pricing is setting the price of a product or service based on what the competitors are charging.
- There are three competitive pricing strategies:

- Price is **the same** as that of your competitors
- Price is **slightly below** that of your competitors
- Price is **slightly above** that of your competitors

- If your price is **the same** as that of your competitors, you are putting the consumer into a direct product comparison situation.
- This means that if your product offers more features than that of your competitors, you have a chance of attracting more customers.
- If you price your product/service **below** that of your competitors, you are creating an attractive proposition for the consumer base, but you are also putting your business at risk of losing money.
- Pricing low needs to be very well thought-out to ensure that all costs are covered.
- If you price your product/service **above** that of your competitors, your customers would expect more in terms of the level of service or the product features.
- One should be sure that his/her product/service can actually offer this or else s/he would risk losing a large chunk of his/her consumer base to the competitors. (This is “premium pricing” mentioned earlier)

 **Task**

Evaluate the best pricing strategy for your product/service by answering these questions:

- *Have you covered your production and service delivery costs?*
- *Are your prices in line with your longer term business goals?*
- *What is the customer willing to pay?*
- *What kind of customer do I want to target?*
- *How should I react to my competitor's prices?*
- *Can I base my price on value?*
- *Should I offer different levels of products or services at different price points?*
- *Should I adjust my prices?*
- *Is the customer willing to pay more for my product?*
- *Should I bundle my products for a single price?*
- *Should I offer a discount?*
- *How does the customer want to buy my product or service?*
  (one-time purchase, annually, monthly, etc.)

Concepts

Promotion

- Promotion of a product/service consists of these elements:

1. Advertising
2. Public relations
3. Sales promotion
4. Personal selling

- They are used as tools to communicate to the target market and produce organisational sales goals and profits.
- Let's look at each element through the promotion that the new amusement park "*Fun Town"* adopted to attract customers.

1. **Advertising**

- Advertising is any form of **one-way communication** in which the company is identified.
- *Fun Town* realised that it needed to have a good advertising campaign because this would allow the company to reach a large number of people effectively.
- *Fun Town* used **television, radio, newspaper, social media and Internet ads** to introduce the target market to a grand opening of the amusement park.
- The park also used giant **billboards and e-mails** to reach other local customers.
- They promoted senior citizen discounts, family discounts and grand opening specials to lure the target market into trying a day at Fun Town.

2. **Public Relations**

- This is the communication between the organisation and the public. Its main purpose is to:

- help **build a positive public image** for a company,
- **supports new product** launches and sales,
- helps a company to **evaluate public attitudes**, and
- communicates the overall goals of the company.

- *Fun Town* has multiple days throughout the year where they donate a percentage of ticket sales to local charities.
- They also have days where they close the park down and invite disadvantaged youths to enjoy the rides for free.
- In addition, *Fun Town* uses their public relations team to handle any negative park issues. For example, if a visitor is injured on a ride, this team must evaluate public attitudes and communicate with the media that the appropriate corporate response occurred.

3. **Sales Promotion**

- This consists of methods of **stimulating consumer purchase**.
- This is usually based on a **short-term** or immediate goal.
- Examples of sales promotion items are **contests, giveaways, free samples or coupons**.
- *Fun Town* has invested heavily in sales promotion:

- They have had contests, like the first 1,000 people in the park would get a prize.
- They also had giveaways of free *Fun Town* water bottles, t-shirts, hats and canvas bags.
- They released a large number of coupons into the marketplace, such as BOGO (buy one, get one free) or 15% off for students, family coupons for 20% off the day, etc.

4. **Personal Selling**

- Personal selling is the process of communicating with a potential buyer **face-to-face** with the purpose of selling a product or service.
- This method of selling is more likely to be effective with certain types of products or services, especially those of small businesses.

- Personal selling allows the salesperson to target the message specifically to the audience and receive immediate feedback. In this way, it is more precise than other forms of promotion and often has a greater persuasive impact.

However personal selling cannot reach as many potential customers as advertising, and the cost of each contact is much higher.

Concepts

Product Packaging

Task

Why do you think packaging is important?

