

SIMPLE STEPS FOR STARTING YOUR BUSINESS

Session 4: Financial Matters



YOUR PRESENTER



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As a SCORE mentor, he focuses on helping clients investigate initial transaction tax/fee exposure and establish the needed compliance processes to keep their businesses out of tax regulatory trouble.

ABOUT SCORE

As a resource partner of the SBA, we help small businesses by:



Providing free
business advice and
mentoring



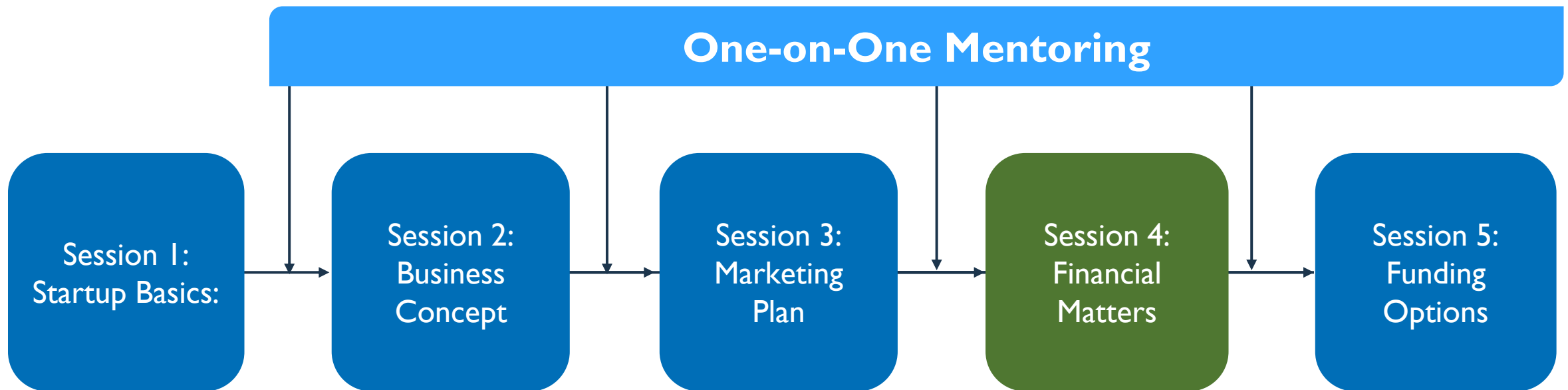
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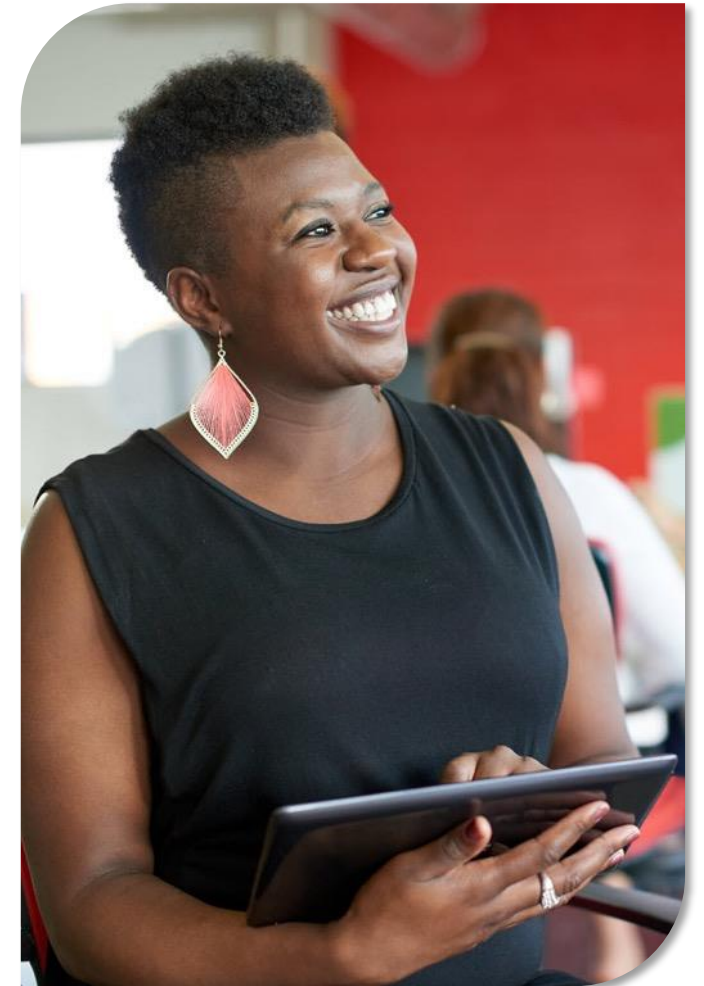
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Simple Steps for Starting Your Business Series



