

# **STARTING YOUR OWN BUSINESS**

One of the most common reasons for business failure is inadequate planning. This often results in people going into business with too little capital, taking on unprofitable businesses or having unexpected problems. Following are points you should consider before going into business.

## **LOOKING AT YOURSELF**

In many cases the success of a small business depends as much on the skills, initiatives and capacity for work of the owner as the business itself and the economic climate. Listed are some behavioural characteristics which many small business operators have. Try to answer these questions honestly.

Are you a self starter?	Y	N
Are you independent?	Y	N
Do you like to work alone?	Y	N
Are you prepared to work long hours?	Y	N
Do you remain calm when things go wrong?	Y	N
Are you healthy?	Y	N
Can you accept responsibility?	Y	N
Are you decisive?	Y	N
Can you handle constant interruptions?	Y	N
Are you optimistic?	Y	N
Can you accept change readily?	Y	N
Can you live with an uncertain future?	Y	N

If you answered no to more than two of these questions, you should re-think very seriously, or consider getting a partner whose strong points will compensate for your weak traits.

## **YOUR FAMILY**

If you decide to go into business, you may not have the time or energy to be as involved in family activities as you are at present. Your income may drop, in the short term at least, and your family assets may be required as security for any business borrowings. Hence family support is essential for the success of a small business.

Does your spouse \ partner support your wish to go into business?	Y	N
Will he \ she support you emotionally?	Y	N
Will he \ she support you financially?	Y	N
Is your family prepared to go without holidays and luxury items for some time?	Y	N
Are you?	Y	N
Can you put your work before family during work hours?	Y	N
Are you and your partner prepared to risk financial loss?	Y	N
Have you discussed these points with your partner?	Y	N

If you have answered no to more than two of these questions, you should seriously rethink your decision to go into business.

## **YOUR EXPERIENCE**

Building a business on a product or activity of which you have some knowledge will improve your chances of success. Understanding the business environment and knowing why some firms in the industry fail when other succeed can give you the edge.

A knowledge of basic business management techniques is important. If you have not had previous management experience, consider attending management workshops or seminars. There are a number of local organizations who run seminars aimed at building your knowledge and skills in specific areas of your business. Alternatively, retain the services of business professionals. A good business development advisor, such as those at Compass Business Partners Ltd will ensure that all of the appropriate groundwork is in place as your business grows. Your advisor will also act as a sounding board for new ideas or as a sympathetic ear when the pressure starts to build. More importantly your business advisor will have the skills to combat almost any issue you will face in business, or at the very least know someone who can help.

## WHY GO INTO BUSINESS

It's important to recognize why you want to start a business. Common reasons are:

- To earn a better living*
- To be independent*
- To do something different*
- To create a job for yourself*
- As an investment*

Your reasons will affect how you will run the business and what return you will seek for your efforts.

## YOUR PERSONAL NEEDS

### Regular Monthly Expenses

House \ Rent payments	_____
Loan \ Hire purchase payments	_____
Telephone, Electricity, Rates	_____
Food, Clothing	_____
Entertainment	_____
Transport	_____
Other	_____
 Total Monthly Income Needed	 _____

This is the minimum amount that you would need to be able to withdraw regularly from you business. This may not be possible during the startup phase, so you will need to consider how you will meet these costs during this time. You may be able to survive on you savings or from your partners earnings, but keep in mind that often the startup cost of your business will be higher than you anticipate.

## **SHOULD I BUY OR START AFRESH?**

Many people feel that starting their own business will be cheaper because they will not have to pay for goodwill. This is not always the case, and in many instances it actually proves cheaper to buy an existing business. You need to do your homework on your startup costs and then weigh this up against the cost of buying an existing business. Also consider the benefits of buying an already established business – it already has a market, products, customers and a track record to help you assess its potential.

## **PREPARING A BUSINESS PLAN**

As pointed out earlier one of the most common reasons for business failure is inadequate planning. The truth is, most small businesses don't plan at all!