Product packaging

- Packaging could be considered as the 5th P as it plays an important role in the success or failure of the sales of the product.
- The purpose of product packaging is to **protect the product from damage** during transportation and while the product sits on retail shelves.
- How a product is packaged may be what **attracts the consumer** to take a look on the product as is sits on store shelves.
- For this reason, many companies conduct extensive research on colour schemes, designs and types of product packaging that is the most appealing to its intended consumer.
- Packaging also portrays **information** about the product. Outside packaging may contain directions on how to use the product.
- Food packaging contains ingredients and nutritional information about the product. This information can help to sell the product because it allows potential customers to obtain the necessary information they need to make a purchase decision.
- Packaging can also differentiate one brand of product from another brand, through logos, colour schemes, etc.

- This makes products easily recognisable for the consumer to grab while rushing along the shelves.
- If the product packaging changes, it may alter the brand perception of the company. This doesn't mean that the consumer would not still purchase the product, but it may delay the purchase until the person is able to identify the product according to its new packaging.

1.5 Introduction to Budgets

Concepts

What is a budget?

This is a detailed statement outlining estimated project costs to support the project.

A budget should include all the Direct Costs and Indirect Costs required to carry out the project.

Direct Costs – Expenses that are specifically associated with the product or service, such as purchasing raw material.

Indirect Costs – Expenses that cannot be specifically identified with the product or service, such as the use of facilities.

Task:

Group work: Choose any product of your choice and make a list of direct and indirect costs involved in its production.

Direct Costs	Indirect Costs
Physical assets (equipment, machinery, vehicles for distribution…)	Rent and utilities (electricity, water, telephones…)
Maintenance and operating costs	IT systems and networks
Materials	Management and Accounts
Direct labour costs (salaries and benefits)	Indirect labour costs (idle time, paid sick leave, time spent on indirect jobs)
Scrapped and reworked product	Legal functions
Direct supervision of personnel	Warranty and guarantees
Staff training	Quality assurance
	Insurance policies
	Marketing and publicity
	Taxes
	Purchasing and contracting
	Safety and security

Cost-Benefit Analysis

- Prior to taking on a new project, conducting a cost-benefit analysis would help evaluating all the potential costs and revenues that may be generated if the project is completed.
- The outcome of the analysis will determine whether the project is financially feasible or if another project should be pursued.
- A cost-benefit analysis is carried out in three steps:

1. Compile a comprehensive list of all the costs and benefits associated with the project.

- Costs should include direct and indirect costs, intangible costs, opportunity costs and the cost of potential risks.
- Benefits should include all direct and indirect revenues and intangible benefits, and increased sales from customers.

Additional info:

Direct costs: products from suppliers

Indirect costs: Electricity bills

Intangible costs: permits, insurance

Opportunity costs: investments

Costs of potential risks: lack of skilled employees requiring training

Direct revenue: less defects in products

Indirect revenues: savings on electricity

2. Apply a common monetary measurement to all items on the list. Be realistic; do not underestimate costs or overestimate benefits.

3. The final step is to quantitatively compare the results of the costs and benefits to determine if the benefits outweigh the costs.

- If so, then the decision is to go forward with project.

- If not, a review of the project is to be carried out to see if adjustments can be made to either increase benefits and/or decrease costs to make the project viable. If not, the project may be abandoned.

Worked Example at Cost benefit Analysis

Cost Benefit Analysis for Computerised Customer Service System				
Costs				
Category	**Item**	**Qty**	**Price**	**Total**
Equipment	Workstations c/w software	10	£2,500	£25,000
	Server	1	£3,500	£3,500
	Printers	3	£1,500	£4,500
	Network cable installation	1	£4,500	£4,500
	Specialised software (site licence)	1	£16,000	£16,000
Training	Basic computer skills	8	£400	£3,200
	Office software	8	£400	£3,200
	Customer service system	12	£750	£9,000
Other	Man hours lost	320	£25	£8,000
	Sales lost during initial phase (est)		£40,000	£40,000
			Total Cost:	**£116,900**
Benefits (estimated per annum)				
Postal campaigns and telesales				£60,000
Lead conversion				£45,000
Customer retention				£35,000
Accuracy of client information				£15,000
Improvements in management efficiency				£30,000
			Total Benefit:	**£185,000**

The 10 steps to develop a successful budget

1. Strategic Plan

- Every organisation should have a goal to accomplish. This is written in the Vision and Mission Statement.
- A strategic plan is the HOW the organisation plans to achieve its mission.
- The first step in the budgeting process is having a written strategic plan. This ensures that organisational resources are used to support the strategy and development of the organisation.