AGENDA

- Financial planning
- Financial projections
- Forecasting sales
- Pricing fundamentals
- Understanding financial statements
- Recordkeeping



THE IMPORTANCE OF FINANCIAL PLANNING

- Match business concept with personal income goals
- Gain a better understanding of financial risks and rewards of entrepreneurship
- Figure out how much money you will need to start and run your business
- Identify development and startup costs, ongoing operations expenses and funds needed to finance the business
- Create a plan to help guide future business decisions and monitor results
- Enables you to communicate with stakeholders (investors, lenders, employees, etc.) about the business's finances

THE IMPORTANCE OF FINANCIAL PLANNING

- A financial plan is your forecast of sales, costs, profits and assets for the first year or more after startup
- Use it to predict how successful your new business might be and to understand where your money will be allocated and where it will come from
- Helps you examine the feasibility of your numbers and organize your business finances
- It's a:
 - Modeling tool that helps you evaluate variable factors
 - Benchmark for tracking progress
 - Blueprint you can adjust to achieve your financial goals



Common Concerns:

- The spreadsheets look complicated. I don't think I can do this on my own.
- I don't understand all the figures and math.
- This is overwhelming.
- Can I start my business without a financial projection model?

Businesses don't plan to fail – they often fail to plan!



The first six worksheets are:

1. Required Startup Funds
2. Salaries and Wages
3. Fixed Operating Expenses
4. Projected Sales Forecast
5. Projected Sales Forecast (2)
6. Cash Receipts – Disbursements

FINANCIAL PROJECTIONS TEMPLATE REQUIRED STARTUP FUNDS

Fixed Assets	Amount
Real Estate-Land	100,000
Real Estate-Buildings	30,000
Leasehold Improvements	15,000
Equipment	5,000
Furniture and Fixtures	2,000
Vehicles	20,000
Other	
Total Fixed Assets	\$ 172,000

Operating Capital	Amount
Pre-Opening Salaries and Wages	-
Prepaid Insurance Premiums	2,500
Inventory	30,000
Legal and Accounting Fees	3,000
Rent Deposits	-
Utility Deposits	300
Supplies	1,000
Advertising and Promotions	2,000
Licenses	-
Other Initial Start-Up Costs	-
Working Capital (Cash On Hand)	3,000
Total Opening Capital	\$ 41,800
Total Required Funds	\$ 213,800

- How much do you need?
- What will it be used for?
- Also consider starting costs for employees: salaries, taxes, benefits
- This develops the Assets part of opening Balance Sheet

SOURCES OF FUNDING

Sources of Funding	Percentage	Totals
Owner's Equity	53.79%	115,000
Outside Investors	0.00%	-
Additional Loans or Debt		
Commercial Loan	15.81%	33,800
Commercial Mortgage	23.39%	50,000
Credit Card Debt	0.00%	-
Vehicle Loans	7.02%	15,000
Other Bank Debt	0.00%	-
Total Sources of Funding	100%	\$213,800
Total Funding Needed		

SALARIES AND WAGES

Employee Types	Number of Owners /Employees	Average Hourly Pay (to 2 decimal places, ex. \$15.23)	Estimated Hrs./Week (per person)	Estimated Pay/Month (Total)
Owner(s)	1	23.08	40	\$ 4,000
Full-Time Employees	3	5.77	40	\$ 3,000
Part-Time Employees	0			\$ -
Independent Contractors	0			\$ -
Total Salaries and Wages	4	\$ 28.85	80	\$ 7,000

