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Shell *LiveWIRE* Business Plan Guidelines

Shell *LiveWIRE* is sponsored by Shell Australia and supported by Rotary International and the State and Territory governments of Australia.

Shell *LiveWIRE* is based on the successful Shell UK Ltd initiative that began in 1982. The program commenced in Australia in 1987 in Western Australia and since then has grown and expanded to include all the States and Territories of Australia.

The program has been set up to assist young people between the ages of 18 and 28 to start their own business. The aim is to encourage each *LiveWIRE* entrant to develop a comprehensive business plan, detailing the relevant aspects of their prospective business prior to committing any money. *LiveWIRE* considers that the creation of a business plan should be the first step when setting up a business and that the plan should be updated from year to year thereafter. Prizes to the value of \$90,000 will be awarded this year to budding young entrepreneurs. There are individual State prizes plus a national prize of a trip for two to the UK to be won.

LiveWIRE entrants are required to make a serious commitment to developing a comprehensive business plan. It may be, after thorough investigation, that a *LiveWIRE* entrant discovers their business idea is not realistic. In such cases, and when the allocated mentor agrees that the business idea would not work, the *LiveWIRE* entrant has still achieved something valuable – they have gained experience, know what is required for any future business idea and, importantly, have not wasted any money.

There is no financial cost to join the Shell *LiveWIRE* program. However, it is expected that you make a serious commitment to work with your mentor on the development of your business plan. Mentors commit valuable personal time to help you develop your business plan. The *LiveWIRE* program cannot function without mentor support. Should a *LiveWIRE* entrant just 'drop out' of the program, they would be undermining the scheme and perhaps preventing the program from being offered to future young people who want to succeed in developing their business plans.

The following guidelines, together with support and direction from your mentor, will assist you in constructing and writing an appropriate business plan ready to be submitted for judging by the Shell *LiveWIRE* judging panel in each State and Territory.

Introduction

Essential components in your business plan include:

- *The summary* – an overview of your proposed business venture.
- *The product or service* – on which your business is based.
- *Industry and market analysis* – the market, the customers and the competition.
- *Marketing strategy* – promotion, advertising and public relations.
- *Finance* –
 - capital requirement;
 - cash flow forecasts (more than one year and best/worst case scenarios); and
 - profit and loss projections (more than one year and best/worst case scenarios).
- *Managing and operating the business* – the people, their skills and competencies.
- *Appendices* – verifiable data supporting your identified business opportunity.

Completed business plan submissions should be addressed to the Shell LiveWIRE Director in your State or Territory at the relevant address provided below.

Victoria
C/- Shell Australia Limited
1 Spring Street, Melbourne 3000

New South Wales
C/- Shell Australia Limited
NSW State Office
Durham Street, Rosehill 2142

Western Australia
C/- Shell Australia Limited
22 Bracks Street, North Fremantle 6159

Tasmania
C/- Rotary International
138 James Street, Devonport 7310

Queensland
Shell Australia Limited
PO Box 1456, Brisbane 4001

South Australia
C/- Shell Australia Limited
Elder Road, Birkenhead 5015

Northern Territory
C/- Shell Australia Limited
38 McMinn Street, Darwin 0800

*Shell LiveWIRE program
closing dates will be advised
at a later date and will be strictly adhered to.*

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1. The summary

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The first part of your Shell *LiveWIRE* business plan is *the summary*.

The summary describes to the audience who you are, what type of business you wish to start, where the business will be located, how much capital the business will require, how much and what type of funding the business will require, how the funds will be spent and how you propose to repay those funds.

It is important that *the summary* addresses the following criteria. The information provided will enable the Shell *LiveWIRE* judges to gain an overview of your business plan, prior to reading your full submission.

However, the summary is prepared last, after all the elements of the business plan been researched and completed.

Describe who you are

Provide an introductory 'snapshot' of yourself and any key people involved in the operation of your business. Outline your core competencies and experience.

Design your information to answer the question: Why will I, or my business partners and I, succeed in this business?

Describe the type of business proposed

State clearly and simply what products or services you are going to sell, to whom it will be sold and for what purpose it will be used. Explain why customers will buy your products or services and at what price.

Describe the business location

Explain where you will locate the proposed business and the benefits of the location.

Outline how much capital is required to establish your business

Outline the total amount of capital you calculate the proposed business will require, how that capital will be used and provide a breakdown of fixed assets and expenses.

Refer to *Appendix 1 – Business establishment worksheet*.

Outline how much and what type of finance is required

You may provide part of the total capital required to establish your business and the remainder of the finance may be sourced from someone else. This someone else may be a bank manager, friend or family member.

Provide a clear statement of how much finance is required and from whom it will be obtained.

Outline how you propose to repay any business loans

In the event you borrow money to finance the business, you will be required to repay the loan.

Set out clearly how you propose to repay the loan, by stating the repayment date, repayment amount, duration of repayments and interest rates payable on the business loan monies.

2. Your business and the market

2.1 Your business idea

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You know you have a great feeling about *your business idea*...
Everyone you talk to seems to love it...

Now, how are you going to prove that you have an attractive business opportunity?
Clear thinking must take over from the creative brainstorming.

You will need facts supported by industry information.
You need market research.

To start your market research planning, briefly describe in your own words, your great idea for a business.

2.2 Market research

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Market research, in its broadest sense, refers to gathering and analysing information in order to make the decisions upon which you will plan your business.

Your research can involve a variety of techniques ranging from reading the community newspaper to determine the number and type of businesses operating in your local area, to more formal research methods such as questionnaires or surveys.

Before writing your business plan, it is necessary to have thoroughly researched factual information in order to identify a marketable product or service, select a suitable location, determine the size and characteristics of the target market and establish the best way to promote supplies.

Market research is an essential step in determining the viability of your proposed business venture, because it enables you to:

- find out whether there is actually a need for your proposed business and the likely demand for the product or service;
- ascertain who your customers are likely to be and gauge their preferences, so you can tailor the product or service to match those needs;
- discover what similar businesses are doing by looking at both general industry trends and your competitors;
- establish which products or services will be accepted in the market; and
- look for where new opportunities may lie.

Facts on individual businesses and your market can be obtained from many sources including:

- Australian Bureau of Statistics (ABS);
- Small Business Development Corporation (SBDC) in each State or Territory;
- trade and business associations;
- Austrade;
- existing businesses;
- local government (shire and city) departments;
- industry wholesalers;
- industry surveys;
- banks;
- Australian Securities Commission;
- business magazines (*Business Review Weekly*);
- newspapers (*Financial Review*);
- trade journals;
- companies' annual reports;
- credit agencies (Dun and Bradstreet);
- product brochures;
- newspaper searches;
- the Internet;
- retired business executives;
- editors of trade magazines;
- university professors; and
- government advisory bodies.

Well-researched factual information will allow you to draw strong conclusions. Details of your information sources are to be included as an appendix to your business plan.

Your *market research* provides you with the information required to develop all sections of the business plan, which are explained in these guidelines.

2.3 Your product or service

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When you commenced your *market research* planning, you prepared an overview of your business idea.

Now describe in detail, the *product or service* you plan to supply. In doing so, you are taking another step in the development and evaluation of your proposed business.

Do you have a number of *products or services* that you wish to supply (sell)?

If so, whilst you explore the potential of each product or service you should identify what you think will be your main *product or service*.

3. Industry analysis

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3.1 Your industry

Clarify in your mind and explain the type of business you wish to start. Is it a manufacturing, service, rural, retail, or wholesale business? Perhaps it is a combination of a number of these types.

For example, a business set up to manufacture and repair coloured leadlight panels could well describe itself as a manufacturing and servicing business, operating both as a wholesaler and a retailer. As a wholesaler, where it supplies (sells) its products to other businesses for them to supply (sell) to the public; and as a retailer, where it also supplies (sells) direct to the public.

Clarify your thinking further by asking yourself what will be the main source of business profits. Define your proposed business by the source of your profits.

For example, taking the leadlight business described above, if you are a manufacturer who derives the bulk of your profit from supplying (selling) manufactured items to other businesses rather than by supplying (selling) services directly to the public, you would define yourself as a manufacturer.

3.1.1 Identify the industry in which you will operate

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Initially you should address which industry group your proposed business fits within. Would your business fit into the transport industry, tourism or perhaps the aquaculture, viticulture or computer entertainment industry? If your industry is not obvious, think of those industries that are closely related to your proposed business.

You should consider:

- is the market for your product or service growing – are there more people buying or are existing customers buying more of the product or service?
- what other industries 'cross' into your industry?
- if any of those other industries expand will your business industry follow?
- what is happening in the economy at present that is relevant to your industry?
- what technological developments are occurring?
- what social trends are occurring?

Seek information from the Australian Bureau of Statistics or the State Government small business agencies. They may be able to provide you with figures on how the industry as a whole has been faring over the last few years – whether it has been growing or declining, how many and what type of firms are operating in this industry and from where these firms currently operate.

Other possible sources of information on your industry include industry associations which may have been formed to help businesses such as yours (e.g. Motor Trade Association if your business relates to the automotive industry). The State Reference Library may also be able to provide you with relevant figures and information.

Assess how the industry is performing overall throughout Australia, then assess your own State and, more specifically, have a look at the immediate area or region in which you intend to operate your business.

Make yourself aware of changes in the industry environment.

Discuss your business concept and industry with the Department of Commerce and Trade, Chamber of Commerce, specific industry associations and other closely affiliated or affected bodies and groups.

Check out industry magazines, the Internet, libraries and government agencies for information on your industry.

Talk to those who have been in the industry for a reasonable period of time. What problems and/or growth prospects do they foresee and how do these relate to your type of business. If you tell them you are undertaking research and that you are just starting out, then they may be willing to assist you. It is worth a phone call – what is the worst they can say to you?

By looking at your industry from an overall perspective you can determine three things:

- what *has* happened in the past;
- what *is* happening right at this point in time; and
- what is *likely* to happen in the future.

Bear in mind that many of the people who will be reading your business plan may know virtually nothing about the type of business you plan to start or the industry in which your business will operate. You need to convince them that the industry in which you intend to operate is capable of supporting your business, therefore enabling your business to operate profitably.

3.1.2 *Trends and seasonal factors*

Are local trends in your industry behind or equal to *trends* in other geographical locations and, if so, in what manner. Do not simply state that local *trends* are up and positive. Expand on your statement and explain why *trends* are headed in the direction you claim.

You are expected to demonstrate you have undertaken comprehensive and thorough research and can make comment with authority on the industry and its *trends*. The facts you gather will empower you to know whether the industry is profitable and attractive to you. Explain why you have this view and where you obtained the source data which convinced you of this view.

What *seasonal factors* are experienced in your industry? Outline both the busiest and quietest times of the year and explain why.

Remember, every industry has seasonal factors. Research those *seasonal factors* that impact on your industry.

Summarise what you have found out and back this up with all the relevant facts, figures and the opinions you have collected from industry experts.

3.2 Your customers

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3.2.1 The customer profile

Regardless of whether your proposed business will supply (sell) directly to customers or supply (sell) through other businesses, you must develop a precise understanding of who will be 'your customers'.

This understanding is called the *customer profile*. It includes all the demographic features of the groups of customers who will purchase your products or services.

The features in a *customer profile* include, but are not restricted to:

- sex;
- age;
- occupation;
- address or location;
- lifestyle characteristics;
- attitudes and values;
- recreational activities;
- income level;
- spending habits;
- debt levels;
- disposable income;
- education;
- expectations;
- membership of groups; and
- life stage.

In this part of your business plan think about and provide a detailed description of your intended *customer profile*. Your customers can be classified into market segments such as geographic location, gender, income, lifestyle, etc.

Will your potential customers be tourists, teenagers, single men or women, couples, retired people, etc.? Will they be mainly from your local area or will they be from a wider geographical area? What age are they? What occupations do they have?

Through the analysis of Census data, the Australian Bureau of Statistics (ABS) has developed a number of *customer profiles* for different industries. Access this information. However, as it is usually on a national scale, you would need to prove that the same information applies in your region. Generally speaking, the ABS is a good starting point.

Often the best way to find out the most valuable information about your potential customers is to go out and ask them!

There are many ways to collect new data. You could write a questionnaire, get a focus group together or you could observe customers. Depending upon your product or service you may also get customers to test a prototype and then ask them questions.

3.2.2 Customer buying motives

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Another aspect you should address in this section of your business plan is what you consider to be the main issues your customers take into consideration when making a decision to spend money on the type of product or service you will be offering.

You should explain what you consider would motivate customers to buy your type of product or service.

Are they purchasing out of necessity, convenience, reliability, price quality, value for money and reliability, or are expert advice, prompt, efficient and friendly service of equal or more importance to them.

Research these motives carefully. Discuss them with experienced business operators and determine clearly what drives your customers' buying decisions. Do not assume customers buy on price alone as the research does not bear out this assumption. They may be driven by emotion.

Consider carefully the business you are really in and the benefits associated with your product or service. This means:

- are you supplying (selling) a cleaning fluid or are you supplying (selling) 'time saving'; or
- are you supplying (selling) haircuts or are you supplying (selling) a change in 'self-image'?

It may not be the product or service, but the benefit behind the use of the product or service, that creates the sale. Your aim is to find out what customers want in your type of product or service and to find out what type of customers are in the market for the product or service you offer.

Remember, people buy solutions to their problems. Analyse their problems and ensure you offer a solution that translates into tangible benefits. Explain the benefits and clearly state why customers will want to buy from your proposed business.

3.2.3 Potential customers in the trading area

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Outline the geographical boundaries of your trading area. Attach a map as an appendix to your business plan if necessary. Be specific with your boundaries. statements such as 'the whole of Australia' are too vague.

Specify and research your target trading area.

- What is the size of the market for the product or service you are offering?
- How many people are likely to be customers of yours?
- How many customers are you likely to deal with each week or month?
- During each visit, how much money, on average, is each of your customers likely to spend on the products or services you provide?

When your business is established is there potential for growth in the market?

Research the facts and support your statements with reference to your information sources.

3.3 The competition

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As well as knowing your own business and its potential customers, you also need to research your business competitors carefully. Ensure that you are fully aware of any competition either from within or outside of your target market. Include part-time and casual operators.

Access the Yellow Pages, local newspapers and local service directories. Research your trade suppliers.

In researching your competitors, some of the issues you need to consider are:

- How long have the competitors been in business?
- Is this their only product or service?
- How does what you intend to offer compare with their 'total package'?
- What percentage of the market do they have – market share?
- How many supplies (sales) do they seem to make in a day/week/month?
- How many outlets do they have?
- What is their annual turnover?
- How well is your competition operating at present?
- Do they have a good reputation for service or paying their accounts?
- What are their strengths and what are their weaknesses?

Look at the strengths and weaknesses of your competitors. Their strengths will show you what you need to consider in your business and their weaknesses may provide you with an opportunity.

What is it, that they may not 'do or have' that your business could offer or provide?

Of your competitors, identify the businesses within your trading area which currently supply the products or services to the customers you hope to attract.

Research your competitors:

- What do you estimate their supplies (sales) figures to be?
- How much of their business can you realistically hope to win?
- Why will people change their previous buying habits to become customers of yours?
- How will your competitors react when you come into the market and entice some of their customers away from them?
- Will your business have any noticeable effect on other competing businesses?

Your competitors will be promoting their strengths and trying to hide their weaknesses. It is up to you to play detective and work out what it is they are hiding. Ask questions about both their strengths and weaknesses – you will want to have a rounded knowledge of where you can outperform them and where you can not do so.