2. Business Goals

- **T**o implement its strategic plan, an organisation takes the annual business goals and develop them to be able to achieve them.
- The budget provides the financial resources to achieve these goals.
- *Example:* An organisation needs to expand its premises. There need to be money budgeted for this to happen.

3. Revenue Projections

- Revenue (profit) projections should be based on past financial performance, as well as projected growth income.
- The projected growth may be tied to organisational goals and planned initiatives that will initiate business growth.
- *Example:* If there is a goal to increase sales by 10%, those sales projections should be part of the revenue projections for the year.

4. Fixed Cost Projections

- Projecting fixed costs are predictable monthly costs that do not change, such as employee compensation costs, facility expenses, utilities, mortgage/rent payments, insurance, etc.
- Fixed costs do not change and are a minimum expense that need to be funded in the budget.

5. Variable Cost Projections

- Variable costs are costs that fluctuate from month to month, such as supply costs, overtime costs, etc. These are expenses that should be budgeted and controlled.

- *Example:* A temporary increase in overtime due to Christmas sales should be budgeted.

6. Annual Goal Expenses

- Projects related to goals should also be given budgets and incorporated into the annual budget.
- Projections of costs should be identified, laid out and incorporated into the departmental budget that is responsible for completing the goal.
- *Example:* If the sales department has a goal of increasing sales by 10%, costs associated with the increased sales (additional marketing materials, travel, entertainment) should be incorporated into that budget.

7. Target Profit Margin

- Profits are important for all organisations and healthy profit margins are a strong indicator of the strength of an organisation.
- Every organisation, whether they are for-profit or not-for-profit, should have a targeted profit margin. Profit margins allow for reinvestment into the facilities and development of the organisation.

8. Board Approval

- The management of the organisation should approve the budget and keep current with budget performance.
- The management should also review monthly financial statements for the following reasons.

- To monitor budget performance
- To be familiar with all expenditures
- To safeguard the organisation against misappropriation of funds or fraud.

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9. Budget Review

- A budget review committee should meet on a monthly basis to monitor performance against goals.
- This committee should review budget variances and assess issues associated with budget overages.
- It is important to do this on a monthly basis so there can be a correction to overspending or modification to the budget if needed.
- Waiting until the end of the year to make corrections could have a negative impact on the final budget outcome.

10. Dealing With Budget Variances

- Budget variances should be reviewed with the responsible department manager and questions should be raised as to what caused the variance.
- Sometimes unforeseen situations arise that cannot be avoided so it is also important to have an emergency fund to help with those unplanned expenditures.

- Example: If a system suddenly goes down and needs to be replaced, this would be a budget variance that needs to be funded.
- Good budgeting processes can help the organisation to develop, while poor budgeting and monitoring of budgets can blindside an organisation and affect its long-term financial health, viability, and eventually, customers.

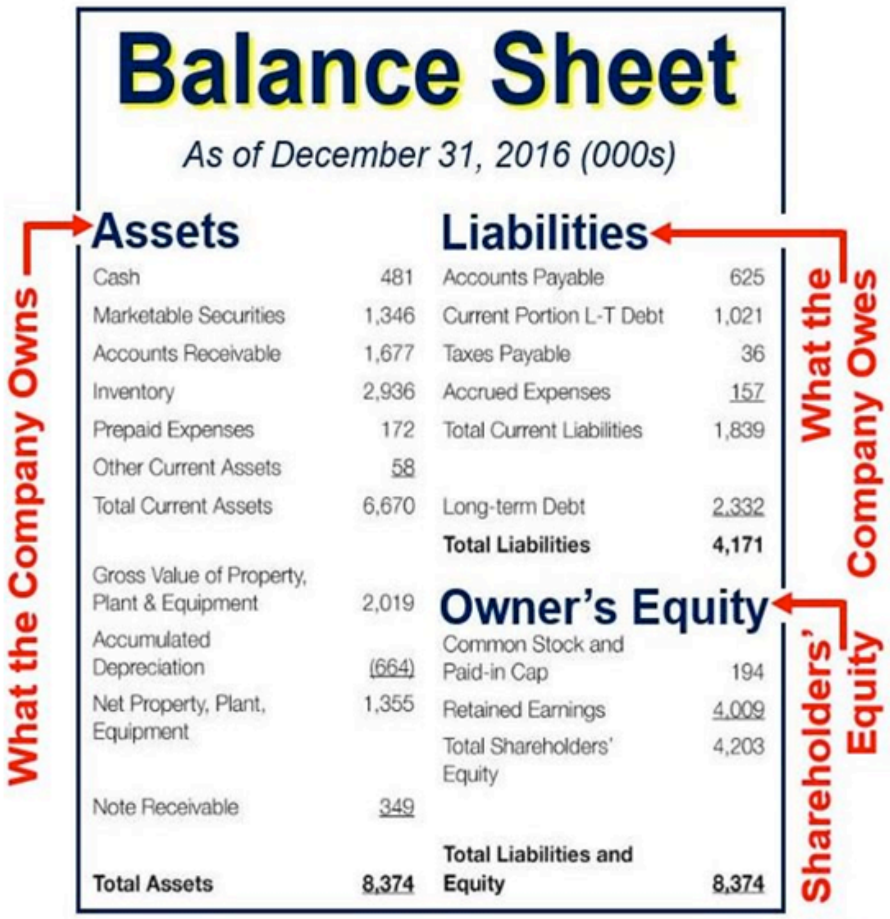
Defining the Capital Needed to Start a Business