Payroll Taxes and Benefits	Wage Base Limit	Percentage of Salary/Wage	Estimated Taxes & Benefits/Month (Total)
Social Security	\$ 110,111	6.20%	\$ 434
Medicare	--	1.45%	\$ 102
Federal Unemployment Tax (FUTA)	\$ 7,000	0.80%	\$ 19
State Unemployment Tax (SUTA)	\$ 7,000	3.45%	\$ 81
Employee Pension Programs	--	2.85%	\$ 200
Worker's Compensation	--	0.00%	\$ -
Employee Health Insurance	--	0.00%	\$ -
Other Employee Benefit Programs	--	0.00%	\$ -
Total Payroll Taxes and Benefits		14.75%	\$ 834
Total Salaries and Related Expenses			\$ 7,834

FIXED OPERATING EXPENSES

	January
Expenses	
Advertising	900
Car and Truck Expenses	800
Commissions and Fees	-
Contract Labor (Not included in payroll)	-
Insurance (other than health)	400
Legal and Professional Services	150
Licenses	-
Office Expense	250
Rent or Lease -- Vehicles, Machinery, Equipment	200
Rent or Lease -- Other Business Property	300
Repairs and Maintenance	
Supplies	300
Travel, Meals and Entertainment	300
Utilities	500
Miscellaneous	200
Total Expenses	\$ 4,300

There are 5 elements that comprise a financial plan:

1. Required startup funds
2. Salaries and wages
3. Fixed operating expenses
4. Projected sales forecast
5. Cash receipts and disbursements



REQUIRED STARTUP FUNDS

Here are some factors to consider as you calculate your required startup funds.

- How much money do you need to get your business up and running?
- What will it be used for?
- What are your expected sources of capital?
- How much will be financed by you and your partners, and how much by other sources?

SALARIES & FIXED OPERATING EXPENSES

SALARIES AND WAGES:

- Include wages for employees and the business owners
- Remember to include taxes on wages
- Typically, mandatory and voluntary fringe benefits total about 30% wages

FIXED OPERATING EXPENSES:

- Fixed operating expenses are the administrative expenses necessary to run the business
- These include costs such as insurance, rent, utilities, sales commissions, advertising, taxes and licenses



What unit categories make sense for your business?

- You need to figure out if you're selling:
 - Products
 - Services (hours or fixed price)
 - Combination (packages)
- Determine what makes up your “unit of sale”
- Determine your direct cost per unit
- Determine your price per unit

SALES UNIT DATA SOURCES



Sales unit category or grouping

- Product, service, package, volume, customer type

Unit cost and price

- Build up from sources
- Subcontract
- Competition

Sales volume in units

- Estimate from market
- Competition
- Back in number to make business profitable

Smart Pricing Strategy:

Starts with understanding the market price: the average price charged by your competitors and the price at which their product or service is generally valued in the marketplace. You can then choose to charge a:

- Premium price (if you have a superior, value-added product or service)
- Discount price (which is generally hard for small companies to sustain)
- Similar price to your competitors' (market price)

Elements of pricing:

- Premium price (if you have a superior, value-added product or service)
- Consumer reaction
- Competition
- Cost
- Credit terms and discount

PRICING CONSIDERATIONS

Channel:

You may need to vary prices based on your sales channel/s. For example, if you sell directly to consumers and retailers/resellers, you'll have to charge the retailers less so they can sell it for the same retail price you do and still make a profit. If you sell to businesses, remember small businesses have lower budgets than big corporations.

Mark-up on Cost:

Calculating pricing based on a markup of your cost to produce the product/service.

Bundling:

Charging lower prices when customers buy more than one product or service

Target Market:

If you market to luxury buyers or your clients need extra attention, build the additional costs into your prices.