Remember, a financier will read your business plan with particular focus upon why you claim your proposed business will attract customers. Before you submit your Shell *LiveWIRE* business plan in its final form, revisit this section of the guidelines and ask yourself the question:

Does the information provided, demonstrate in clear and compelling terms, that customers will buy from the business and therefore enable it to achieve sufficient supplies (sales) to make a profit?

This is the primary question any financier or investor will look to answer from your business plan.

3.4 The 'SWOT' analysis

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A *SWOT* analysis is a study of the Strengths, Weaknesses, Opportunities and Threats of any given situation.

In this case, the *SWOT* analysis will describe the current market situation as it relates to your business and explain the *strengths, weaknesses, opportunities* and *threats* that will affect your proposed business.

3.4.1 Your business in the marketplace

From the market research you have undertaken you will have some understanding of what is happening in the market and in your industry.

Given this understanding, apply the *SWOT* analysis process to your business and compare yourself to the business ventures of your competitors.

In looking at your business, what are your:

- *Strengths:*
 - How will your business differ from your competitors?
 - What is great or different about your product or service?
 - Why will your business idea succeed?
- *Weaknesses:*
 - What are the weakest elements of your business idea?
 - What elements could potentially hold you back?
 - How will you overcome these negative elements?
- *Opportunities:*
 - Positive environmental factors that will help your proposed business, such as changes in social values.
 - What trends are likely to affect market demand for your product or service?
 - What has been the performance of the market and what gaps are there in the market?
 - What influence could changes in legislation, taxation or changes in government have?

- *Threats:*
 - Are there any potential negative changes in the business environment, such as legal requirements, that would make it more difficult to supply (sell) your product or service?
 - What are the potential problems in the market?
 - How would you cope with negative changes if they became a reality?

This section of your business plan must link your research to your proposed business.

For example, if you found through your market research that the most popular colour for your product is blue, then you should explain this and how it will be incorporated into your marketing plan.

Outline the *strengths* and *weaknesses* of your proposed business, for these are the positive and negative elements over which you have control.

When you have identified those areas relating to your proposed business, you can act upon them and develop strategies to:

- address the identified *weaknesses* and *threats*; and
- find ways to capitalise on the *strengths* and *opportunities*.

3.5 Competitive advantage of the product or service

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What is special or unique about your product or service?

Competitive advantage is based upon what is defined as your *unique selling propositions*. *Unique selling propositions* are those unique features of a product or service which provide the benefits that satisfy the customer's buying motive.

Itemise the advantages, benefits or improvements which your product or service will provide that could cause a change of customer behaviour in your favour.

Link your *unique selling propositions* to the customer buying motives you have researched and discussed earlier. It is critical to your business success.

For example, will your prices be more competitive because you will be a local provider?

Is your main competitive advantage that:

- yours will be one of the few businesses in your area offering this product or service?
- the product or service you are offering is of better quality than your competitors? In what way is it better?
- the product or service you are offering is better value (lower cost) than the product or service that is offered by your competition?
- you are specialising in one particular product or service, whereas your competitors concentrate on a much broader range of products or services. 'They therefore cannot deal adequately with those customers who want specialised attention'?

- there is enough market demand to accommodate another business of this type in your area?
- you have some special flair or idea for this type of business which those who are currently operating in this market area lack? or
- you can offer a combination of the above advantages?

Explain why people will want to buy the product or service your proposed business will be offering and what will entice them to do business with you rather than with your competitors.

3.6 The marketing strategy

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The *marketing strategy* is your plan for how you will achieve your marketing goals.

Develop your marketing goals by:

- describing the target market (specifically the intended people who will buy);
- stating specific supply (sales) goals for this group (the number of supplies (sales) by category); and
- setting specific time periods for each goal (when goal is to be achieved).

It is not enough to say 'a lot' of supplies (sales). You need to work out in either percentage or actual dollar terms how much you expect to supply (sell) because of your marketing. It will be an informed estimate based on your market research.

Your goals should be quantified. However, they do not always have to be in immediate supply dollars. Your first objective may be to increase awareness of your product or service in the market.

As stated previously, the marketing strategy is your plan for how you will achieve your marketing goals. Describe your intended marketing strategy and why you have chosen it by addressing the following criteria.

(a) Product or service – outline the features you will emphasise in your marketing.

- How will your product or service be different?
- How will your product or service help customers?

Justify why you have chosen this strategy.

(b) Pricing policy – outline your pricing policy.

- Will you aim for the high end of the market?
- Will you be a budget alternative?
- Where will your product or service sit in relation to your competitors?

Justify why you have decided to take this stance – use your market research.

(c) Distribution – outline how you will deliver your product or service to your customers.

- Will you lease a shop? If so, in what area? Why in that area?
- Will you deliver through a website?
- Through a retailer?
- Through mail order?

Justify why you have chosen a particular distribution method – use your market research to explain this. If you are breaking away from traditional distribution techniques explain why.

(d) Promotion – outline which promotional methods you will use and why.

- Advertising – radio, TV, newspapers, magazines, billboards.
- Direct mail.
- Sales promotion – competitions, free coupons.
- Public relations – sponsorships.
- Publicity – media releases.
- Personal selling – direct contact with potential consumers.

Justify why you have selected a particular method/s. Use your market research to explain why this will be the best way to reach your target market.

3.6.1 *Marketing your product or service*

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Provide as much detail as possible about the main product or service upon which you will base your proposed business. Describe exactly what it is you plan to supply (sell) and explain why you think people will buy that product or service from you.

In marketing your product or service you need to ‘sell’ the benefits it offers to your customers and highlight its advantages.

If you intend penetrating the same market as your competitors, are you providing a different option to your customers that is more appealing to them.

Some business ventures supply (sell) more than one type of product or service.

The number and value of each type of product or service supplied is known as the ‘Supplies mix’.

Note: Prior to the introduction of the Goods and Services Tax (GST), supplies were known as sales.

However, under the GST system, the word ‘supplies’ replaces the word ‘sales’. ‘Supplies’ means the value of the transaction after the ‘uplift’ to include GST at the point of supply (sale). The GST is discussed in more detail in the section titled ‘Your business finance’.

If your proposed business will supply (sell) a range of different products or services you need to estimate:

- which products or services you will be offering;
- how many of each product or service you will supply (sell);
- how much it will cost you to produce or supply each product or service; and
- how much you will charge customers for each product or service.

From your market research you will have information that you can use to estimate monthly supplies figures. You will need to base your estimates on your research and clearly explain how you are drawing your conclusions. These figures are reflected on your **Sales volume and revenue forecasts (Appendix 3)** worksheet which is discussed in more detail in the section titled 'The financial plan'.

Be VERY careful when making predictions. Ensure that they are based on your research and that they take into account any variations that may occur during the year. These variations may include seasonal variations or promotional activities that you intend to undertake at particular times of the year.

Research and define the expected costs involved in achieving your marketing objectives. Include the cost of supplying goods and services to customers as well as advertising and promotional budgets.

Most suppliers will provide quotations on request, which will enable you to estimate your costs. However, always explain that you are undertaking research. Firstly, to be fair to them and secondly, to avoid getting phone calls for the next three months asking you if you are ready to buy yet!

Your **Sales volume and revenue forecasts** are based on all the market research you have undertaken and reflects your judgement.

Gather all your facts before attempting this worksheet.

To complete this worksheet you must research and resolve the following points:

- when you will start trade (month) and seasonal variations that are likely to affect forecasted volumes;
- the list of goods and services you will supply to paying customers. If there is not enough room on the sheet, prepare additional sheets and bring their sub totals forward on this sheet at the Total Supplies (C/F to P&L) row;
- the value of supplies you will charge before the GST uplift of 10%;
- your estimate of the volume of trade you anticipate for each item, taking into account the amount of time and/or productive capacity of the business and researched market demand for the item;
- your credit-granting policy before you start your business; and
- your opinion of the credit collections policies, to which your trade suppliers will expect you to adhere to, the GST component of supplies for GST collection and GST payments to the Australian Tax Office.

BUSINESS PLAN GUIDELINES

In the event you make GST-free supplies, those supplies should be shown separately.

Do not include the GST calculations on that sheet. You may wish to obtain advice on how to carry those figures forward from your Shell *LiveWIRE* mentor.

The completed calculations based upon your market research, assumptions and judgements are then carried forward to the cashflow forecast and profit and loss projections.

These estimates **MUST** be based upon research and factual sources, for these estimates represent the core of your potential financial returns.

If you have trouble forecasting on these worksheets you should return to your market research and undertake additional research.

Discuss your conclusions with an accountant or your Shell *LiveWIRE* mentor.

More information on **Sales volume and revenue forecasting** are included in the section titled 'The financial plan'.

3.6.2 Pricing considerations

Commenced		Completed	
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During your market research you will become aware of the prices of the products or services provided by your competitors.

Given your awareness of these prices, you will be mindful of the placement of your product or service in the marketplace.

Pricing considerations:

- Where will your product or service sit in relation to your competitors?
- Will you aim for the high end of the market?
- Will you be a budget alternative?
- Where will your product or service sit in relation to your competitors?

The price you charge your customers is critical. If the price is too high you make a good margin on your product or service, but customers do not want to buy from you. If the price is too low, everyone will buy from you but you will not make any money.

You need to confirm that the price you wish to charge your customers will meet your costs, provide an adequate margin and meet customers' expectations. If the supply price of your product or service cannot fully recover these elements, your business will experience hardship.

3.6.3 Development or design of products or services prior to marketing

If your product or service is not quite ready to market yet, describe the work required and estimate the time and cost involved in bringing it to the marketable stage.

3.6.4 Distribution

Commenced		Completed	
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Once you have manufactured your product or developed your service, you may need to transport your products or services to the places where they are to be supplied or delivered.

You have previously addressed the issue of the distribution of your products or services when developing your marketing strategy.

Now, outline in detail how you plan to transport or distribute your product or service and the costs involved.

3.6.5 Promotion

Commenced		Completed	
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Once you have identified where your potential market sits and who are your customers, you are in a better position to identify the best and most effective ways to advertise or promote yourself and your products or services to them. This will make your advertising accurate and effective.

Outline which promotional methods you will utilise and why.

- Supplies promotion – competitions, free coupons.
- Public relations – sponsorships.
- Publicity – media releases.
- Personal selling – direct contact with potential customers.
- Advertising – radio, TV, newspapers, magazines, billboards.
- Direct mail.

Justify why you have selected a particular method/s. Use your market research to illustrate why this will be the best way to reach your target market. Your customer profile is invaluable when determining how to package your product or present your service and where to advertise it.

Ensure that your advertising is appropriate to whichever group you are targeting and that it is presented in a manner which is familiar to them and appeals to their needs.

List the methods you intend to use to promote your product or service, e.g. newspaper advertising, flyers or some other medium. Next to each method, show as a percentage how much of your supplies (sales) you think you will achieve from each method.

3.6.6 Prime markets being targeted

Commenced		Completed	
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Effective targeting of your market is important, as it enables you to understand the different types of markets and how the range of customers satisfy their needs.

When determining your target market, consider these factors:

- the costs of supplying (selling) to the group;
- the anticipated supplies (sales) volumes;
- the size and number of competitors; and
- the resources required to supply (sell) into the market.

Prioritise your target markets. List the main markets that you intend to target, ranking them in order of preference. Prioritise those you think will give you the earliest return with the least amount of money needed to be spent to achieve supplies. Next to each market estimate as a percentage as to how much of your time and effort you will allocate in relation to your marketing monies.

You can consider your market as any group who can become aware of, and have a use for, the product or service you are offering. Within this large group there may be sub-groups who are easier for you to reach and who are more likely to buy from you. Firstly, try to identify the characteristics of the sub-group that will form the bulk of your customers, and gradually widen your view until you are sure that you have described each group or type of person who may become a customer of yours. It is then just a matter of listing the groups of people you have identified in order, from those you consider will be your biggest customers, through to those who will make the least significant contribution to the success of your business.

You are now in position to judge how much effort you should make to get your message through to each group and how much time and money you plan to spend on advertising your product or service to each group. Perhaps you will decide to put most of your effort into winning a core of regular customers. You may decide, however, that in order to maximise supplies you need to attract customers from further afield.

3.6.7 Market segmentation

Commenced		Completed	
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The most fundamental principle in marketing is knowing who your customers are and what they need. Yet many small business operators do not understand this.

For most products and services there is not just 'one' market, but groups of sub-markets. These sub-markets are groups of people who have some common characteristics or needs, but who differ in character and need from other groups.

These sub-groups are called *market segments* and there are three basic parts to market segmentation:

- *Human need*: this is usually defined as an individual need. For example, shoes – when someone buys a pair of shoes it is a very personal choice.
- *Product type*: here you are looking at groups of people coming from far-ranging and different areas, but all requiring the same or similar products or services. For example, a set of scuba diving tanks – recreational divers, professional fishermen, marine photographers or perhaps members of the army or police forces could use this product.
- *Industry type*: the product or service may have industry-related connections such as spanners, trucks or perhaps generators.

Once you have decided into which category your business fits, you then need to look closely at the customers who inhabit that particular category.

Again there are three general customer categories:

- *Geographical*: this will identify where you might find your customers (e.g. city, regional or rural and whether they are north in the tropics or south in the cooler climate).
- *Demographic*: demographics are the very specific characteristics of your customers (e.g. age, income bracket, marital status, occupation, education level, cultural and religious background).

- *Psychographic*: here you look at your customers' lifestyles, behaviour patterns, values and possible beliefs. (e.g. whether they perceive themselves as middle class, upper class, working class, etc. and if their lifestyle is active, conservative, health or environmentally orientated).

List the personal characteristics of the customers within whichever product category listed above you expect to find your customer and describe the market segments in which you will focus your efforts.

3.7 Possible alternative products or services

Commenced		Completed	
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If you can think of ways in which you may be able to strengthen your business by adding to the range of products or services you offer, then you should discuss these possibilities here.

For example, a person could plan to set up a shop primarily to sell pre-owned surfboards. This business could later be expanded to sell other products which would appeal to those customers who buy surfboards.

List the ways in which you can strengthen your business. Be sure to include any possible income that you may derive from utilising previous skills or qualifications for work that can be obtained through a subcontract arrangement

3.8 Market share

Commenced		Completed	
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Thinking about all the information you have gathered should enable you to make a soundly-based estimate of what percentage of the people in your trading area, buying this type of product or service, will buy it from you.

This is called your *market share*. Within this heading, describe what you think your *market share* will be after one month, after six months and after one year. You can describe this share of the market as a percentage of the total market.

Later, when your business is operating, you will be able to use these estimates to see whether your business is performing as well as you expected.

You should also think about other products and services which may be regarded as competitors to your business. Consider:

- are you likely to win customers away from other types of related products and services; and
- is there a danger that growth in one of these related products will seriously hamper your attempts to build a viable business.

Using your research information you can prepare an estimate of the supplies (sales) you will achieve in your first year of operation. You should make your most accurate estimate of how many supplies (sales) you will achieve each month from the time your business starts until the end of your first full year of operation. Then add up these estimated monthly supplies (sales) to give you an annual estimate of supplies. This information can be most clearly set out in the form of a table similar to the one shown overleaf.

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MONTH	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
UNITS	180	165	170	125	135	150	180	185	190	95	115	130
SUPPLIES \$	3600	3300	3400	2500	2700	3000	3600	3700	3800	1900	2300	2600

Estimated annual totals: Units: 1,820 (@ \$20 each) Supplies: \$36,400

These estimates will be carried forward into the financial worksheets in the section titled 'Your business finance'.