Some definitions:

A balance sheet:

- This is a financial statement that gives investors an idea as to what the company owns and owes at a specific point in time.
- It is made up of three segments which are:

- the company's assets,
- the company's liabilities, and
- the amount invested by shareholders (owner's equity).



Balance Sheet

As of December 31, 2016 (000s)

Assets		Liabilities	
Cash	481	Accounts Payable	625
Marketable Securities	1,346	Current Portion L-T Debt	1,021
Accounts Receivable	1,677	Taxes Payable	36
Inventory	2,936	Accrued Expenses	157
Prepaid Expenses	172	Total Current Liabilities	1,839
Other Current Assets	58		
Total Current Assets	6,670	Long-term Debt	2,332
		Total Liabilities	**4,171**
Gross Value of Property, Plant & Equipment	2,019	**Owner's Equity**	
Accumulated Depreciation	(664)	Common Stock and Paid-in Cap	194
Net Property, Plant, Equipment	1,355	Retained Earnings	4,009
		Total Shareholders' Equity	4,203
Note Receivable	349		
Total Assets	**8,374**	**Total Liabilities and Equity**	**8,374**

Assets:

- An asset is a **resource with economic value** that a company owns with the expectation that it will provide future benefit.
- Assets are reported on a company's balance sheet.
- An asset can be thought of as something that in the future can generate **cash flow, reduce expenses, improve sales and adds value to the firm**.

Liabilities:

- A liability is a company's **financial debt** or obligations that arise during the course of its business operations.
- Liabilities are settled over time through the transfer of economic benefits including money, goods or services.
- Liabilities include loans, mortgages, etc.
- These are recorded on the balance sheet.

Owner's Equity:

- This is the value of an asset less the amount of all liabilities on that asset.
- It can be represented with the accounting equation:

Assets - Liabilities = Equity

- In finance in general, you can think of equity as one's degree **ownership** in any asset after all debts associated with that asset are paid off.
- *Example:* A car or house with no outstanding debt is considered entirely the owner's equity because he or she can readily sell the item for cash, and pocket the resultant sum.

Capital requirement:

- This is the sum of funds that your company needs to achieve its goals.
- Plainly speaking: *How much money do you need until your business is up and running?*
- You can calculate the capital requirements by adding **founding expenses** (notary fees, legal fees, registration fees, real estate broker costs, etc.), **investments** and **start-up costs** together.
- By subtracting your equity capital (owner's equity) from the capital requirements, you calculate how much external capital you are going to need:

Equity – Capital requirements = External capital required

- Capital requirements planning is closely linked with all other parts of your business plan, because its follow-up costs have to be considered in the planning.

Considerations:

The startup expenses have to be considered. For most startups, revenue in the first few months is not sufficient to cover the cost. You are usually busy acquiring customers and processing orders, before you can finally write your first invoices and get paid. You still need to be able to compensate for expenses in these difficult first months. The capital requirement for the startup phase is equivalent to the minimum of the monthly cash and cash loss.

Do not forget to consider interest expenses and repayments in your capital requirement.

It could be necessary to plan for higher capital requirements, so you can satisfy both your operating costs and mortgage payments.

Plan a reserve for contingencies, such as delayed orders, higher renovation expenses or new, unplanned assets. Calculate how much deviation a worst-case scenario would result in, for both the investment and the startup phase.