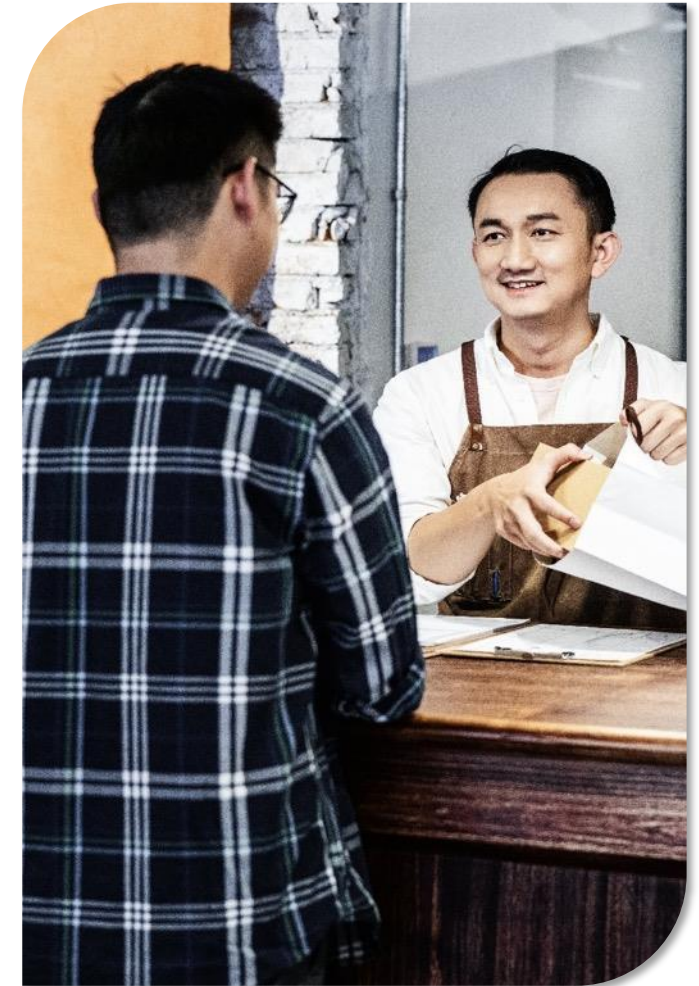
PRICING CONSIDERATIONS

Promotional Pricing:

- Consider offering sales or promotional prices to attract new customers or encourage customers to buy more

Introductory Pricing:

- New companies often offer introductory pricing, to entice consumers to take a chance on doing business with them