You should prepare an estimate of the volume of supplies (sales) you anticipate for each product or service for each month for the first year of trade.

These estimates represent the most critical judgements you will make in business planning.

Pause, reflect, consult, research and, above all, take your time. The time you spend shaping and crafting these figures, based upon factual research, is the most valuable time you will spend in developing your business plan.

3.8.1 Growth potential

How much do you predict that the market for your products or services will grow through new customers, changes in trends or change in your market share. Can you see the possibility of expanding your business to include other related products or services.

Possible sources of information are once again local councils, trade suppliers, industry associations or other groups with vested interests in the field in which you intend to operate. Be sure to name your information sources to validate your claims.

4. Sustainable development

4.1 What is sustainable development?

Sustainable development (SD) is simply development that meets the needs and aspirations of the present generation – that's you – and does not compromise the ability to meet their own aspirations of future generations – that's your children and grandchildren. It requires us all to try and strike a balance between economic development, environmental protection and social objectives. At Shell and Livewire, we think of it as people, planet and profits.

4.2 Conducting a basic sustainable development audit

In the early stages in particular, it is not necessary to get consultants involved – you can conduct a basic SD audit yourself. The aim is to highlight areas of actual or potential concern so that you can then carry out some research to help you to address those issues.

As you develop your business ideas and begin to plan ask yourself the following questions:

- How will my business affect the local community? Is there a need for me to consult with any local people before I start?
- Will the product or service I provide affect the environment? What waste will it produce? What will I do with that waste? Is any of it recyclable? Can I use renewable sources of energy/materials? Include in this the entire process you are involved in from choice of suppliers through to customer disposal of your product.
- What are the most environmentally friendly materials and can you avoid those that are known to damage the environment? For example these include heavy metals such as mercury, lead or zinc. Such materials affect the ozone layer, create toxic residues, etc.
- Look at energy efficiency in your workplace. What does energy cost you? Waste in this area has a direct effect on your profitability. Include use of power, heat, light and efficiency of electrical and other power driven equipment.
- Set yourself a list of business principles for your company. Insist on honesty, integrity and fairness in all aspects of your business.
- Respect the rights of yourself and your potential employees or co-workers. Provide them with good and safe working conditions and endeavour to develop and make the best use of their talent. Encourage employees to be involved in the planning and direction of your company. Your commercial success will depend on the commitment and talent of your staff.
- Seek mutually beneficial relationships with contractors, suppliers and customers, and promote your business principles in so doing.

By taking this approach, you can show that SD is something that you practise, as well as preach. SD should be part of the culture of your company – culture being ‘the way we do things around here’.

4.3 What next?

The information here is only intended to suggest to you that there are real benefits in considering these issues right at the outset of your business. Only you can decide how you can take these issues forward in relation to your business. We strongly recommend that if you are to be successful and respected in business you will want to take these matters seriously.

5. Building your business

Most small businesses are built in four phases:

- *Phase 1: Idea generation, research and planning.* This is the phase during which you create your vision, research the market and prepare your business plan. Although this phase can take a lot of time (usually at least a few months), costs are usually minimal and usually funded by the prospective business owner(s).
- *Phase 2: Establishing the business.* This phase includes all the activities you need to do before you can really get your business under way. It starts when you make a commitment to establish the business and extends until the time you're ready to 'open your door for business'. During this phase you may start to spend some serious money – e.g. on registering your business, buying equipment and supplies and finding premises (if you can't run the business from home).
- *Phase 3: Early-stage trading.* This phase runs from the time you're ready to make your first sale to the time that the business is on a secure footing in terms of customers, earnings, etc. During this phase, sales revenues are often slim (often less than your operating costs, at least for a while). The shortfall between revenues and costs during the phase will need to be funded – by you (from your savings) or from other sources.
- *Phase 4: Later-stage trading and growth.* Finally, your business is growing, and revenues exceed your costs. This is the phase when your business starts to accrue money (and can pay off debts incurred during the first three phases).



The term of your business plan should take you to at least the end of Phase 3, and preferably into Phase 4, so that you, and other stakeholders (including providers of funds), will know how and when your business becomes self sustainable.

5.1 Establishing the business (Phases 1 and 2)

Phases 1 and 2 include all of the work and expenditure needed to get ready for business. These phases include all activities up to the point where the business will earn its first dollar of sales.

The objective of Phase 1 is to develop your business concept into a workable business plan. Typical tasks include:

- development of your business idea into a marketable concept;
- conducting initial research, including the activities described in Chapter 3;
- finding your business premises and developing a fit out plan;
- preparing your business plan;
- identifying sources of funds, business clients and suppliers.

Your business preparation will progress to a point at which you cannot proceed without substantial financial or contractual commitment. That point marks the commencement of Phase 2.

Phase 2 focuses on the establishment of the business – e.g. on incorporating a company, printing stationery, setting up premises, etc. This is the time during which you begin to incur significant costs. You should not commence Phase 2 without:

- a detailed timeline that sets out all Phase 2 tasks and major financial outlays;
- a plan for obtaining sufficient funds to reach Phase 4 – hence the need for the financial plan.

Typical activities during Phase 2 are shown in Table 1.

Table 1: typical activities during the establishment phase

- Establishing a business (identity) to own and operate the business. This may involve registration with federal and state agencies such as the Tax Office, ASIC, Workcover, etc.
- Obtaining funds, in the form of:
 - equity (your own investment and money from other owners or investors in the business);
 - loans and overdraft credit facilities (debt finance, from yourself and from other individuals, and from other sources such as banks);
 - business credit (deferred payment from suppliers);
 - leasing (from finance companies or banks, often introduced by suppliers);
 - grants;
 - guarantees (not exactly funds, but a commitment of resources to support the business).
- Acquiring licences or franchises.
- Acquiring and setting up or fitting out business premises.
- Acquiring initial inventories.
- Acquiring equipment.
- Developing products or capabilities.
- Developing promotional materials and undertaking advertising.
- Arranging payment facilities (credit card or other electronic payment merchant facilities).
- Arranging business insurance.
- Developing a website (including registering a domain name).
- Arranging and establishing other services and facilities (e.g. telephone, internet access, directory listing, industry association listing).

5.1.1 *Threats and risks during the establishment phase*

The key risks in Phase 2 are caused by inadequate preparation for Phase 2, including:

- insufficient development of the product or service concept;
- inadequately researched competition (products and suppliers), prices, business regulation, business location;
- insufficient funds and 'staying power'.

The consequences of these risks being realised can include:

- taking too long to get into Phase 3, which will mean that it takes you longer to begin earning revenue while you are paying for the cost of premises, licences, insurance, debt finance (loans and overdrafts);
- failing to get into Phase 3, which could mean that you go out of business before you commenced, and that you are left with residual rent, licence and debt commitments.

The best way to avoid these risks is to do an excellent job of business and financial research and planning in Phase 1.

5.2 **Early stage trading (Phase 3)**

In some cases your first business day will be a sell out, with queues of customers wanting to buy your product or service. This is sometimes the case with franchises. For many other businesses it will take time to reach a point at which sales exceed expenses. During this period your requirement for funds will increase.

In addition to funding the gap between your cash inflows and outflows, you may need to provide business credit to customers. Further, you may have to provide for losses of revenue through bad debts (customers who do not pay at all), theft and spoilage (goods you have purchased that are not available for sale), and discounting and provision of free samples of goods or services.

Typical sources of finance in Phase 3 include:

- equity investment (usually from yourself and/or from family members and friends, possibly from business angels, and potentially even from venture capitalists if your business meets their very strict investment criteria);
- loans and overdraft credit facilities (debt finance from yourself and from other individuals or from other sources such as banks); and
- business credit (deferred payment from suppliers).

5.2.1 *Threats and risks during Phase 3*

Few people develop a plan that will intentionally lead them into trouble – yet many new businesses do find themselves in trouble in Phase 3 and either spend too long in this phase or never survive it. The most significant risks in Phase 3 are:

- lower than planning sales performance;

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- the discovery of costs that were underestimated or not included in the plan;
- a lack of adequate funds; and
- following a course different to what was outlined in the business plan.

In the last few years many new technology ventures (dot coms) and other business ventures from new airlines to small businesses failed during Phase 3. These businesses were never able to achieve a level of reliable profit.

The huge amounts of cash invested in these firms were often lost through unsustainable 'cash burn rates'. These unsustainable burn rates were attributable in many cases to a combination of:

- a non-viable set of assumptions about the attractiveness of the business (value) proposition;
- under-estimation of the defensive reactions of competitors;
- a failure to acknowledge and address the various problems; and
- gambles on quick fix 'marketing' tactics, including heavy price discounting combined with high advertising expenditure.

The best ways to address these sorts of risks include:

- monitoring the performance of your business against your plan – which should tell you if you have a problem developing;
- re-planning using new assumptions – which will tell you where your business is headed unless you do something;
- revising your business plan, taking into account any revisions to assumptions or tactics – which will tell you where your business is headed if you follow your revised plan.

The key to survival and success is to develop a good plan, maintain that plan and use the plan.

5.3 Later stage trading and growth (Phase 4)

If you reach Phase 4 you will have reached the point where business sales reliably exceed break-even volume or utilisation, and your business is reliably profitable. You are now able to consider positive future options for growth, safe consolidation or even sale or franchising of your business.

During Phase 4 you will often need to maintain your Phase 3 sources of finance, but you will usually be in a position to take a more strategic view of the structure of those finances, especially if the level of outstanding debt is declining. With your business relatively safe, your commercial risk is lower, and you can afford to shop around for good financing deals.

You may even find that you have surplus cash, and are in a position to invest that surplus. At this point it is important to be fully aware of the timing and magnitude of future commitments, such as:

- income and other tax instalments;
- renewal of loans;
- renewal of leases for business premises and/or relocation;
- payout or renewal of equipment leases;

- replacement of equipment;
- extension or redevelopment of business facilities.

5.3.1 Threats and risks during Phase 4

Whilst some risks are reduced as a business moves from Phase 3 to Phase 4, the range of operational and other risks increases. Issues that are relevant to business planning include:

- inadequately funded (under-capitalised) growth;
- inefficiency – inventory levels, production costs, administrative overheads;
- competition – if you're successful, other people may decide to develop a 'me too' business that will put pressure on your prices and sales volume;
- unexpected cost increases – some small businesses can find their landlord wanting a larger return from a profitable business tenant, and can demand a rent increase. Some shopping centre managers may even force you to move from your current location to a larger location, increasing your rental space and your cost per square metre as well as forcing you to fit out new premises and make good the old premises.

Your business plan should become a 'living document' in which key price, volume and cost assumptions are updated and the consequences and required strategies to address those consequences developed and evaluated.

6. The financial plan

Why prepare a financial plan? For at least two very good reasons:

- First, a financial plan will allow you to work out what your funding needs are – particularly while you are establishing your business and during the first few years of operation.
- Second, a financial plan will show you when you can expect the business to start earning revenues in excess of its costs.

Companies fail if they run out of money. Almost all of the numerous 'dot-bombs' and other tech stock failures we saw during the last few years had one thing in common: their 'burn rate' (i.e. their expenses) continually ran ahead of their revenues until there was nothing left in their bank accounts. If you prepare a rigorous financial plan you can substantially reduce the risk of that happening to your business

The purpose of this chapter is to help you:

- to work out how much money you will need to cover establishment costs;
- to estimate your likely costs during the initial stage after establishment (e.g. during the two years);
- to evaluate the adequacy of the price(s) you wish to charge in relation to costs;
- to estimate how much revenue you are likely to earn during the first few years of trading (which depends upon the prices you charge and the number of sales you can win);
- to work out the likely timing of cash inflows and outflows from your business operations (which affects the amount you will need to borrow or invest to fund any mismatch in timing);
- to prepare a Cash Flow Statement;
- to calculate how much money the business will need to find (from your own savings, or from friends, family, government grants, bank loans, etc) to fund any operating cashflow deficits that exist in the early stages of your business;
- to understand the different sources of finance (your own savings, bank loans, venture capital, etc) and the pro and cons of each;
- to analyse the likely performance of your business in order to understand the sources of value and how you can improve the medium-term value of the business to you, the main business owner.

6.1 Cash flow planning

Cash is the lifeblood of a business. Cash is needed to:

- establish the business;
- sustain the business; and
- provide returns to investors and other stakeholders in the business.

Cash flow is the flow of money into and out of the business. The two critical issues in management of cash flow are:

- solvency – to have enough money to meet the needs of the business' operations, and
- business value – to accumulate enough money (or realisable net assets) to meet the needs and expectations of investors and other stakeholders.

Cash flow and profitability analysis are critical elements of the Livewire business plan, with emphasis on:

- relationship between selling price and total unit cost;
- break-even analysis;
- overall profitability analysis;
- cashflow estimates and funding for best, worst and most likely business scenarios in each year; and
- justification/basis of estimates.

This chapter discusses cashflow planning, and the process of building a cashflow and profit plan. To illustrate key points in this discussion, the chapter uses an example that is relevant to some businesses involved in providing services, in retail sales or in manufacturing. *The example is illustrative only; it is not intended to be a template for your cash flow and profit plan, nor is it intended to suggest a level of detail that you should use.*

6.1.1 Cash flow plan

A cash flow plan is a spreadsheet that shows expected movements of cash into and out of the business for the next few years (usually 2–3 years). The plan is divided into calendar months (some businesses may use 13 periods of 4 weeks).

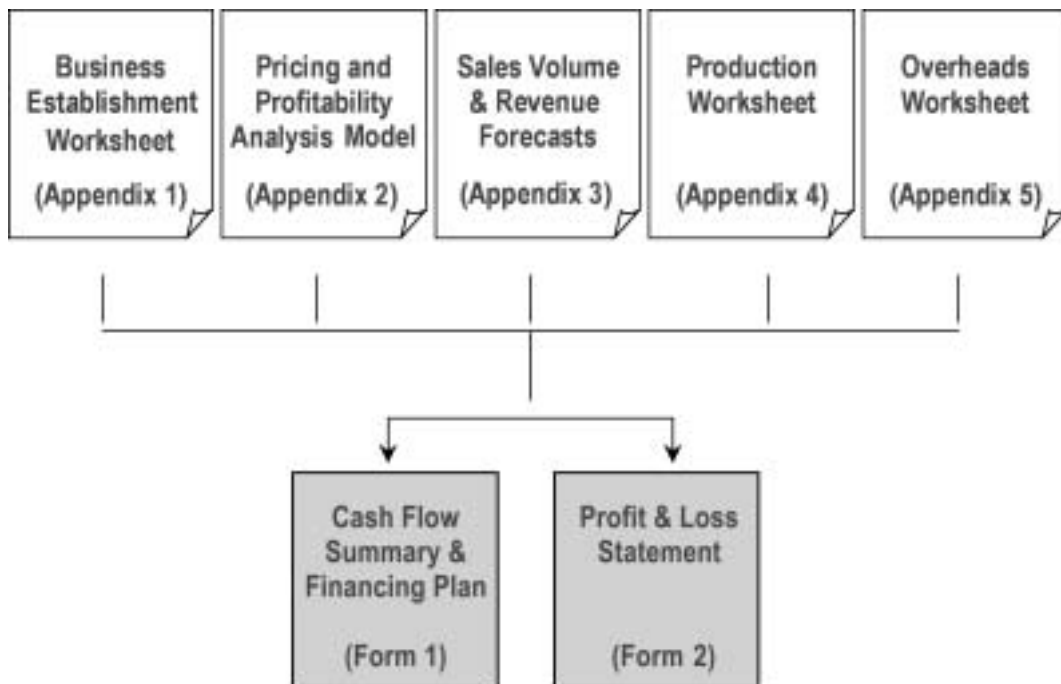
Cash flows are set out for each month in terms of:

- Cash inflows (receipts), which include:
 - money received by the business from its operations;
 - money received from incidental operations, such as the sale of assets, cashing in investments, receipt of dividends and interest on investments;
 - money invested in the business as equity; and
 - money lent to the business (debt financing).