Reasons for writing a business plan include:

- Support a loan application
- Raise equity funding
- Define and fix objectives and programs to achieve those objectives
- Create regular business review and course correction
- Define a new business
- Define agreements between partners
- Set a value on a business for sale or legal purposes
- Evaluate a new product line, promotion, or expansion

## **WHAT'S IN A BUSINESS PLAN?**

A business plan should prove that your business will generate enough revenue to cover your expenses and make a satisfactory return for bankers or investors.

1. Executive Summary--features the highlights of your plan and sells your idea in two pages or less.
2. Company Summary--a factual description of your company, ownership, and history.
3. Products (or Services or both)--describes your products and/ or services and how they stand out from competitive products and services.
4. Market Analysis--provides a summary of your typical customers, competitive landscape, market size, and expected market growth.
5. Strategy and Implementation--describes how you will sell your product, how you will put your plan into action, and establishes milestones.
6. Management Summary--provides background on the management team, their experiences, and key accomplishments.
7. Financial Plan--contains key financials including sales, cash flow, and profits.

## WHAT MAKES A SUCCESSFUL BUSINESS PLAN?

- A well thought out idea
- Clear and concise writing
- A clear and logical structure
- Illustrates management's ability to make the business a success
- Shows profitability

## HOW DO YOU WRITE A BUSINESS PLAN?

Sitting down looking at a blank computer screen as you prepare to start your business plan can be daunting. You may want to look at some alternatives that will make the process a bit easier.

### **Hire a Professional**

A professional consultant will create the business plan for you, but you still have to be prepared to think through your business and understand the underlying concepts in your business idea. You will have to work closely with the consultant to ensure that he or she develops a good plan that accurately represents your business or business idea.

### **Buy a Book**

There are many good books on the market that will help you to understand what needs to go into a good business plan.

### **Use Business Planning Software**

A good business planning software package will provide you with an outline for a well-developed, objective-based and professional business plan. Software packages will remove the problem of starting from scratch by structuring your plan for you. The software should ask you the right questions that will pull out the most important underlying concepts within your business idea. Be careful though – this software can be expensive!

## THE PURPOSE OF PROFIT

Profit is needed to:

- Reward the owner for working in the business
- Reward the owner for investing in the business
- Replace assets
- Finance the increased working capital needs

Too many business owners do not plan to make an adequate profit.

The following exercise is designed to calculate what your minimum profit must be to meet the requirements outlined above.

***What is my profit target?***

	Target	Example
1. What is a reasonable salary for yourself?		\$30,000
2. Wage for your partner (if applicable)		\$15,000
3. If you didn't start this business, you could invest your money. (say cost of startup is \$30,000 then the opportunity cost of the business is \$30,000 x average interest rate of say 6%)		\$ 1,800
4. Your plant, fixtures and other assets will need replacing say every 3 years. Plan to meet these replacements out of profits. Divide the present value of these assets by 3		\$ 6,000
5. As you business grows your working capital needs will increase. This needs to be financed out of profits. Current working capital x say 10%		\$ 1,000
6. As your business grows you will need to increase your holdings of stock, expand your plant and possibly invest in new plant. If you assume a growth rate of say 5% of capital then allow \$30,000 x 5%		<u>\$ 1,500</u>
<b>Total Required Profit Margin</b>		<b><u>\$55,300</u></b>

If the business you are considering does not appear to have the potential to produce this profit within say 2 – 3 years then maybe it is not the business for you.

These figures are illustrations only. You will need to calculate the figures for your proposed business. The following shows in general terms how to calculate the figures for use in the above profit target calculation.

- a reasonable salary for yourself needs to reflect the level of input you have in your business. The value you use is somewhat arbitrary, but it needs to be a figure that you are happy with. You may wish to base it on your current income.
- Business startup costs are generally made up of two parts. The cost of buying assets, and the cost of gaining market recognition. Thus it may well be that your total startup cost might comprise \$18,000 spent on

- physical assets and \$12,000 spent on marketing and promotion of your business. Item 4 in the profit target calculation is concerned only with the physical assets ie the \$18,000
- Working capital is essentially the difference between your current assets and your current liabilities. Your current assets should always be greater than your current liabilities. To ensure this in times of growth, it is wise to plan for an increase in net working capital. This is most easily done by generating profits which are retained in the business – often in the business bank account. In the above illustration we have use a rate of 10%. This rate is arbitrary but it needs to be more than the average inflation rate.
  - For a new business a growth rate of 5% is reasonable for planning purposes. If your actual growth rate exceeds this, then your business plan should be flexible enough to allow for a more rapid expansion of your business.