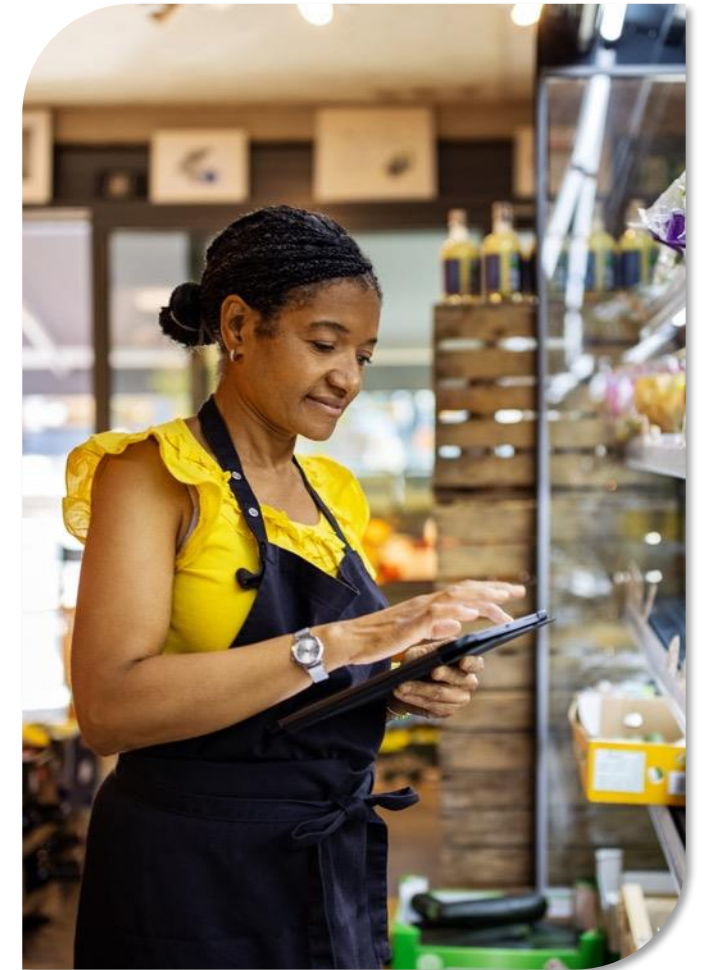
SETTING YOUR INITIAL PRICES

Consider the **COGS** (cost of goods sold):

The direct costs of producing the products. Add to that total to create a profit margin.

When pricing a service, consider standard industry practices, plus market prices.

What do your competitors charge? Will you will match it, beat it or charge more?



ADJUSTING YOUR PRICES

Monitor customer demand. Is your product or service selling? If not, rethink your pricing.

- Compare your sales to the competition.
- Are your sales similar to, better than or worse than theirs?
- Ensure you're providing value commensurate with your price.
- Consider using credit terms or bundling products/services to make your offerings more attractive.
- Unless you're experiencing increased demand, before increasing prices, look for ways to reduce costs.

DON'T GET INTO A PRICE WAR

- Setting your prices too low may sound like a great way to boost sales
- But prices that are too low disrupt the marketplace by leading to a price war
- Unnaturally low prices can't be sustained—and in a price war, the new business suffers the most
- This is one war you can't win, so don't start one



GROSS PROFIT MARGIN

What is gross profit margin?

- Sales (\$) minus direct cost of sales

Why is it important?

- Requires you to cost out what you're selling
- Helps you determine adequacy of gross price for what you're selling



PROJECTED SALES FORECAST

Product Lines I	Year I Totals	January
Recycled Products		
Goods Sold	125	6
Total Sales	\$250,000	\$11,000
Total CIGS	\$137,500	\$6,050
Total Margin	\$112,500	\$4,950

ADDITIONAL INPUTS

Accounts Receivable (A/R) Days Sales Outstanding			
Percent of Collections	Year 1	Year 2	Year 3
Paid within 30 days	30%	30%	30%
Paid between 30 and 60 days	30%	30%	30%
Paid in more than 60 days	40%	40%	40%
Allowance for bad debt	0%	0%	0%
This should equal 100% ---->	100%	100%	100%

Accounts Payable (A/P)			
Percent of Disbursements	Year 1	Year 2	Year 3
Paid within 30 days	0%	0%	0%
Paid between 30 and 60 days	100%	100%	100%
Paid in more than 60 days	0%	0%	0%
This should equal 100% ---->	100%	100%	100%

Income Statement:

- Gross profit margin and overhead expense management

Cash Flow Statement:

- Funds management

Balance Sheet:

- A/R, Inventory & A/P management

Breakeven Analysis:

- Use of industry comparison ratios



WHY 3 FINANCIAL STATEMENTS?



1. Income statement

- How long to reach profitability?
- Do I make a profit or loss?

2. Cash flow statement

- Do I have enough sources of funds to operate, sustain & grow the business?

3. Balance sheet

- What are my assets & liabilities?
- How much am I worth?

INCOME AND EXPENSE STATEMENT (P&L)

	January	February	March
Revenue			
Plant Mix	10,000	10,000	10,000
Plant Mix – Web	-	-	-
Plant Mix – Distant Nursery	-	-	-
Product 4	-	-	-
Product 5	-	-	-
Product 6	-	-	-
Total Revenue	\$ 10,000	\$ 10,000	\$ 10,000
Cost of Goods Sold			
Plant Mix	5,500	5,500	5,500
Plant Mix – Web	-	-	-
Plant Mix – Distant Nursery	-	-	-
Product 4	-	-	-
Product 5	-	-	-
Product 6	-	-	-
Total Cost of Goods Sold	\$ 5,500	\$ 5,500	\$ 5,500
Gross Margin	\$ 4,500	\$ 4,500	\$ 4,500
Payroll	\$ 7,834	\$ 7,834	\$ 7,834