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- Cash outflows (payments), which include:
 - money paid by the business to establish and continue operations;
 - payments for incidental operations, such as purchase of assets, investment of surplus funds or payment of interest on loans;
 - dividends or drawings paid to stakeholders, and repayments of equity investments; and
 - repayment of money lent to the business (reduction of debt).

The cash flow plan is supported by the following documents that explain the basis and calculation of estimates. The example used throughout this chapter includes the following supporting documents.



The critical financial planning documents for the Livewire competition are:

- the cash flow summary and financing plan, which summarises cashflows, calculates overall deficits (or surpluses) and determines how those deficits will be financed (or the surpluses invested); and
- the profit and loss statement, which determines accounting profit.

Examples of these documents are provided at **Forms 1 and 2** at the back of this document. A 10-step summary of the process of financial planning is provided at Appendix 7.

Financial planning documents should show expected results for the duration of the business plan (usually 3–5 years) for various scenarios (e.g. best, most likely and worst cases).

6.2 Business Establishment Worksheet

The Business Establishment Worksheet (Appendix 1) sets out:

- the costs of establishing the business; and
- other capital acquisitions.

This worksheet is very important because it sets out your most significant financial commitments, and is the basis for your first 'round' of financing.

Business establishment outlays are based on the plan you have developed for Phases 1 and 2 (see Chapter 4).

Typical business establishment outlays may include the items in Table 2.

Table 2: typical outlays included in the Business Establishment Worksheet

- Commissioning market research or buying research materials.
- Buying the services of advisers and consultants in areas such as business planning, business structures (especially if trusts or tax planning is involved, business financing, leasing an taxation, contracting, intellectual property (trademarks and patents), insurance and franchises).
- Establishing a business (id)entity such as registration of a business name, registration of a company and/or trust.
- Acquiring licences and franchises (initial costs only).
- Acquiring and setting up or fitting out business premises (including initial deposits – advance payments of rent should be recorded in the Overheads Worksheet).
- Acquiring initial inventories and stores, including initial supplies of printed stationery.
- Acquiring of equipment, tools and vehicles (including initial payments or deposits on leases).
- Developing products or capabilities.
- Developing promotional materials and undertaking initial advertising.
- Establishing loans, overdraft facilities and guarantees.
- Arranging and establishing other services and facilities (e.g. telephone, internet service, website, directory listing, industry association listing).

Many of these payments may be in the nature of capital outlays, and are treated separately from other costs for the purposes of tax and financial reporting.

6.2.1 Example of a Business Establishment Worksheet

Appendix 1 shows an example of a Business Establishment Worksheet. The key elements of this worksheet are:

- a schedule of business establishment and capital outlays (including GST paid);
- a worksheet that determines the amount of GST included in the outlays;
- a payment schedule in which some payments are deferred according to terms of business (trade) credit.

6.3 Pricing and costing worksheets

In planning a new business it's essential to set out cash flows associated with the normal operations of the business – the provision and sale of goods and/or services. Three inter-related models are critical:

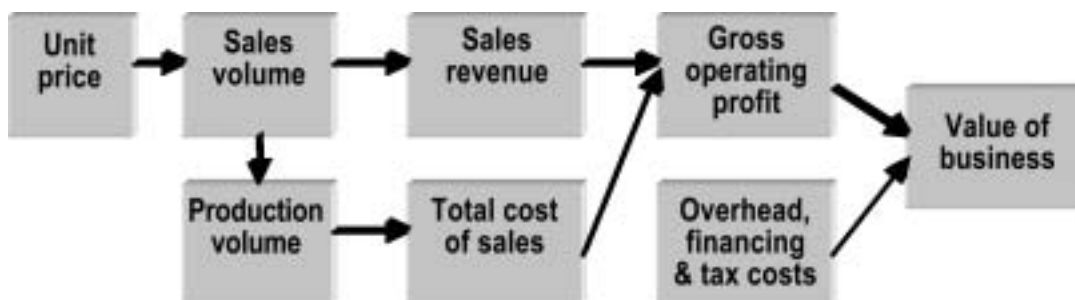
- a Pricing & Profitability Analysis Model (Appendix 2),
- Sales Volume and Revenue Forecasts (Appendix 3),
- a Production Worksheet (Appendix 4).

In thinking about your business, one of the most important questions you can ask is: what 'drives' the value in my business?

In most retail and manufacturing businesses:

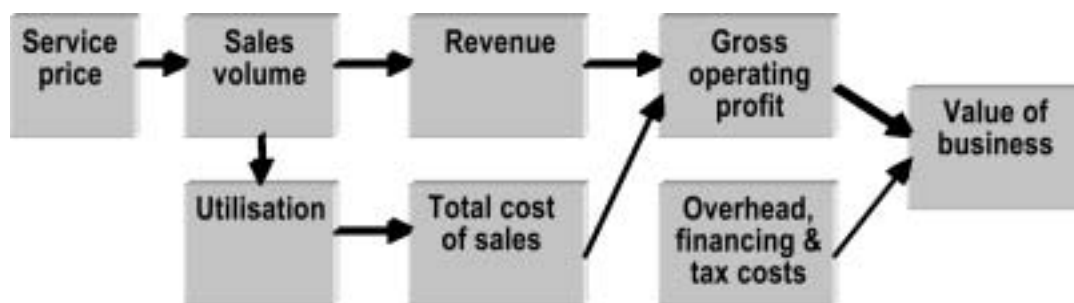
- unit price is a driver of demand for a product or service, and is therefore a driver of sales volume;
- sales volume is a driver of sales revenue and production volume;
- production volume is a driver of total cost of sales, and of unit cost of a product;
- the difference between sales revenue and cost of sales is referred to as gross operating profit, and
- the relationship between gross operating profit and the sum of administrative, overhead, financing and taxation costs is a driver of the value of the business.

The following diagram illustrates this set of relationships.



In service businesses (e.g. a coffee shop, hairdresser, trade service):

- service price is a driver of demand for a service, and is therefore a driver of sales volume;
- sales volume is a driver of sales revenue and utilisation;
- utilisation is a driver of total cost of sales, and of unit cost of a service; and
- the difference between sales revenue and cost of sales is referred to as gross operating profit, and
- the relationship between gross operating profit and the sum of administrative, overhead, financing and taxation costs is a driver of the value of the business.



Where do we start? The market research you have conducted (Chapter 3) has provided you with an appreciation of:

- the price and demand for a product or service;
- a business volume curve; and
- likely promotion costs to achieve your business volume forecast.

On the assumption that you have achieved a reasonable level of confidence in these estimates for planning purposes, we suggest the following process:

- Set out your initial estimates of price and costs in the Pricing & Profitability Analysis Model (Appendix 2).
- Set out your estimates of sales volume and credit terms in the Sales Volume and Revenue Forecasts (Appendix 3).
- Estimate production volume for each product in the Production Worksheet (Appendix 4).
- Estimate management, administrative and other overhead outlays in the Overheads Worksheet (Appendix 5).
- Review the Pricing & Profitability Analysis Model (Appendix 2) to determine the break-even point for your initial level of production or service capacity.
- Conduct several iterations of this process to fine tune your estimates and plans.

6.3.1 Scenario analysis

In the process of working your way around this loop, consider the sensitivity of your business to changes in assumptions. Suppose demand is not what you think it is? Suppose your competitors decide to become more competitive and discount their prices, or increase their advertising? Suppose interest rates change?

You should develop feasible scenarios (sets of business assumptions) to help you:

- understand the dynamics and performance of your business;
- understand your vulnerability to changes in the business environment;
- know when your business is at risk.

It would be almost impossible to specify and evaluate every set of assumptions that could affect your business. A manageable set of feasible scenarios includes:

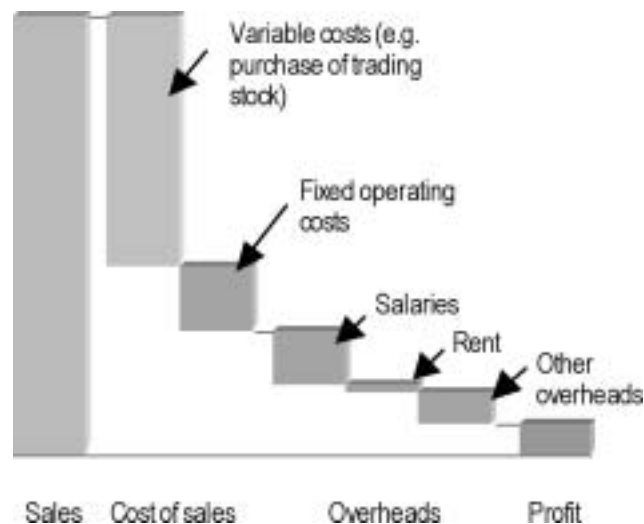
- a best case scenario: the best realistic set of business circumstances;
- a most likely scenario; and
- a worst case scenario: the most pessimistic set of business circumstances.

Develop a set of plans for each scenario and include those scenario plans in your business plan. This will help you and other stakeholders in your business understand the level of upside potential and downside risk in your business.

6.4 Pricing and Profitability Analysis Model

Pricing and profitability analysis of a hypothetical small retail business

Suppose your business is a typical, profitable small retail business, like the example shown below.



Key points to note about this hypothetical business are as follows:

- variable costs (purchases) are 68% of unit price, and the business has 32% of every dollar of sales to cover costs and profit;
- fixed costs are 25% of unit price ...
- producing a profit of 7%.

Profit in this example is greatly affected by changes to price, volume and fixed expenses. In the above structure, if sales are \$200,000 and business volume increases by 10%, then:

- sales will increase by 10% from \$200,000 to \$220,000;
- variable costs (purchases of trading stock) will increase by 10% from \$136,000 to \$149,600;
- fixed costs will remain the same at \$50,000;
- profit will increase by 46% from \$14,000 to \$20,400.

On the other hand, profit can be wiped out by:

- a 22% reduction in the volume of products sold; or
- a 7% reduction in price (assuming no change to sales volume); or
- a 28% increase in fixed expenses; or
- a combination of a 10% discount on sales that produces an increase in sales volume of 12%.

Suppose you wish to increase your prices by 5% expecting that there will be a reduction in sales volume. How big a reduction in sales volume can you withstand before your profit falls below its current level of \$14,000? The answer in this case is 13%.

6.4.1 *Break-even analysis*

A person who understands the dynamics of their business is able to respond appropriately to:

- changes in customer demand;
- changes in the behaviour of competitors;
- requests for price discounts;
- changes in cost of sales;
- proposals to increase advertising or move to more expensive premises.

The key is understanding your 'break-even' sales volume. As we've seen in the examples above, the profitability of a business that has a mix of fixed and variable costs is driven by sales volume. The formula for determining break-even sales volume is simply:

$$\begin{aligned} \text{Break-even Volume} &= \text{Fixed Costs} / \text{Gross Profit per Unit} \\ &= \text{Fixed Costs} / (\text{Price} - \text{Variable Cost Per Unit}) \end{aligned}$$

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Here's a worked example using the numbers above:

Fixed Costs = \$50,000

Price = \$200/unit

Variable Cost = \$136/unit

Break-even Volume = $\$50,000 / (\$200 - \$136) = 781$ units.

At break-even volume:

Sales = \$156,250 (i.e. $781 \times \$200$)

Variable costs = \$106,250 (i.e. $781 \times \$136$)

Fixed costs = \$50,000

Profit = 0 if Sales = Costs (i.e. $\$156,250 = \$106,250 + \$50,000$).

6.4.2 Break-even analysis in a services business

For a business that sells labour-based services the equivalent to break-even volume is 'break-even utilisation'. Utilisation is the percentage of total available hours that are revenue earning (billable). Break-even utilisation is the utilisation level that equates total revenue to total costs, i.e.:

Break-even Billable Hours = $(\text{Salaries} + \text{Other Fixed Costs}) / \text{Rate per Billable Hour}$

= $(\text{Total Cost}/\text{Avail Hr} \times \text{Avail Hrs} + \text{Fixed Costs}) / \text{Rate per Billable Hour}$

Break-even Utilisation = $\text{Break-even Billable Hours} / \text{Total Available Hours}$

Here's a worked example for a services business. Suppose that the business has three advisers and the total salary cost is \$45,333 per person. They work 36 hours per week for 44 weeks per year. They charge clients \$60/hour for their advice. What percentage of their time do they have to be earning revenue in order for the business to break even? The answer is 65%. Here's how this is worked out:

Number of staff = 3

Available time per staff member = $36 \text{ hrs/week} \times 44 \text{ weeks/yr} = 1,584$ hours

Total available time = $3 \times 1,584 = 4,752$ hours

Total cost of staff = \$136,000/yr

Total fixed costs = \$50,000/yr

Price charged per hour of service = \$60.

Break-even Billable Hours

= $(\$136,000 + \$50,000) / \$60$

= 3,100 hours

Break-even Utilisation = $3,100 / 4,752 = 65\%$.

Sales = \$186,000 (i.e. $3,100\text{hrs} \times \$60/\text{hr}$)

Total cost of staff = \$136,000

Fixed costs = \$50,000

Profit = 0 if Sales = Costs (i.e. $\$186,000 = \$136,000 + \$50,000$).

Example of a pricing and profitability analysis

The Pricing and Profitability Analysis Model (Appendix 2) comprises the following elements:

- Unit Price and Input Costs Table;
- Break-even Volume Estimate; and
- Profit Calculator – a rough estimator of profit levels for various sales volumes.

Prices and input costs entered in this model are used by the Sales Volume and Revenue Forecasts (Appendix 3) and Production Worksheet (Appendix 4). These prices and costs should be inclusive of GST.

The overhead contribution estimate should include:

- an estimate (budget target) for management, administrative and other overheads (including interest and taxes) – from Appendix 5; and
- an estimate (budget target) for depreciation and amortisation of capital and some other payments in the Business Establishment Worksheet (Appendix 1).

The profit estimate is your budget target for returns. It may be estimated as a percentage of the selling price, or on any other basis.

This model will develop an estimate of break-even volume: the sales volume that will produce sales revenue that equals fixed and variable costs. It is a rough estimator used for broad feasibility and profitability analysis.

6.5 Sales volume and revenue forecasts

Sales revenue is the value of business you conduct. In most businesses:

- you enter into a contract to sell something or deliver a service for a price;
- you deliver the product or service and thereby earn the right to be paid; and
- you receive the amount agreed in the contract.

In a retail store all of this can happen in what appears to be a single transaction. You offer to sell a product for an advertised price, your customer agrees to pay the price, you release the product to the customer and the customer pays you in cash or (less often) by cheque.

6.5.1 Setting out your sales forecasts

For each product or service set out your forecasts of:

- sales volume;
- unit price (including GST and any other taxes, but net of any discount); and
- sales revenue (sales volume multiplied by unit price).

Add up your product or service sales revenue forecasts to produce a total sales revenue forecast. This line of figures (for each month) represents your earned revenue.

6.5.2 *Business cycles and seasonality: good and bad times*

Most businesses are affected by:

- long-term business cycles – differences in the business environment over several years; and
- seasonality – differences in business activity during the year.