## **BORROWING MONEY**

It is often said that small business people have a difficult time borrowing money. This is not necessarily true.

Banks make money by lending money. However, the inexperience of many small business owners in financial matters often prompts banks to deny loan requests.

Requesting a loan when you are not properly prepared sends a signal to your lender. That message is: High Risk!

To be successful in obtaining a loan, you must be prepared and organized. You must know exactly how much money you need, why you need it, and how you will pay it back. You must be able to convince your lender that you are a good credit risk.

## **BUSINESS INSURANCE**

Like home insurance, business insurance protects the contents of your business against fire, theft and other losses. Contact your insurance agent or broker. It is prudent for any business to purchase a number of basic types of insurance. Some types of coverage are required by law, other simply make good business sense. The types of insurance listed below are among the most commonly used and are merely a starting point for evaluating the needs of your business.

**Liability Insurance** -- Businesses may incur various forms of liability in conducting their normal activities. One of the most common types is product liability, which may be incurred when a customer suffers harm from using the business product. There are many other types of liability, which are frequently related to specific industries. Liability law is constantly changing. An analysis of your liability insurance needs by a competent professional is vital in determining an adequate and appropriate level of protection for your business

**Property** -- There are many different types of property insurance and levels of coverage available. It is important to determine the property you need to insure for the continuation of your business and the level of insurance you need to replace or rebuild. You must also understand the terms of the insurance, including any limitations or waivers of coverage.

**Business Interruption** -- While property insurance may pay enough to replace damaged or destroyed equipment or buildings, how will you pay costs such as taxes, utilities and other continuing expenses during the period between when the damage occurs and when the property is replaced? Business Interruption (or "business income") insurance can provide sufficient funds to pay your fixed expenses during a period of time when your business is not operational.

**"Key Man"** -- If you (and/ or any other individual) are so critical to the operation of your business that it cannot continue in the event of your illness or death, you should consider "key man" insurance. This type of policy is frequently required by banks or government loan programs. It also can be used to provide continuity in operations during a period of ownership transition caused by the death or incapacitation of an owner or other "key" employee.

**Automobile** -- It is obvious that a vehicle owned by your business should be insured for both liability and replacement purposes. What is less obvious is that you may need special insurance (called "non-owned automobile coverage") if you use your personal vehicle on company business. This policy covers the business' liability for any damage which may result for such usage.

**Office and Director** -- Under some circumstances, officers and directors of a corporation may become personally liable for their actions on behalf of the company. This type of policy covers this liability.





**Home Office --** If you are establishing an office in your home, it is a good idea to contact your homeowners' insurance company to update your policy to include coverage for office equipment. This coverage is not automatically included in a standard homeowner's policy

# CHECKLIST OF ISSUES TO COVER

## **Business Name & Ownership**

- The name of the proposed business and its location
- The legal structure of the business – company, partnership, sole trader. See the section on business structures for more information.
- The time commitment of the owners – full or part-time.

## **Your Product Or Service**

- What is the product or service
- Special features of the product or service which will create customer appeal and improve its chances of success.

## **Your Market**

- Main customers and where they are located
- Size of the market
- Your target market share
- Growth projections for your target market
- Your competitors and how you rate their businesses
- Details of the research information which has helped you determine these market characteristics

## **Marketing Your Product \ Service**

- What sales, promotion and distribution methods will you use
- What will you charge for your product \ service
- What help will you require from advertising agencies
- What will the initial marketing costs be
- What will the ongoing marketing costs be

## **Purchasing**

- Where will you source the goods you will sell
- What is the frequency of supply
- What is the reliability of supply
- What are the usual payment terms

## **Employment**

- What are your workforce requirements
- Calculate the costs – these will need to be included in your budget

**Breakeven**

- Prepare a schedule for the start of your business from arranging financing, to starting operations through to the approximate date when your business will be breaking even.