CASH FLOW PROJECTION

	January	February	March
Beginning Balance	\$ 3,000	\$ 3,000	\$ 3,000
Cash Inflows			
Cash Sales	3,000	3,000	3,000
Accounts Receivable	-	3,000	7,000
Total Cash Inflows	\$ 3,000	\$ 6,000	\$ 10,000

Cash Outflows			
Investing Activities			
New Fixed Asset Purchases	-	-	-
Additional Inventory			
Cost of Goods Sold	-	5,500	5,500
Operating Activities			
Operating Expenses	4,300	4,300	4,300
Payroll	7,834	7,834	7,834
Taxes	-	-	-
Financing Activities			
Loan Payments	1,346	1,346	1,346
Owners Distribution			
Line of Credit Interest		70	157
Line of Credit Repayments			
Dividends Paid			

CASH FLOW PROJECTION

	January	February	March
Beginning Balance	\$ 3,000	\$ 3,000	\$ 3,000
Cash Inflows			
Cash Sales	3,000	3,000	3,000
Accounts Receivable	-	3,000	7,000
Total Cash Inflows	\$ 3,000	\$ 6,000	\$ 10,000

Cash Outflows			
Investing Activities			
New Fixed Asset Purchases	-	-	-
Additional Inventory			
Cost of Goods Sold	-	5,500	5,500
Operating Activities			
Operating Expenses	4,300	4,300	4,300
Payroll	7,834	7,834	7,834
Taxes	-	-	-
Financing Activities			
Loan Payments	1,346	1,346	1,346
Owners Distribution			
Line of Credit Interest		70	157
Line of Credit Repayments			
Dividends Paid			

BALANCE SHEET

Balance Sheet	12/31/2022	12/31/2023		12/31/2022	12/31/2023
Assets			Liabilities and Equity		
Cash	\$22,455	\$67,250	Accounts Payable	\$9,605	\$8,250
Accounts Receivable	\$100	\$575	Deposits taken	\$9,000	\$10,000
Inventory	\$70,000	\$51,250	Accrued Payroll	\$4,300	\$4,519
Supplies	\$15,000	\$8,250	Loan payments due	\$8,500	\$8,500
Prepaid Expenses	\$500	\$2,200			
Total Current Assets	\$108,055	\$129,525	Total Current Liabilities	\$31,405	\$31,269
Equipment and tools	\$35,000	\$42,500	Loans from Family	\$25,000	\$24,000
Leasehold Improvements	\$25,000	\$23,000	Loans from Banks	\$14,500	\$22,500
Other Fixed Assets			Total Liabilities	\$70,905	\$77,769
Total Fixed Assets	\$60,000	\$65,500	Equity	\$97,150	\$117,256
Total Assets	\$168,055	\$195,025	Total Liabilities and Equity	\$168,055	\$195,025

- Assets = What the business owns
- Liabilities = What the business owes
- Owners' Equity = The amount contributed by the owners + the amount earned (lost)
- Assets = Liabilities + Owners' Equity

BREAKEVEN ANALYSIS

Gross Margin % of Sales	
Gross Margin	\$ 151,300
Total Sales	\$ 347,000
Gross Margin/Total Sales	43.6%
Total Fixed Expenses	
Payroll	\$ 94,013.18
Operating Expenses	\$ 71,068.69
Operating + Payroll	\$ 165,082
Breakeven Sales in Dollars (Annual)	
Gross Margin % of Sales	43.6%
Total Fixed Expenses	\$ 165,082
Yearly Breakeven Amount	\$ 378,608
Monthly Breakeven Amount	\$ 31,551

Breakeven is where:

Gross Profit Margin

=

Total Expenses

OR

Sales Volume = 0 Profit

**Breakeven Sales \$ = Fixed
Cost / GM%**

The spread between breakeven and sales forecast is very important (the wider the better).