Your exposure to business cycles and seasonal factors will depend on the nature of your business and your markets. To take a few examples:

- Good and bad times for people in the building industry can depend on (a) economic cycles that affect account inventory levels (the stock of property), interest rates, performance of alternative investment opportunities (e.g. the stock market), and (b) the time of the year.
- People involved in general retailing benefit from high volumes of consumer spending in November-January and at Easter.
- Some outdoor activities do better business in summer (e.g. general tourism) while others do better in winter (e.g. skiing).

Work these factors into your sales volume expectations – and even into your thinking about:

- when is the best time to begin business;
- different ways of selling your product at different times of the year (for example, some ski resorts attract a great deal of business in the summer time as hiking and leisure venues, whilst some other summer-oriented areas, such as the Blue Mountains, attract 'Yule-fest' business in mid winter);
- changing the mix and orientation of your products and services during the year.

6.5.3 *Electronic payment and trade credit*

Many businesses offer alternatives to payment by cash, including:

- Credit cards (e.g. Visa, MasterCard). In a credit card sale a customer buys your product or service by a line of credit extended by a credit provider. The credit provider pays you immediately the full value of the sale and recovers the money from your customer. For this service the credit provider charges a fee (between 2% and 8% of the sale) based on the amount of credit extended – which amounts to a percentage of the sale. There is also a standing charge for facilities.
- Charge cards (e.g. American Express, Diners Club). These work in much the same way as a credit card.
- Debit cards (offered by many banks). In a debit card sale a customer buys your product and pays for it by an immediate transfer of funds from the customer's bank account to your bank account. The provider of this service charges your business a fixed transaction fee of around 70 cents, which is cheaper than the credit card fee because no 'borrowing on credit' is involved.

- Invoice payment, in which you immediately or some time later give the customer an invoice (a bill) for the product or service and expect the customer to pay the invoice within a time period specified on the invoice. This involves deferring receipt of the proceeds of your sale, which means that your business has to find that money from another source until it receives payment. Depending on the payment facilities you have provided, payment of the invoice may be by:
 - cash or cheque;
 - credit card, charge card or debit card;
 - Bpay, in which the customer transfers funds directly from their account to your account through a service provider.
- Direct debit, in which the customer authorises their bank or credit card or charge card provider to pay an invoice you send to that bank or provider.
- Scheduled fees (e.g. rent, subscriptions, fixed fees), in which a customer is expected to pay for services or products on a scheduled date. A debt is created in a service contract without the need for an invoice. Payment is by any of the above methods.

Allowing customers time to pay is basically lending customers money, and these customers become trade debtors to your business. The risks involved in trade credit include:

- customers exceeding the terms of credit (paying after the due date);
- customers disputing the invoice;
- customers not paying; and
- costs of negotiation and recovery of money.

The time impacts and costs (including bad debts) of your terms of payment need to be incorporated into your financial plan.

6.5.4 Scheduling cash receipts

The simplest way of scheduling cash receipts is to estimate the proportions of your sales revenue that will be received:

- within the same month as the sale;
- 1, 2 and 3 months after the sale; and
- indefinitely (written off as bad debts).

Then, in respect of deferred receipts, shift the proportion of revenue expected to be deferred into a later month, depending on the number of months that payment is expected to be deferred.

Bad debts are simply written off.

Now, for each month, simply add up the amounts expected to be received in that month, including:

- sales expected to be received in that month;
- sales from the previous month expected to be deferred one month;
- and so on.

6.5.5 Transaction taxes

Your sales activities may include collection of Federal, state and/or local government taxes or levies. These include goods and services tax (GST), and stamp duty, sales tax, property tax, etc. Because you are collecting these taxes on behalf of the Government, the taxes should not represent an impact on your business model. However there may be an impact on your cash flow, depending on the timing of your liability to pay the 'collected' tax.

In the case of GST, the timing of your liability to pay 'collected' tax is dependent upon your annual turnover. Below \$1,000,000 per year you may elect to account on a cash receipts basis or on an 'earned' basis. Above \$1,000,000 per year (unless you have special permission) you must account for GST when you earn it, rather than when you receive it.

6.5.6 Example of sales volume and revenue forecasts

Appendix 3 provides an example of a sales volume and revenue forecasts calculation. This worksheet has two elements:

- an estimate of sales volume and revenues; and
- a receipts schedule that shows when payments are actually received.

6.6 Production worksheet

The terminology of the business activity will vary according to the nature of your business. In the Production Plan example shown at Appendix 4 the terminology and approach are most applicable to inventory driven businesses, such as manufacturing, wholesale or retail selling and service activities. The term 'production', which is appropriate to manufacturing businesses could easily be replaced by the term 'stock purchases' for reselling and some service businesses.

6.6.1 Production volume

To provide a satisfactory level of customer service most businesses often have to manufacture or purchase more finished product (stock), or provide more capacity, than their customers will buy. For example:

- a self-serve retail store will have more cash register capability than customers to bring checkout time into line with reasonable expectations;
- perishable products prepared or offered for sale in a restaurant, fruit shop or flower shop will have to be thrown out when they are no longer attractive or suitable for sale, or they may be returned by the customer;
- some products will be damaged or lost in packaging and transport from a production facility to a point of sale;
- a services business, such as a hairdresser, accountant, consultant, or tradesman, will have periods in which staff are on stand by.

There is also a need to consider losses during the production or service delivery process (in which time and materials are lost through error):

- a self-serve retail store may have breakage of products (biscuits, bottles, jars);

- a restaurant may lose materials that are burnt or spoiled during food preparation;
- quality control in a production facility may reject a proportion of products during testing;
- a services business may have to spend time (unpaid) correcting errors or performing rework.

If these factors are relevant to your business, you will need to 'gross up' your production volume to allow for a lost production, or lost capacity factor.

For each product or service determine a production volume or level productive capacity, having regard to closing inventory levels (to avoid creating an 'out of stock' situation)

6.6.2 *Unit costs of production*

Depending on the nature of your business, calculate the cost of:

- manufacturing, delivering and selling the quantity of product required by the 'grossed up' production volume;
- purchasing, presenting and selling the volume of product required by the 'grossed up' business volume;
- providing the gross capacity or capability of your service organisation.

In developing the cost estimate, try to identify any costs that are:

- variable – costs that change according to the level of volume in your production volume plan; or
- fixed – costs that remain the same for all feasible production levels in your production volume plan.

Most operating cost estimates will comprise the following elements:

- direct internal labour, paid as salary (probably a fixed cost), fixed or casual wages (probably a variable cost);
- direct external labour, paid as contract labour services (may be fixed or variable depending on the nature of the contract – for example, 'piecework' would be a variable cost);
- direct materials, inventories, supplies, fuel (very likely to be variable costs);
- indirect labour, materials and services.

For each cost item consider the need to provide for losses of utilisation or materials and services – these are losses that occur between 'purchase' and use in the production or service delivery process:

- For internal labour, estimate the proportion of a person's time that is actually available for production or billable time. Consider that:
 - a person's salary covers 52 weeks in a year, plus a leave loading and any bonus;
 - 2 of the 52 weeks are paid public holidays;
 - normally 4 of the remaining 50 weeks are recreation leave;
 - something in the order of 2 of the remaining 46 weeks may be sick leave;
 - within an 8 hour day a person may not be productive all day.

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- For direct materials consider that:
 - some perishable materials (e.g. food, flowers, fluids) must be thrown away at the end of their shelf life;
 - some raw materials are stolen, damaged or ruined in the warehouse.

If these factors are relevant to your business, then you will need to 'gross up' your staffing or purchasing volume to allow for lost time, materials or services.

When estimating costs of production, consider the following items for the grossed up levels of production in the Production Volume Worksheet (Appendix 4):

- Direct Labour:
 - staff and wages numbers;
 - total cost of staff and wages;
 - total available hours (staff numbers multiplied by the number of hours per week multiplied by the number of weeks a person is expected to be at work);
 - utilisation of total available hours (expected billable or production hours divided by total available hours);
 - total cost per billable or productive direct labour hour.
- Direct Materials:
 - total purchases;
 - losses (proportion of materials purchased but not expected to be available for use);
 - total cost of direct materials (total purchases divided by (1 minus the loss proportion)).
- Direct Services and Facilities (e.g. delivery services).
- Indirect Labour: total cost of salaries and wages.
- Indirect Materials.
- Indirect Services and Facilities (e.g. scheduled maintenance).

So far the Production Worksheet identifies cash flows required to purchase inputs required to produce the grossed up volume of production or service capacity specified in the Business Volume Table.

There are several other costs that need to be taken into account when determining profitability and pricing:

- administrative and overhead costs;
- financing cost; and
- depreciation (amortisation of capital expenses) – depreciation and amortisation are not cash flows, but they are factors that need to be taken into account in determining:
 - unit price profitability;
 - business profitability in an accounting period (e.g. a month, quarter or year); and
 - income tax liability (which may generate a cash flow when tax is paid).

6.6.3 *Example of a business operations plan*

Appendices 2-4 provide an example of a business operations plan. This example accepts:

- input cost estimates into the Pricing & Profitability Analysis Model (Appendix 2);
- payment terms (for deferred payment, e.g. trade credit) and GST are entered into the Production Worksheet (Appendix 4).

6.7 Overheads Worksheet

The Overheads Worksheet (Appendix 5) outlines payments for all cost items that are not directly associated with production and distribution.

Typical expense items in this plan include:

- Total cost of management and administrative staff. For a very small business this includes wages paid to the business owner(s).
- Accommodation expenses, including:
 - rent, cleaning, and rates;
 - heat, light and power (where not included in the operating expense plan).
- Insurance.
- Telephone and Internet services.
- Selling and promotion expenses (advertising, printing).
- Travel and accommodation.
- Repairs and maintenance (where not included in the operating expense plan).
- Equipment lease payments.
- Annual licence fees, professional and industry memberships, corporate registration fees etc.
- Provision of electronic payment facilities (e.g. EFTPOS, credit card, Bpay).
- Interest payments. This will be a rough estimate at this stage – the final estimate of interest payment is developed at the end of the planning process because it is dependent upon the final level of debt after taking into account all other payments, including taxation and drawings or dividends.
- Taxation.

6.7.1 *Taxation and other government charges*

Governments at various levels need to raise revenue to support their activities. Government revenue raising (fiscal policy) has become a dynamic and complex issue for many reasons including:

- a perceived need to broaden the revenue base;
- absence of coordination of revenue raising regimes at Federal and state levels;

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- use of fiscal policy to provide incentives or support other government policies;
- response to revenue avoidance.

Your exposure to taxation and other revenue raising activities may be far wider than you may realise – depending on the nature and structure of your business. These may include:

- federal income and related taxation, at personal and company level, including income tax, GST, FBT, levies;
- customs, excise, levies and charges relating to imports and exports;
- revenue-raising services, such as licences, inspections, approvals.

In addition to understanding taxation from the point of view of estimating its cost impact on your business, there is the likelihood that your business may benefit from the many incentives available.

The Livewire website will provide links to sources of information about taxation and relevant government policy.

6.7.2 Example of an Overheads Worksheet

Appendix 5 provides an example of an Overheads Worksheet. The key elements of this plan are:

- a schedule of management, administrative and other overhead outlays (including GST paid);
- a worksheet that determines the amount of GST included in those outlays;
- a payment schedule in which some payments are deferred according to terms of business (trade) credit.

6.8 Cash Flow Summary and Financing Plan

The Cash Flow Summary and Financing Plan:

- summarises cash inflows and outflows and produces a cumulative balance of working capital or business funding requirement;
- outlines the sources of funds to meet that requirement; and
- estimates the cost of establishing and servicing equity and debt funding.

A sample format for a Cash Flow Summary and Financing Plan is provided at Form 1 at the back of this document.

The total estimate of cash flows provided in this Appendix are a basis for estimating the value of your business. However they are not an estimate of profit, which is an accounting number, discussed below.

6.8.1 Example of a Cash Flow Summary and Financing Plan

The bottom line in Appendix 6 is an estimate of the cost of finance based on the cash flows estimated in Appendices 1 and 3–5. This estimate may be used to update the estimate of the cost of finance you entered in the Overheads Worksheet (Appendix 5).

A sample format for a Cash Flow Summary is provided at Form 1 at the back of this document.

6.9 Basic Accounting Statements

There are many approaches to evaluation of the value and performance of a business. Business valuation based on analysis of long term cash flows is the most rigorous and objective method used by most analysts.

Business performance evaluation often takes a shorter term view – generally monthly for internal performance evaluation and quarterly, half yearly or yearly, for external reporting and evaluation.

Stakeholders who are interested in reporting and evaluation include:

- owners, who need to know what funds are available for distribution as drawings or dividends;
- management, whose remuneration may be based on accounting measures such as sales revenue, profit or composite measures such as return (profit) on capital employed;
- providers of debt financing, and advisers such as credit assessors, who need to form an opinion about the level of risk in your business;
- government revenue raising agencies who need to appropriate a proportion of the profit generated by your business; and
- insurers.

The requirement to understand business profitability on a short term (or venture) basis led to the discipline of accounting, the purpose of which is to relate costs to revenues on a periodic or venture basis. This will often involve:

- determining when to recognise revenues and expenses (e.g. accrual or cashflow methods);
- depreciation of capital assets;
- amortisation of periodic expenditures; and
- revaluation of balance sheet items, including write-offs.

The most basic accounting statements used for performance evaluation are:

- a Profit & Loss statement – often shortened to "P&L" and also sometimes called a Profit Statement or a Revenue Statement; and
- a Balance Sheet.

Stakeholders will often have conflicting objectives in evaluating the performance of a business, and therefore there are almost as many standards for the production of accounting statements as there are stakeholders.

6.9.1 The Profit & Loss Statement (P&L)

The purpose of the Profit & Loss Statement is to determine the level of profit (or loss) earned in a period of time. The Profit & Loss Statement is a key business planning document in the Livewire competition.

The basic elements of a Profit & Loss Statement are set out in Table 3, and a sample format is provided at Form 2 at the back of this document.

Table 3: basic elements of a Profit & Loss Statement

- Revenue.
- Cost of sales, including costs (including payments, amortised expenses and depreciation of capital assets) related to the earning of that revenue.

- Gross profit: calculated as revenue minus cost of sales. *(Subtotal)*
- Other operating expenses, excluding depreciation, interest and taxation.

- Earnings before depreciation, interest and taxes: calculated as gross profit minus other operating expenses. *(Subtotal)*
- Depreciation.

- Earnings before interest and taxes. *(Subtotal)*
- Interest (cost of debt finance).

- Earnings before taxation. *(Subtotal)*
- Income tax payable (based on the earnings before taxation subtotal and any eligible losses brought forward from previous years).

- Net profit after tax. *(Subtotal)*
- Abnormal items (such as capital gains or losses, or write-downs of assets, such as investments or amounts receivable).

- Transfers to retained earnings – the balance of any profit or loss is added to, or deducted from, owners funds – this is reported in the balance sheet. *(Final total)*

In the preparation of a Profit & Loss Statement, the following points should be considered:

- Are revenues and expenses recognised on an accrual basis or a cash flow basis? This is a decision on the accounting method to be used.
- Revenues do not include receipts of a capital nature, such as:
 - receipts of funds invested or borrowed;
 - proceeds of the sale of corporate fixed assets.
- Similarly, expenses do not include payments of a capital nature, such as:
 - repayments of equity or loan principal;
 - payment of dividends;
 - rent deposits;
 - the purchase of fixed assets, such as equipment – the cost of these sorts of purchases are spread over several years – the portion that is charged in any year is called depreciation.
- Revenues and expenses may be expressed net of GST.