**Management**

- Detail the management and organizational expertise you can contribute
- Detail your workskills, qualifications and experience related to the product or service you intend to sell.
- List any plans you have made for training to improve your management skills

**Consultancy Services**

- Detail the consultancy services you will be using eg accountant, solicitor, banker.

**Business Records**

- Detail the system for keeping accurate business records
- Identify who will be responsible for keeping these records

**Establishment Costs**

- Investigate the costs of setting up your business. You need to include:
  - Establishment Costs
    - Tools
    - Insurance
    - Security deposits or bond payments
    - Licence \ Permit fees
    - Advertising & promotion costs
    - Stationary
    - Consultancy costs
  - Assets
    - Computer systems
    - Vehicles
    - Equipment
    - Plant
    - Installation costs for these
  - Initial Labour Costs
    - Advertising for staff
    - Training staff & self
    - Protective clothing costs
    - OSH compliance costs

## WHAT ARE YOU PUTTING INTO THE BUSINESS

Many a business owner has gone into business under the illusion that they do not need to put any of their hard earned life savings into the venture. This is simply not correct. Why should a bank put money into your business venture and bear the risk if you're not prepared to risk your own funds? Investing your own funds into your business venture is a show of your faith and dedication to what you are doing and it gives financiers confidence that you've done your homework.

You need to detail:

- What assets you are contributing to the business
- What cash you are contributing, where it will come from and when
- What materials or saleable components you are contributing.
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### **Time and Expertise Contributed**

For most business owners the biggest thing they contribute to their business is **TIME**. For most business owners the one thing they undervalue most often is **TIME**.

Your time is valuable and any time you spend setting your business up needs to be included in your startup financing plan. You need to keep track of:

- Time involved in researching, and developing your product \ service and the market
- What your time is worth
- You need to ensure that your business is going to be able to adequately compensate you for the time and effort you put into it.



## YOUR STARTUP FINANCING PLAN

Funds required for:

Land \ Buildings	_____
Plant & Equipment	_____
Vehicles	_____
Computers	_____
Establishment Costs	_____
Initial Staff Costs	_____
Working Capital	_____
Other	_____

Total Funds Required =====

Less Your Funds Contributed

Assets	_____
Cash	_____
Materials	_____

Total Funds Contributed =====

Balance to be sought =====

As a general rule you should aim not to borrow more than the amount you have contributed, and borrow only if adequate security is available.

## **BUDGETING AND CASHFLOW**

You will need to calculate the cost of doing business throughout the year and the sales you can conservatively expect. This information is shown in a budget. You will then need to estimate when the cash will be coming in and going out of the business over the year. Often there will be seasonal peaks and you will need to do some cashflow planning to ensure that surplus cash inflows are saved for periods when cash shortages might occur.

The funds required to establish a business vary widely from industry to industry. You will need to do your homework. You will need to have your budgeting and cashflow information sorted before you approach financiers for loans.

## **CONTINGENCY PLANNING**

No matter how rosy the prospects seem there is always a chance that your plans will come unstuck. If this happens you need to have a contingency plan to put in place. Your contingency plan should cover the following:

- How will I handle a shortfall in sales or cash receipts
- How will an increase in my materials costs affect profitability?
- How will an increase in my materials costs affect sales
- Is my business reliant on a key person and what will I do if that person leaves?
- How susceptible am I to competitors pushing the sales price of my product down & how will I deal with this?

## **RISKS AND REWARDS**

Running a small business is a high risk occupation. It can cause periods of unmitigated stress and leave you wondering what on earth possessed you to go into business in the first place.

However, running a small business can be a challenging and satisfying way of life. There are many things you can do to make running your business easier and less stressful. These include:

- Do something you are good at and enjoy doing
- Make sure you have the support of family before you start
- Write a business plan & have someone who knows about business plans and business in general review it for you
- Consultants are there to help – use them! They may cost money but good advisors will provide your business with benefits that far outweigh their fees.
- Systemise, systemize, systemize. The more you can replace yourself with a system, the more time you can have off – its that simple!
- **HAVE FUN!!!!**