



*Rural Women's
Network*

START YOUR OWN BUSINESS

WORK BOOK 5

FINANCE

FINANCE

INTRODUCTION

This work book seeks to answer the following financial questions to help you progress with your business idea:

- How can I develop a sales forecast?
- What's the difference between cash flow and profit and loss – and how do I develop these forecasts?
- How can I raise the money to set up my business?
- What is the role of an accountant and do I need one?
- What records do I need to keep?

SALES FORECASTING

This is probably the biggest 'guesswork' area of the whole business plan. Whilst it is guesswork, it does need to be an 'educated guess' with some thought behind it, rather than a 'stab in the dark'. These are the factors you will need to consider in estimating your sales income for your first year of trading.

- General Trend – for a new business, you should expect sales to start low. Imagine your first week in business, how many times will the phone ring? How many trade fairs will you attend? How long will it take your prospective customers to become aware of your business and/or to leave their existing supplier? It often takes 2 years for prospective customers to become aware of a new business.
- The Demand for your product or service. This can be estimated from your Market Research. You may have orders already.
- Capacity – this would be the maximum amount you could produce from projected resources. For example if you have not included staff costs, and you are only able to work 30 hours per week. Your capacity will be reached at the expected output for 30 hours of your own work and your sales forecast cannot exceed this level.
- Seasonality – will there be a greater demand at different times of the year e.g. Christmas, Tourist Season, Summer etc. This affects not only demand but also capacity – are you planning to take holidays, can you work 30 hours per week during school holidays?
- Other Factors – for example promotional activity – if successful this should be affecting demand for your product/service – its timing should affect your sales forecast.

For example, if a livery business can stable 12 horses, and charges £100 per week, then £1200 per week would be the maximum capacity. If 3 owners have expressed keen interest in switching to the new stables, then the sales forecast for the first week might be £100 and the second £200, the third £300. This would allow for a slightly staggered start. In reality, even though 3 are interested, would they **all** switch on day one?

There may be fewer horses on livery during the summer months when owners may have access to grazing.

An advertising feature planned in the local paper may yield a further 2 customers in month 2, giving further increases to our forecasted sales. Unless the market research suggests that there is a pressing demand and shortage for the facility, it would possibly only reach full capacity after 6-12 months.

Below is a check list of factors to consider in compiling your sales forecast

- General Trend
- Demand
- Capacity
- Seasonality
- Other Factors

Using the information that you have about your proposed business, use the table below to compile a sales forecast for your first twelve months.

| | M1 | M2 | M3 | M4 | M5 | M6 | M7 | M8 | M9 | M10 | M11 | M12 |
|--|----|----|----|----|----|----|----|----|----|-----|-----|-----|
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CASH FLOW AND PROFIT AND LOSS

It is really important that you understand the difference between profit and loss and cash flow. For example, a business can be really profitable, but be on the verge of going under because of poor cash flow. This may be caused by the amount of time it takes debtors to pay, lack of credit facilities with suppliers. It is therefore extremely important that you are able to forecast your profitability and when money is likely to come in and go out of your account.

CASH FLOW FORECASTING

This is a prediction of the business bank/cash accounts.

- It will include only those items which involve a movement in cash/liquid funds.
- These items will be included as they are paid or received.
- It shows how much liquid funds will be available/needed during a specific period of trading. (How much you are likely to spend in a month, and how much you are likely to receive from customers, grants, loans etc.)

PROFIT & LOSS FORECASTING

This is a prediction of how much profit will be earned (or loss incurred) during a specific period.

- It will include any item which affects profitability.
- These items will be included on a time basis according to when they are earned or incurred, regardless of when or indeed whether they have been paid/received.
- It shows how much income is earned after deduction of costs.

FOCUS ON THE DIFFERENCE

A Wealthy Woman?

A woman owns a house worth £750,000. The House Price Index is increasing at the rate of 15% per annum. She works part time and earns £100 per week. Her weekly outgoings are £200 per week.

A Wealthy woman
CASH FLOW

PROFITABILITY

This example illustrates the different focus, and demonstrates why it is important to look at both. Clearly something needs to be done to address the negative cash flow – either some form of borrowing or perhaps releasing capital from the house to provide an income, or letting a room to provide supplementary income.

The Farmer

At the start of the year, a farmer has 10 cows and 20 sheep. Cows are worth £300 each and sheep are worth £50 each. During the year each cow has 2 calves and each sheep has 3 lambs. No livestock are sold. Feed and vet bills total £100 for sheep and £100 for cows for the year and are paid immediately.

CASH FLOW

PROFITABILITY

| | Cows £ | Sheep £ |
|------------------------|---------------|----------------|
| Start of Year | | |
| End of Year | | |
| Growth in Value | | |
| | | |
| Less Costs | | |
| Profit | | |

The Fashion Victim

A Fashion business buys (and pays by cheque) merchandise for £65,000 during the year. There is no opening or closing stock. The merchandise is sold for £50,000 during the year and payment is received by a combination of cash and cheque. The owner takes no drawings whatsoever, but introduced £25,000 of her own funds during the year.