6.9.2 Balance Sheet

The purpose of a Balance Sheet is to report the financial position of the business entity at a single point in time. While the Profit & Loss Statement reports on how a business has performed between two dates, the Balance Sheet reports on the company's financial position on a particular date.

A Balance Sheet reports the balances of three main categories of account on a particular date:

- Assets (things the business owns), which may be:
 - 'Current assets': these are assets expected to be consumed within a financial year. Current assets include items such as cash, trading stock, stationery and accounts receivable (money owed to the business).
 - 'Non current assets': these are assets that will be consumed over several financial years (or are of that nature). Non current (fixed) assets include items such as equipment, software, buildings, motor vehicles and long term investments.
- Liabilities (money the business owes to others), which may be:
 - 'Current liabilities': these are debts or other financial commitments that the business is expected to pay within the financial year. Current liabilities include items such as overdrafts and amounts owed to trade creditors.
 - 'Non current liabilities': these are debts or other financial commitments that are not expected to be completely paid within the financial year. Non current liabilities include items such as long term loans and employee entitlements.
- Owners (shareholders) funds, which include:
 - investments of equity;
 - accumulated net profits (retained earnings);
 - provisions for special purposes such as asset revaluations.

The general principle of a balance sheet is that owners' funds (equity capital) are the difference between what the business owns (total assets) and what the company owes (total liabilities).

There are many ways of presenting a Balance Sheet – however they all represent the basic principle stated above: you own the difference between what the business owns and what the business owes.

7. Business plan explanations

Prices

Prices are the charges you make to supply goods and services to others.

Costs

Costs are those charges you pay to others for the supply of goods and services.

Manufacturers

For *manufacturers*, the cost of your raw materials will strongly influence the final price of supply of the finished product. The higher the cost of raw materials the higher your supply price will need to be to cover labour and overheads.

Negotiate with suppliers for the optimum balance of the best quality and the most competitive priced raw materials for your product. The definition of cost is what it actually costs you to either buy the parts, to make the parts or what it costs you to purchase the product before you supply it.

Retailers

The cost of supplies for *retailers* is commonly your buying cost from the wholesaler, plus any fees and charges associated with freighting, storage and commissions.

These costs are calculated and proportionally allocated to each item. Combined, these buying costs and additional costs become your *cost of supplies*.

Service-based businesses

Commonly, but not always, *service based businesses* do NOT have a *cost of supply*, as the business supplies services for which an hourly or service fee is raised.

Where you will have a *cost of supply* calculate the costs associated with each individual unit of supply (the cost of supply for a service business is usually the cost per service of hired labour).

Demand and supply price

The more effective your advertising and promotion is, the more aware the marketplace will be of your business. The greater demand, the more materials you will need to buy or the more products you will have to purchase. Greater volume means greater bargaining power in relation to price from your suppliers.

At the other end of the scale, if you supply (sell) large quantities you may be able to reduce the margin of profit to make the items even more attractive to the customer and, therefore, supply (sell) even more products and make more money from volume supplies (sales) rather than increased margins.

Supply mix and price

Essentially, a *supply mix* is the number of products or services in your 'business basket'.

You can have too many supplies (products or services) and, therefore, care is needed to ensure that the range of supplies (products or services) you provide are those most relevant to the needs of the customers and the most profitable to you.

If you can identify the most profitable supplies and eliminate those supplies that will not sell so well, you will be able to better price those supplies that are in demand and, therefore, increase your profits.

Market competition

The secret to successful business is to find a market niche. In other words identify a customer demand that is not being serviced or is under-serviced and make that the objective of your business.

Unfortunately, many people will see a successful business and say '*I can do that*' and open up a similar business next door. The only problem is that there might only be enough market demand for one business to operate. With two businesses competing for limited customers, both could experience financial hardship due to the discounting war that is likely to ensue.

Quite often competitive dynamics means reducing prices as an incentive to gain customer attraction rather than looking at improving merchandising and other benefits such as customer service, product quality and after supplies service. Reducing supply price to meet market competition at any time requires a great deal of consideration.

Do not automatically assume that you can compete on price until you have fully researched all business costs and have understood the internal cost structure of your business.

8. Appendices

Appendix 1 – Business Establishment Worksheet

Appendix 2 – Pricing and Profitability Analysis Model

Appendix 3 – Sales Volume and Revenue Forecasts

Appendix 4 – Production Worksheet

Appendix 5 – Overheads Worksheet

Appendix 6 – Cash Flow Summary and Financing Plan

Appendix 7 – A 10 step guide to preparing your financial plan

Form 1 – Cashflow Statement

Form 2 – Profit & Loss Statement

Appendix 1: Business Establishment Worksheet

Initial purchases

	GST rate	Days' Credit	Jul-02	Aug-02	Sep-02	Oct-02	Nov-02	Dec-02	Jan-03
Establishment costs by date of acquisition									
Business name and company registration	0%	0			\$ 750				
Legal & accounting advisers	10%	30	\$ 750	\$ 1,000					
Computer and office equipment	10%	30		\$ 6,500					
Cabling for phone & computer	10%	30			\$ 500				
Software	10%	60		\$ 1,500					
Website	10%	60			\$ 4,000				
Telephone account and listing	10%	30			\$ 125				
Furniture	10%	90			\$ 475				
Research materials	10%	30	\$ 750	\$ 200	\$ 300				
Stationery	10%	0			\$ 500				
Licence	0%	0			\$ 2,000				
Deposit on property lease	10%	0			\$ 1,500				
Fit-out of premises	10%	60		\$ 3,000	\$ 1,500				
Total purchases			\$ 1,500	\$ 12,200	\$ 10,150	\$ -	\$ -	\$ -	\$ -

Adjustments required for trade credit (payment) terms*

Paid in same period (cash)	0	\$ -	\$ 200	\$ 3,550	\$ -	\$ -	\$ -	\$ -	\$ -
30 days' credit	30	\$ 1,500	\$ 7,500	\$ 625	\$ -	\$ -	\$ -	\$ -	\$ -
60 days' credit	60	\$ -	\$ 4,500	\$ 5,500	\$ -	\$ -	\$ -	\$ -	\$ -
90 days' credit or more	90	\$ -	\$ -	\$ 475	\$ -	\$ -	\$ -	\$ -	\$ -
Total purchases		\$ 1,500	\$ 12,200	\$ 10,150	\$ -	\$ -	\$ -	\$ -	\$ -

Establishment costs by date of payment*

Pay cash	0	\$ -	\$ 200	\$ 3,550	\$ -	\$ -	\$ -	\$ -	\$ -
30 days' credit	30	\$ -	\$ 1,500	\$ 7,500	\$ 625	\$ -	\$ -	\$ -	\$ -
60 days' credit	60	\$ -	\$ -	\$ -	\$ 4,500	\$ 5,500	\$ -	\$ -	\$ -
90 days' credit or more	90	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 475	\$ -	\$ -
Total purchases		\$ -	\$ 1,700	\$ 11,050	\$ 5,125	\$ 5,500	\$ 475	\$ -	\$ -
GST included in purchases		\$ -	\$ 170	\$ 980	\$ 513	\$ 550	\$ 48	\$ -	\$ -
GST recovered from ATO (quarterly)		\$ -	\$ -	\$ 1,150	\$ -	\$ -	\$ 1,110	\$ 598	\$ -
Purchase costs excl GST		\$ -	\$ 1,700	\$ 9,900	\$ 5,125	\$ 5,500	\$ 635	\$ 598	\$ -

* Business frequently buy goods or services, then pay later in accordance with the suppliers' credit terms - i.e. they receive "trade credit" from suppliers. Likewise, businesses will often need to supply their goods or service, then receive payment some time later - i.e. they provide trade credit to their customers. The gap between trade debtors and trade creditors is important because it is either a source of funding (where amounts owed on supplies can be deferred longer than amounts received from customers) or it requires funding (e.g. where the trade credit terms on supplies are shorter than the term for payments from customers).

GST on initial purchases

	Jul-02	Aug-02	Sep-02	Oct-02	Nov-02	Dec-02	Jan-03
\$ -	\$ 75	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
\$ -	\$ 100	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
\$ -	\$ 650	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
\$ -	\$ -	\$ 50	\$ -	\$ -	\$ -	\$ -	\$ -
\$ -	\$ 150	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
\$ -	\$ -	\$ 400	\$ -	\$ -	\$ -	\$ -	\$ -
\$ -	\$ -	\$ 13	\$ -	\$ -	\$ -	\$ -	\$ -
\$ -	\$ -	\$ 48	\$ -	\$ -	\$ -	\$ -	\$ -
\$ -	\$ 75	\$ 20	\$ 30	\$ -	\$ -	\$ -	\$ -
\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
\$ -	\$ -	\$ 200	\$ -	\$ -	\$ -	\$ -	\$ -
\$ -	\$ 300	\$ 150	\$ -	\$ -	\$ -	\$ -	\$ -
\$ 150	\$ 1,220	\$ 890	\$ -	\$ -	\$ -	\$ -	\$ -

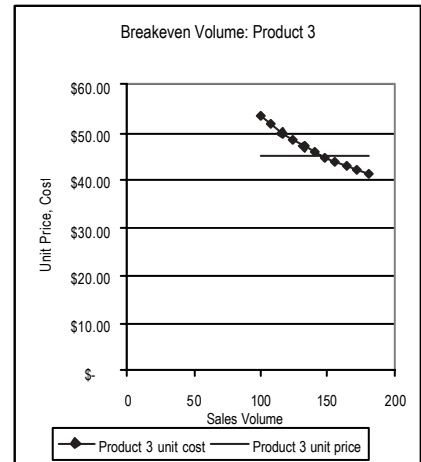
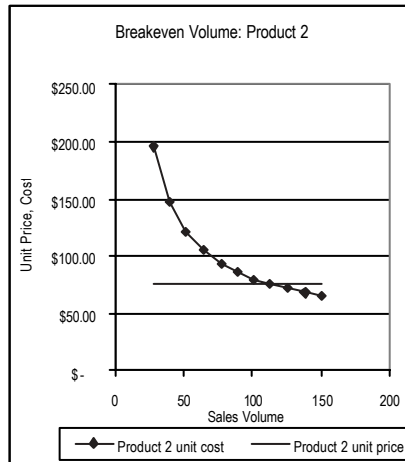
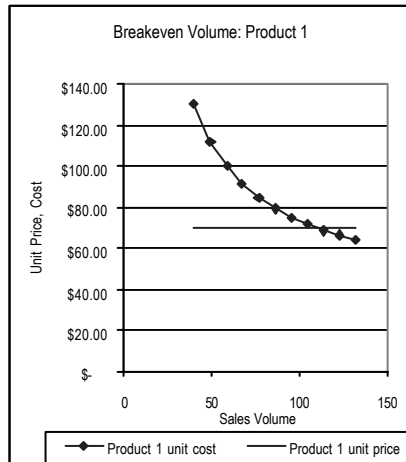
\$ -	\$ 20	\$ 230	\$ -	\$ -	\$ -	\$ -	\$ -
\$ -	\$ 150	\$ 750	\$ 63	\$ -	\$ -	\$ -	\$ -
\$ -	\$ -	\$ -	\$ 450	\$ 550	\$ -	\$ -	\$ -
\$ -	\$ 170	\$ 980	\$ 513	\$ 550	\$ 48	\$ -	\$ -

Appendix 2: Pricing and Profitability Analysis Model

Unit Price and Input Costs

	Product 1	Product 2	Product 3	Total
Unit prices	\$70	\$75	\$45	
Variable costs of production per unit				
Direct labour	\$10	\$8	\$8	
Direct materials	\$3	\$3	\$3	
Direct services	\$1	\$1	\$1	
Profit contribution	\$21	\$23	\$14	
= Total variable costs per unit	\$35	\$35	\$26	
Gross profit per unit (= price - variable costs per unit)	\$35	\$40	\$19	
Fixed costs of production				
Overheads	\$2,800	\$3,500	\$1,800	
Indirect services (e.g. cleaning)	\$1,000	\$1,000	\$1,000	
= Total fixed costs	\$3,800	\$4,500	\$2,800	
Breakeven sales volume (= total fixed costs / gross profit per unit)	110	112	145	
Actual sales volume	95	180	145	
Value of sales (= price * sales volume)	\$6,650	\$13,500	\$6,525	\$26,675
Total variable costs (=variable costs per unit * actual sales volume)	\$3,363	\$6,282	\$3,727	\$13,372
Total fixed costs	\$3,800	\$4,500	\$2,800	\$11,100
= Total costs	\$7,163	\$10,782	\$6,527	\$24,472
Profit	- \$513	\$2,718	- \$2	

Where actual sales volumes are below breakeven, profit will be negative.



Appendix 3: Sales Volume and Revenue Forecasts

Volume Worksheet

		Jul-02	Aug-02	Sep-02	Oct-02	Nov-02	Dec-02	Jan-03
Sales revenues by date of sale								
Product 1	Volume of sales				40	80	120	125
	Unit price	\$ 70	\$ 70	\$ 70	\$ 70	\$ 70	\$ 70	\$ 70
	Sales revenue	\$ -	\$ -	\$ -	\$ 2,800	\$ 5,600	\$ 8,400	\$ 8,750
Product 2	Volume of sales					100	150	250
	Unit price	\$ 75	\$ 75	\$ 75	\$ 75	\$ 75	\$ 75	\$ 75
	Sales revenue	\$ -	\$ -	\$ -	\$ -	\$ 7,500	\$ 11,250	\$ 18,750
Product 3	Volume of sales					100	180	220
	Unit price	\$ 45	\$ 45	\$ 45	\$ 45	\$ 45	\$ 45	\$ 45
	Sales revenue	\$ -	\$ -	\$ -	\$ -	\$ 4,500	\$ 8,100	\$ 9,900
All products	Sales revenue	\$ -	\$ -	\$ -	\$ 2,800	\$ 17,600	\$ 27,750	\$ 37,400

Adjustments required for trade credit (payment) terms*

Receive cash	30%	\$ -	\$ -	\$ -	\$ 840	\$ 5,280	\$ 8,325	\$ 11,220
Payment terms 30 days	40%	\$ -	\$ -	\$ -	\$ 1,120	\$ 7,040	\$ 11,100	\$ 14,960
Payment terms 60 days	25%	\$ -	\$ -	\$ -	\$ 700	\$ 4,400	\$ 6,938	\$ 9,350
Lost revenue (bad debts)	5%	\$ -	\$ -	\$ -	\$ 140	\$ 880	\$ 1,388	\$ 1,870
Total sales revenues	100%	\$ -	\$ -	\$ -	\$ 2,800	\$ 17,600	\$ 27,750	\$ 37,400

Sales revenues by date of payment*

Receive cash	30%	\$ -	\$ -	\$ -	\$ 840	\$ 5,280	\$ 8,325	\$ 11,220
Payment terms 30 days	40%	-- 30 days -->	\$ -	\$ -	\$ -	\$ 1,120	\$ 7,040	\$ 11,100
Payment terms 60 days	25%	----- 60 days ----->	\$ -	\$ -	\$ -	\$ -	\$ 700	\$ 4,400
Lost revenue (bad debts)	5%	----- indefinite deferral ----->						
Total sales revenues	100%	\$ -	\$ -	\$ -	\$ 840	\$ 6,400	\$ 16,065	\$ 26,720
GST included in sales revenues		\$ -	\$ -	\$ -	\$ 76	\$ 582	\$ 1,460	\$ 2,429
GST paid to ATO (quarterly)				\$ -			\$ 2,119	\$ 4,471
Total sales revenues post GST adj		\$ -	\$ -	\$ -	\$ 840	\$ 6,400	\$ 13,946	\$ 22,249

* Business frequently buy goods or services, then pay later in accordance with the suppliers' credit terms - i.e. they receive "trade credit" from suppliers. Likewise, businesses will often need to supply their goods or service, then receive payment some time later - i.e. they provide trade credit to their customers. The gap between trade debtors and trade creditors is important because it is either a source of funding (where amounts owed on supplies can be deferred longer than amounts received from customers) or it requires funding (e.g. where the trade credit terms on supplies are shorter than the term for payments from customers).