Ratios	Year One
Liquidity	
Current Ratio	0.5
Quick Ratio	0.3
Safety	
Debt to Equity Ratio	1.4
Debt-Service Coverage Ratio - DSCR	-0.1
Profitability	
Sales Growth	0.0%
COGS to Sales	56.4%
Gross Profit Margin	43.6%
SG&A to Sales	42.0%
Net Profit Margin	-4.8%
Return on Equity (ROE)	-17.0%
Return on Assets	-7.0%
Owner's Compensation to Sales	13.8%
Efficiency	
Days in Receivables	38.9
Accounts Receivable Turnover	9.3
Days in Inventory	55.2
Inventory Turnover	6.5
Sales to Total Assets	1.4

Test the feasibility of your plans by conducting research:

- RMA annual statement studies
- Industry norms and key business ratios (D&B)
- Financial ratios, business statistics & benchmarks: www.bizstats.com

FINANCIAL STATEMENT ANALYSIS



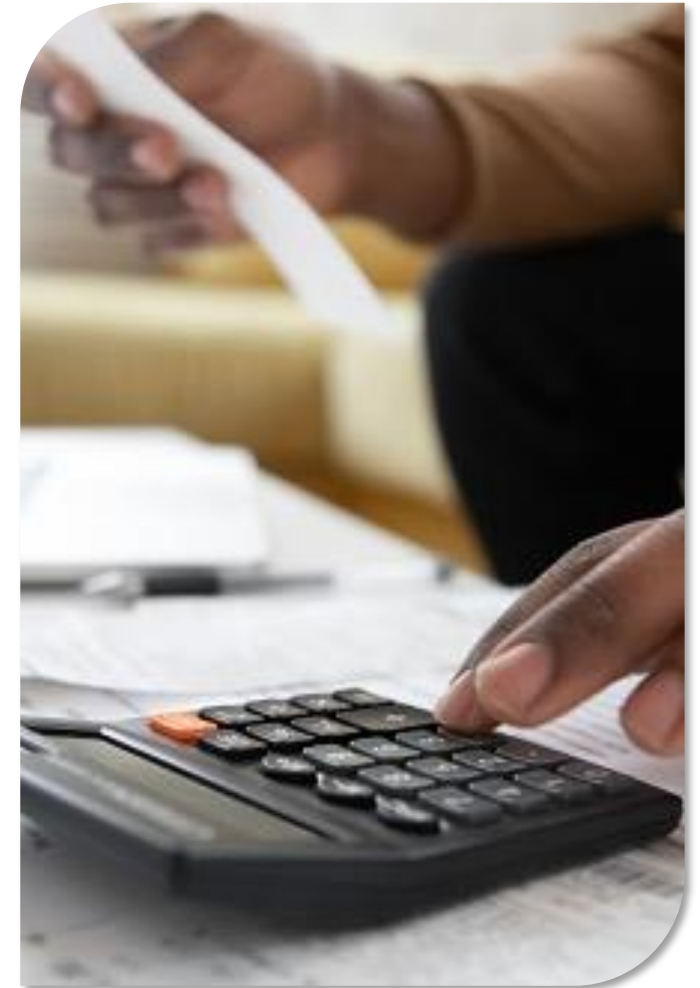
- Monthly preparation and review of financial statements (within 10 days after the close of the month)
- Ratio analysis
- A/R and A/P analysis
- Comparative benchmark analysis

RECORDKEEPING AND FINANCING



- Preparation is essential
- Lenders want facts, research and accurate projections
- Whether you seek funding now or in the future, your records should be in order

- Manual vs. computerized
- Choosing the system
- Hiring a bookkeeper vs. DIY
- Training and educating yourself in accounting and understanding financial statements
- Working with your accountant



Questions?

NEXT STEPS

- Sign up for other [Simple Steps for Starting Your Business](#) and [Small Business Essentials](#) webinars
- Review the Simple Steps for Starting Your Business [Workbook](#)
- Find other SCORE resources for small businesses at score.org/templates-resources
- Book an appointment with a SCORE mentor today at score.org/find-mentor



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