Appendix 5: Overheads worksheet

To avoid circular logic in the spreadsheet, enter interest expense figures from the total cost of loan finance line below this table.

GST Incl	Days'		Jul-02	Sep-02	Oct-02	Nov-02	Dec-02	Jan-03
	Incl	Credit						
Overhead costs by date of acquisition								
Salaries	0%	0	\$ 3,000	\$ 3,000	\$ 3,000	\$ 3,000	\$ 3,000	\$ 3,000
Travel	10%	30						
Insurance	10%	0		\$ 1,500				
Telephone calls	10%	30	\$ 100	\$ 200	\$ 100	\$ 100	\$ 100	\$ 100
Advertising	10%	60	\$ 500	\$ 500	\$ 500	\$ 500	\$ 500	\$ 500
Printing	10%	90	\$ 1,000	\$ 1,000	\$ 1,000	\$ 1,000	\$ 1,000	\$ 1,000
Interest expense budget**	0%	0	\$ 500	\$ 700	\$ 785	\$ 260	\$ 290	\$ 250
Income tax	0%	0						
Rent	0%	30		\$ 1,000	\$ 1,000	\$ 1,000	\$ 1,000	\$ 1,000
Total overheads			\$ 3,500	\$ 4,600	\$ 6,400	\$ 6,385	\$ 4,360	\$ 5,850

Total cost of loan (debt) finance (from Appx 6)** -1 697 783 258 288 247

Adjustments required for trade credit (payment) terms

Pay cash	0	\$ 3,500	\$ 3,000	\$ 5,200	\$ 3,785	\$ 3,260	\$ 3,290	\$ 3,250
30 days' credit	30	\$ 100	\$ 100	\$ 1,200	\$ 1,100	\$ 1,100	\$ 1,100	\$ 1,100
60 days' credit	60	\$ -	\$ 500	\$ -	\$ 500	\$ -	\$ 500	\$ 500
90 days' credit or more	90	\$ -	\$ 1,000	\$ -	\$ 1,000	\$ -	\$ 1,000	\$ 1,000
Total overheads		\$ 3,500	\$ 4,500	\$ 6,400	\$ 6,385	\$ 4,360	\$ 5,890	\$ 5,850

Overhead costs by date of payment

Pay cash	0	\$ 3,500	\$ 3,000	\$ 5,200	\$ 3,785	\$ 3,260	\$ 3,290	\$ 3,250
30 days' credit	30	--30 days -->	\$ 100	\$ 100	\$ 1,200	\$ 1,100	\$ 1,100	\$ 1,100
60 days' credit	60	-----60 days ----->	\$ -	\$ -	\$ 500	\$ -	\$ 500	\$ -
90 days' credit or more	90	-----90 days ----->	\$ -	\$ -	\$ -	\$ 1,000	\$ -	\$ 1,000
Total overheads		\$ 3,500	\$ 3,100	\$ 5,300	\$ 5,485	\$ 5,360	\$ 4,890	\$ 5,350
GST included in overheads		\$ -	\$ 10	\$ 160	\$ 70	\$ 110	\$ 60	\$ 110
GST recovered (quarterly)				\$ 170		\$ 240	\$ 280	
Total overheads excluding GST		\$ 3,500	\$ 3,100	\$ 5,130	\$ 5,485	\$ 5,360	\$ 4,650	\$ 5,070

GST worksheet

	Jul-02	Aug-02	Sep-02	Oct-02	Nov-02	Dec-02	Jan-03
\$	10	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
\$	-	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
\$	-	\$ -	\$ 150	\$ -	\$ -	\$ -	\$ -
\$	10	\$ 10	\$ 20	\$ 10	\$ 10	\$ 10	\$ 10
\$	-	\$ 50	\$ -	\$ 50	\$ -	\$ 50	\$ 50
\$	-	\$ 100	\$ -	\$ 100	\$ -	\$ 100	\$ 100
\$	-	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
\$	-	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
\$	10	\$ 160	\$ 170	\$ 160	\$ 10	\$ 160	\$ 160

\$	-	\$ -	\$ 150	\$ -	\$ -	\$ -	\$ -
\$	-	\$ 10	\$ 10	\$ 20	\$ 10	\$ 10	\$ 10
\$	-	\$ -	\$ -	\$ 50	\$ -	\$ 50	\$ -
\$	-	\$ 10	\$ 160	\$ 70	\$ 110	\$ 60	\$ 110

Appendix 6: Cash Flow Summary and Financing Plan

Notes

1. cashflows are net of GST

2. on this page, positive numbers represent cash inflows (receipts); negative numbers represent cash outflows (payment)

	Appendix	Jul-02	Aug-02	Sep-02	Oct-02	Nov-02	Dec-02	Jan-03
Cashflows from operations								
Sales revenues	3	0	0	0	840	6,400	13,946	22,249
Establishment costs	1	0	-1,700	-9,900	-5,125	-5,500	635	598
Production-related costs	4	0	0	-1,179	-4,848	-7,248	-7,863	-7,716
Overheads	5	-3,500	-3,100	-5,130	-5,485	-5,360	-4,650	-5,070
Net cash flow from operations		-3,500	-4,800	-16,209	-14,618	-11,708	2,068	10,060
Net cash flow from operations - cumulative		-3,500	-8,300	-24,509	-39,127	-50,835	-48,767	-38,707
Sources of finance								
Equity		5,000	5,000	5,000				
Loans from Owner(s)				15,000		-10,000	-5,000	0
Loans from Bank					10,000	20,000		
Total equity and loans		5,000	5,000	20,000	10,000	10,000	-5,000	0
Equity - cumulative		5,000	10,000	15,000	15,000	15,000	15,000	15,000
Loans from owner(s) - cumulative		0	0	15,000	15,000	5,000	0	0
Loans from bank - cumulative		0	0	0	10,000	30,000	30,000	30,000
Total equity and loans - cumulative		5,000	10,000	30,000	40,000	50,000	45,000	45,000
Required overdraft (-) or deposits (cash) in bank (+)		1,500	1,700	5,491	873	-835	-3,767	6,293
Cost of loan finance								
Loan Interest Rate - Owner (%/month)		0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Loan Interest Rate - Bank (%/month)		0.83%	0.83%	0.83%	0.83%	0.83%	0.83%	0.83%
Overdraft Interest Rate (%/month)		1.00%	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%
Deposit Interest Rate (%/month)		0.05%	0.05%	0.05%	0.05%	0.05%	0.05%	0.05%
Establishment Fee		-500		-700	-700			
Loan Interest - Owner		0	0	0	0	0	0	0
Loan Interest - Bank		0	0	0	-83	-250	-250	-250
Overdraft Interest		1	1	3	0	-8	-38	3
Total Cost of Loan (Debt) Finance		-499	1	-697	-783	-258	-288	-247

Appendix 7: A 10-step guide to preparing your financial plan

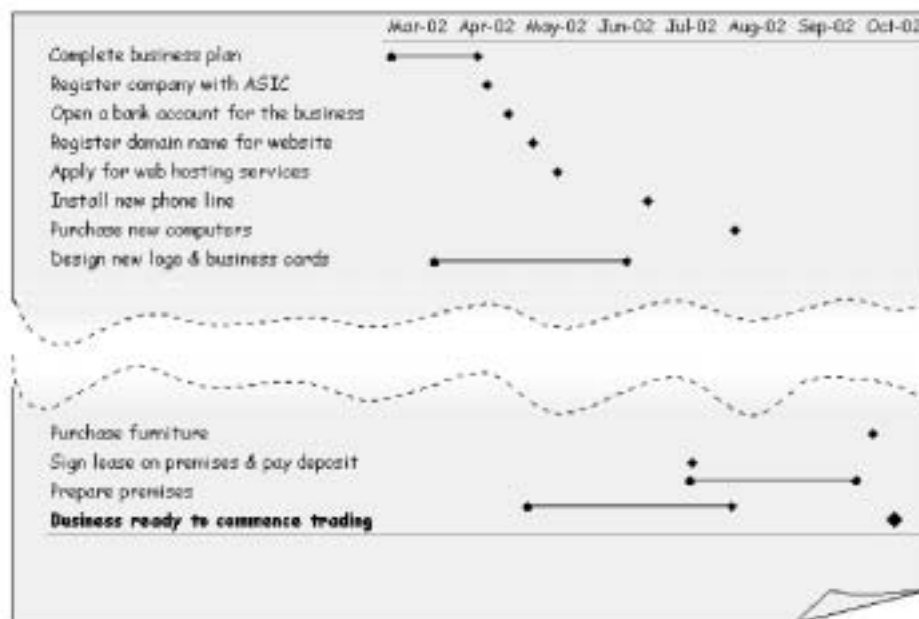
This Appendix provides a quick reference step-by-step guide to the preparation of a financial plan.

Step 1 Prepare the establishment costs budget and establishment timeline

Step 1a Identify your 'establishment activities' – i.e. the tasks and activities that are needed before you can really launch your business and start selling your products and services. Estimate the costs associated with each of those tasks or activities, and then add up the costs to give you a Total Establishment Budget. For estimated costs, you should also include best case and worst case estimates.

	Initial
Complete business plan	\$ 150
Register company with ASIC	\$ 760
Open a bank account for the business	\$ -
Register domain name for website	\$ 250
Apply for web hosting services	\$ 100
Install new phone line	\$ 330
Purchase computers	\$ 8,200
Purchase furniture	\$ 1,600
Sign lease on premises & pay deposit	\$ 2,400
Prepare premises	\$ 650
TOTAL ESTABLISHMENT BUDGET	\$ 15,940

Step 1b Estimate how long each of those tasks is likely to take, and then schedule likely start and end dates for each one.



Step 1c Finally, schedule the expenses according to the month in which they are payable, using the information above.

	TOTAL	Mar-02	Apr-02	May-02	Jun-02	Jul-02	Aug-02	Sep-02	Oct-02
Complete business plan	\$ 150		\$ 150						
Register company with ASIC	\$ 760		\$ 760						
Open a bank account for the business	\$ -								
Register domain name for website	\$ 250			\$ 250					
Apply for web hosting services	\$ 100			\$ 100					
Install new phone line	\$ 330				\$ 330				
Purchase new computers	\$ 8,000						\$ 8,000		
Design new logo & business cards	\$ 280				\$ 280				
<hr/>									
Purchase furniture	\$ 1,600								\$ 1,600
Sign lease on premises & pay deposit	\$ 2,400							\$ 2,400	
Prepare premises	\$ 650								\$ 650
TOTAL ESTABLISHMENT BUDGET	\$16,020	\$ -	\$ 910	\$ 350	\$ 610	\$ -	\$8,200	\$2,400	\$2,250

Step 2 Estimate your likely sales revenue – for at least two years into the future

Step 2a Using the result of your market research, estimate the volume of sales you expect to make during the first two years. Show these sales in the month in which you expect to make the sale. If you sell more than one type of product or service, make an estimate for each different product or service you sell.

Step 2b Calculate the expected revenue for each product by multiplying the expected volume of sales for that product by the price you have decided to charge for that product.

Add up the sales revenue for all products and services, to give you the gross expected revenue for your business.

Develop and evaluate different scenarios – e.g. a best case, worst case and an expected case.

	Annual sales		Per month sales							
	2002/03	2003/04	Mar-02	Apr-02	May-02	Jun-02	Jul-02	Aug-02	Sep-02	Oct-02
<u>Volume of sales</u>										
- Simple 1-page report	2,200	3,300	-	20	40	80	120	180	200	260
- Complete report (standard)	300	600	-	2	4	8	15	20	25	40
- Commissioned work	12	24	-	-	-	1	1	1	1	1
<u>Price per sale</u>										
- Simple 1-page report	\$ 10	\$ 12	\$ 10	\$ 10	\$ 10	\$ 10	\$ 10	\$ 10	\$ 10	\$ 10
- Complete report (standard)	\$ 25	\$ 28	\$ 25	\$ 25	\$ 25	\$ 25	\$ 25	\$ 25	\$ 25	\$ 25
- Commissioned work (avg per job)	\$ 1,500	\$ 1,650	\$ 1,500	\$ 1,500	\$ 1,500	\$ 1,500	\$ 1,500	\$ 1,500	\$ 1,500	\$ 1,500
<u>Value of sales</u>										
- Simple 1-page report	\$ 22,000	\$ 39,600	\$ -	\$ 200	\$ 400	\$ 800	\$ 1,200	\$ 1,800	\$ 2,000	\$ 2,600
- Complete report (standard)	\$ 7,500	\$ 16,800	\$ -	\$ 50	\$ 100	\$ 200	\$ 375	\$ 500	\$ 625	\$ 1,000
- Commissioned work (avg per job)	\$ 22,000	\$ 39,600	\$ -	\$ 200	\$ 400	\$ 800	\$ 1,200	\$ 1,800	\$ 2,000	\$ 2,500
Total value of sales	\$51,500	\$95,700	\$ -	\$ 450	\$ 900	\$1,800	\$2,775	\$4,100	\$4,625	\$6,000

Step 2c Adjust these sales figure to take account of delays in payment.

	Mar-02	Apr-02	May-02	Jun-02	Jul-02	Aug-02	Sep-02	Oct-02	TOTAL
Value of sales									
- Single 3-page report *	\$ -	\$ 283	\$ 400	\$ 800	\$ 1,216	\$ 1,880	\$ 2,300	\$ 2,500	\$ 8,900
- Complete report (standard) **	\$ -	\$ 82	\$ 300	\$ 200	\$ 378	\$ 880	\$ 629	\$ 1,000	\$ 2,980
- Commissioned work (long per job) **	\$ -	\$ 283	\$ 400	\$ 800	\$ 1,216	\$ 1,880	\$ 2,300	\$ 2,500	\$ 8,900
Total	\$ -	\$ 648	\$ 1,100	\$ 1,800	\$ 2,775	\$ 4,168	\$ 4,625	\$ 5,000	\$ 23,600
Value of sales (by date of payment received)									
\$ paid immediately	0%	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
\$ paid within 30 days	75%	\$ -	\$ -	\$ 398	\$ 675	\$ 1,358	\$ 2,881	\$ 3,469	\$ 4,588
\$ paid within 60 days	12%	\$ -	\$ -	\$ -	\$ 54	\$ 118	\$ 218	\$ 333	\$ 492
\$ paid within 90 days	10%	\$ -	\$ -	\$ -	\$ -	\$ 48	\$ 83	\$ 180	\$ 276
Bad debts (not paid)	3%	\$ -	\$ 14	\$ 27	\$ 54	\$ 103	\$ 139	\$ 180	\$ 600
Total	100%	\$ -	\$ 14	\$ 398	\$ 782	\$ 1,584	\$ 2,928	\$ 3,727	\$ 4,433

* Downloaded reports are paid online by credit card, so value is received immediately.
 ** Some received reports receive an invoice payable 30 days after delivery. The rest was of quote is payment, on per schedule above.

Step 3 Identify and classify your cost items

Step 3a Start by listing all the different cost items that your business is likely to incur during its first year or two of operations. Then classify these items into one of the following categories:

- Variable Non-Labour Production Costs (material and services costs that vary according to the level of production volume).
- Labour Costs.
- Fixed Non-Labour Production Costs and Overheads – e.g. phone calls, rent, accountancy fees, stationery.
- Capital Expenditure – i.e. purchases of equipment, machinery or property (other than those you've already counted as part of the Establishment Budget).
- Interest.
- Income tax.

	Cost category
* Telephone – landline	Overheads
* Telephone – mobile	Overheads
* Rent	Overheads
* Electricity	Overheads
* Bonding journals	Overheads
* Lawnmower	Capital
* Stationery	Overheads
* Internet access costs	Overheads
* Software	Capital
* Conferences & seminars	Overheads
* Wages & salaries	Overheads
* Superannuation	Overheads
* Workers' Comp. insurance	Overheads
* Professional Liability insurance	Overheads
* Lawnmower fuel	Cost of sales
* Young plants (for resale)	Cost of sales
* Lawn fertilizers	Cost of sales
* Computers & printer	Overheads
* Accounting fees	Overheads
* Gardening tools	Capital

Step 4 *Estimate variable non-labour production costs*

Step 4a Estimate your planned volume of production (if you are manufacturing goods) or your planned volume of purchases (if you are a reseller or retailer). The volume of production can be calculated as the volume of sales plus extra production to cover for:

- excess stocks held (e.g. to cater for fluctuations in sales), and
- losses due to various factors such as theft, breakage, spoilage and free samples.

Step 4b Set out on paper the relationship between your volume of production and the items in your Variable Production Costs list.

Step 4c Use the results of 4a and 4b to calculate the quantity of materials and services you will need to buy, given your expected production volumes.

Step 4d Estimate the unit costs of the individual items in your Variable Costs of Production list, and multiply these unit costs by the expected volume of purchases you need to make.

Step 5 *Estimate labour costs*

Step 5a Calculate the number of people you will require for the business, given the nature and scale of the business. Include not just salaried staff but also paid board directors, casual staff, subcontractors, etc.

In preparing this calculation note that you need to take into account factors such as public holidays, annual leave, sick leave, etc. The general rule of thumb is that a full-time worker is available for about 220 days per year, taking account of holidays.

Step 5b Calculate the direct and indirect costs of those people.

Direct labour costs include salaries and wages paid to staff, directors' fees paid to board members, etc.

However, there are also a whole set of indirect costs to consider – for example, Workers Compensation Insurance, superannuation, state payroll taxes, etc. The issue of indirect labour costs is too complex to discuss here. Therefore, if you plan to hire staff, make sure you get good advice from a lawyer or an accountant who can give you the guidance you need.

Step 5c Multiply the costs per person by the number of people in each cost group, and then add up all the costs to give an overall figure for wages, salaries, fees and on-costs.

Schedule these costs month by month in accordance with the timing of expected payments.

Step 6 *Estimate fixed non-labour costs and capital expenditure for at least the next 2 years*

Step 6a Step 3 above identified the overheads and capital expenditure costs you expect to incur.

For each of the items in this list, estimate the amount you expect to pay – and schedule the expenses to the month in which the payment is made. Detail all your calculations and specify all the assumptions you use in preparing your estimates.

	Type of units	No of units	Unit price	Total cost	Notes
* Accounting fees	Hourly fee	6	\$ 420	\$ 2,520	Annual return & related work
* Accounting fees	Fixed fee	4	\$ 95	\$ 380	BST tax return, 1 per-qr
* Computers	-	2	\$ 4,250	\$ 8,500	Pentium 400 + 17" monitor & CD: 1 each for me & Tom
* Electricity	Qtrly bill	4	\$ 225	\$ 900	Estimate based on last yr's actuals
* Gardening journals	-	12	\$ 8	\$ 96	Gardeners' Journal only
* Internet access costs	Monthly bill	12	\$ 35	\$ 414	BigPond monthly charge for 150 hrs use.
* Professional Liability insurance	Annual bill	1	\$ 1,500	\$ 1,500	Estimate only: need to confirm
* Rent	Some (b.a.)	25	\$ 175	\$ 4,375	\$175 is o.a. cost per sq metre for 25 Jack St garage
- Receptionist (part-time)	Hrs per yr	520	\$ 25	\$ 13,000	Assume 10 hrs per wk * 52 wks = 520 hrs per yr
- Programmer (for web updates)	Hrs per yr	24	\$ 85	\$ 2,040	Assume 2 hrs per mth * 52 wks = 24 hrs per yr
* Gardening tools	-	-	\$ -	\$ -	-
- Shears	-	2	\$ 25	\$ 50	One each for myself & Tom: SuperCooper Model 123
- Chainsaw	-	1	\$ 1,250	\$ 1,250	Whizzer Pro model.
TOTAL OPERATING COSTS - YEAR 1 BUDGET				\$ 37,725	

Step 7 Calculate your debt interest expense and expected income tax liability

Step 7a Estimate the volume of debt you will require using the method suggested in Step 10 below. If you have several different loans (e.g. a loan from your parents and a bank overdraft) show these separately.

Step 7b Estimate the likely annual rate of interest on each loan.

Step 7c To calculate your annual interest cost on debt, multiply the value of your debt by your assumed interest rate. If you expect to have several loans (e.g. one from your parents at a rate of 5% p.a. and one from the bank at a rate of 15% p.a.), then calculate each separately.

Step 7d Calculate your income tax liability. If this impacts on your estimate of the debt or equity you require, then update those estimates and repeat steps 7b through 7d.

Step 8 Prepare a cashflow report

Step 8a You have now assembled all the information you need to prepare a cashflow report – one of the most important reports for any business.

- In step 1 you calculated your establishment costs
- In step 2 you calculated your cash receipts from business operations
- In Steps 4-6 you calculated your cash payments for business operations, overheads and capital expenditure.
- Finally, Step 7 estimated your debt interest.

The sum of these items above gives you your net cash inflow or cash outflow.

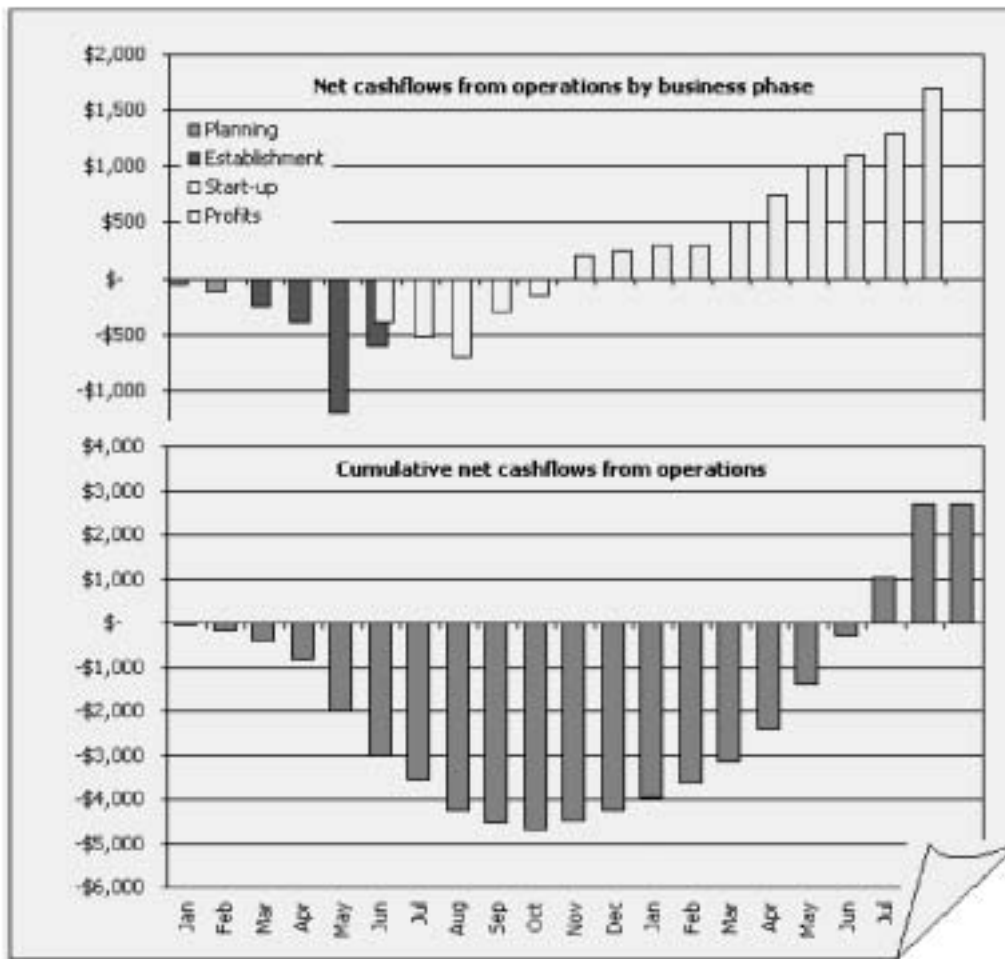
If your net cashflow for a particular month is negative (i.e. if your cash inflows are less than your cash outflows), then you have a cash deficit in that month. Conversely, if your net cashflow is positive, it means you have a surplus in that month

Step 9 Estimate your total funding requirement

Step 9a How much money does your business require during the first month, the first quarter, the first year of operations? How much will you need to borrow or fund from other sources?

The cashflow worksheet you completed in the previous step is probably the most important report you will prepare. It shows exactly how much money you will need, period by period, to fund your business – or how much surplus you have for reinvestment or debt repayment.

A cash deficit represents a requirement for further equity or debt funding which may need to be raised from your own savings, from bank loans, government grants or other sources. We refer to this as your Total Funding Requirement.



Step 10 Estimate your debt funding requirement

Step 10a Calculate the funds you can source from your own savings (assuming you are investing the money as equity, rather than a loan), from other investors (e.g. friends, family, business angels, etc) and from government grants. Call this amount Equity and Grants.

Deduct your Equity and Grants from your Total Funding Requirement. This shows you the amount you will need to borrow in the form of a loan. We call this the Debt Funding Requirement.

Enter this calculated figure at Step 7a above.

Step 10b Confirm the feasibility of the Debt Funding Requirement

There are a number of reasons why your first-cut estimate may not be viable. Most importantly, you may find that banks are unwilling to lend you money if you've just started your business. Second, you may find that your business can't afford the interest on the loan (refer back to Step 7c above).

In practice many start-ups will be unable to raise debt finance and will therefore need to manage with zero debt for many months or even years, until they can prove to a financial institution that their business is financially secure. Of course, the advantage of no debt means no interest payments either.

Step 10c Rework your financials until you end up with a feasible Debt Funding Requirement.

If your first-cut estimate of your Debt Funding Requirement isn't feasible, then you need to rework your financials over and over again until you can reduce that requirement to a feasible figure – e.g. by:

- reducing operating costs or deferring the purchase of equipment;
- using more of your own savings to fund the business, or finding more equity finance (e.g. from a business angel).

Don't be afraid to rework your whole business model if the figures don't work out at first, because many of the best business models are arrived at by finding smart solutions to difficult problems.

Form 1: Cashflow Statement

Scenario name

(e.g. Best Case, Most Likely Case, Worst Case)

Financial year Jul to Jun

Key assumptions in this scenario

	Yr 1	Yr 2	Yr 3	Mth 1	Mth 2	Mth 3	Mth 4	Mth 5	Mth 6	Mth 7	Mth 8	Mth 9	Mth 10	Mth 11	Mth 12
Cash flows from operating activities															
Receipts from sales															
Payments to suppliers and employees															
Receipts from other operating activities															
Interest and other borrowings paid															
Total cash provided (absorbed) by operating activities															
Cash flows from investing activities															
Payments for purchase of investments															
Proceeds from sale of investments															
Payments for capital items															
Proceeds from sale of capital items															
Total cash provided by investment activities															
Cash flows from financing activities															
Government grants (non-repayable) received															
Equity from owners of business (e.g. from you)															
Equity from other sources (e.g. family, venture capital, etc)															
Government loans received															
Government loans repaid															
Bank/other loans received															
Bank/other loans repaid															
Dividends paid to shareholders															
Extra financing required to fund cash deficit															
Total cash provided through debt, equity, etc															
Net cashflow															
Cash at bank - beginning of the month															
Cash at bank - end of month															

** This page shows monthly figures for year 1 only. Copy this page, and repeat the month headings for months 13-24 and 25-36 to give a full 3-year model of month

Form 2: Profit & Loss Statement

Scenario name
 (e.g. Best Case, Most Likely Case, Worst Case)

Financial year Jul to Jun **

Key assumptions in this scenario

	Yr 1	Yr 2	Yr 3	Mth 1	Mth 2	Mth 3	Mth 4	Mth 5	Mth 6	Mth 7	Mth 8	Mth 9	Mth 10	Mth 11	Mth 12
Revenue from sales															
Sales of products	+ Inflow														
Sales of services	+ Inflow														
Other sales revenue	+ Inflow														
Total revenue from operating activities															
Cost of sales															
Materials used in production	- Outflow														
Other	- Outflow														
Other	- Outflow														
Other	- Outflow														
Total cost of operating activities															
Gross profit	+Profit, -Loss														
Other income															
Interest income	+ Inflow														
Dividend & other income	+ Inflow														
Total other income															
Operating expenses															
Accommodation & meals	- Outflow														
Accounting & legal	- Outflow														
Bank charges	- Outflow														
Books & newspapers	- Outflow														
Car expenses	- Outflow														
Consultants	- Outflow														
Entertainment	- Outflow														
Insurance	- Outflow														
Internet & IT	- Outflow														
Rent	- Outflow														
Research & development	- Outflow														
Office expenses	- Outflow														
Salaries & wages (incl directors' fees)	- Outflow														
Promotions & advertising	- Outflow														
Stationery & postage	- Outflow														
Telephone, fax, etc	- Outflow														
Travel	- Outflow														
Total operating expenses															
Earnings before interest, taxation, depreciation & amortisation (EBITDA)	+Profit, -Loss														
Depreciation & amortisation	- Outflow														
Earnings before interest & tax (EBIT)	+Profit, -Loss														
Interest on borrowings	- Outflow														
Earnings before taxation (EBT)	+Profit, -Loss														
Income tax expense	- Outflow														
Net profit after tax (NPAT)	+Profit, -Loss														

** This page shows monthly figures for year 1 only. Copy this page, and repeat the month headings for months 13-24 and 25-36 to give a full 3-year model of monthly figures.

9. Your business plan submission – title page

Congratulations!

Your completed Shell *LiveWIRE* business plan is ready for submission.

Your great business idea may now offer you the opportunity to establish your own business.

We wish you every success

Please photocopy the following title page as the cover sheet to your Shell *LiveWIRE* business plan submission and submit your original plan with two (2) photocopies (for judging purposes).



Shell *LiveWIRE* Business Plan Guidelines

Participant name/s: (1) _____

(2) _____

(3) _____

Date/s of birth (1) _____ (2) _____ (3) _____

Address/es: (1) _____

(2) _____

(3) _____

Telephone: (1) _____ (2) _____ (3) _____

Mobile (1) _____ (2) _____ (3) _____

Fax: (1) _____ (2) _____ (3) _____

Email: (1) _____ (2) _____ (3) _____

Business mentor name: _____

Is this business currently trading? _____

If so, when did trading commence? _____

Business plan submission date: _____

Signature/s (1) _____ (2) _____ (3) _____