A Fashion victim
CASH FLOW

PROFITABILITY

FINE TUNING THE FOCUS

The table below shows the difference between cash flow and profitability. Refer to this table when developing your cash flow forecasts and profit and loss forecasts. This will help you to determine what to include in each.

| Item | Included in Cash Flow? | Included in Profit & Loss? |
|---------------------------|----------------------------------|-----------------------------------|
| Purchase of Fixed Assets | Amount paid out in total | No – depreciation only |
| Owner's drawings | Amount withdrawn | No – not affected |
| Bank Loan Repayments | Amount repaid | No – interest only is an expense |
| VAT (if registered) | Amount paid or received | No – not included |
| VAT (if not registered) | Amount paid | Yes – as part of expense incurred |
| Capital Introduced | Amount received | No – not included |
| Grants Received | Amount received | |
| All relevant items | When received or paid for | When earned or incurred |
| e.g. Sales | When customer pays | When sold or invoiced |
| e.g. Goods for resale | When purchased from supplier | When sold (or used up) |

YOUR OWN FORECASTS

Proformas have been included for your use.

When you have completed these forecasts, consider;

- Is the finance sufficient?
- Is the business forecast to be profitable?
- What are the limitations of these forecasts?

SOURCES OF FINANCE

- Grants
- Own/family savings
- Bank Loans
- Bank Overdrafts

Other (i.e. venture capital)

CREDIT CONTROL – Lending your customers money. This needs careful consideration. Here are some factors to take into account.

- Industry norms – what do your competitors offer?
- Risk – are your customers credit worthy?

Application for Credit Facilities

Credit reference agencies

Bank Status Enquiry

Trade References

Credit Limits

- Cash Flow – can you **afford** to lend your customers money?
- Discounts – a settlement discount may encourage your customers to pay on time.

RECORD KEEPING REQUIREMENTS

1. Detail note of start up capital introduced (inc Equipment, stock, cash etc)
2. Consider appropriateness of a separate bank account for your business and carry out regular reconciliations.
3. If choosing to have a separate bank account, you will need a good user friendly cash book with analysis. Keep it simple and easy. Write up at least weekly.
4. Cash book analysis should have headings agreed with accountant to suit YOUR business or consider using the expense headings on the tax return. One should most definitely be DRAWINGS.
5. If you don't choose a separate bank account, keep analysed lists of business income and expenditure.
6. Keep all invoices, receipts. Number reference them and file them in order.
7. Keep careful note of any capital introduced and its SOURCE.
8. Count and value the stock at the end of your accounting period.
9. List any outstanding expenses at the end of your accounting period.
10. Record all of your business mileage (can be done in a diary)

ROLE OF AN ACCOUNTANT

- What can an Accountant do to help my business?

An accountant should be able to advise how to keep records and the best way to minimise your tax liability. They can also advise on profitability and decision making in business.

- How much will it cost?

Obtain at least two prices for comparison.

- Choosing an Accountant

As with any service for your business, you should ask for recommended providers.

Ask how much the fees will be for your first year.

Check whether you will be charged for telephone consultations.

Ask/consider your VAT registration options.

Ask about your choice of year end date and whether you should consider incorporation.

Think of an example of an expense you are unsure of and ask if it is allowable against tax

- What can I do to minimise accountancy fees/tax liability?

At end of first year ask whether you could improve the accounts information provided for next year

Ask what the fee will be for your second year

Keep your records/documents in good order

- Do I need one?

H M REVENUE & CUSTOMS

You must register as self employed with HMRC within **3 months** of starting your business. There is a £100 penalty for late registration.

HMRC BUSINESS SUPPORT TEAM based at your local tax office can provide **excellent** support and guidance.

- ◆ Carlisle 01228 400987.
- ◆ Barrow 01229 615841
- ◆ Penrith 01768 861755

They run training sessions for new businesses targeted at specific groups e.g. Newly Self Employed, New Employers etc. The number for course enquiries is 0151 242 8380

NATIONAL INSURANCE

- ◆ Class 1 – Employed
- ◆ Class 2 – Self Employed Flat Rate (Small earnings exception on profits less than a certain limit determined by HMRC)
- ◆ Class 3 – Voluntary - for those who do not pay NIC any other way but who want to retain relevant rights
- ◆ Class 4 - Self Employed 8% of profits between certain limits(and 1% on higher profits above those levels)

Details of all rates and limits can be found by telephoning the H M Revenue and Customs Helpline or from the website www.hmrc.gov.uk

Filing your tax return online is an 'easy to use' and effective option. The software calculates your tax for you, you can store your return on your own computer whilst you gather information to complete it, and only when you select 'submit' will it be sent to the Inland Revenue. Start your registration process on www.hmrc.gov.uk

Profit and Loss Forecast

| | £ | £ |
|-------------------------------------|---|---|
| | | |
| Sales (from your sales forecast) | | |
| | | |
| Less Cost of Sales (Variable costs) | | |
| | | |
| | | |
| | | |
| Gross Profit | | |
| | | |
| | | |
| Less all other expenses; | | |
| Rent and Rates | | |
| Advertising / Marketing | | |
| Printing, stationery, postage | | |
| Insurance | | |
| Loan interest | | |
| Motor / travel | | |
| Professional fees | | |
| Depreciation | | |
| Wages (excluding your own) | | |
| Other; | | |
| Bank charges | | |
| | | |
| | | |
| | | |
| Net Profit | | |
| | | |
| | | |

Calculate your Gross Profit % = $\frac{\text{GP £}}{\text{Sales £}} \times 100$

Check required Break Even level of sales:

Break Even Sales Level = $\frac{\text{'all other expenses' £}}{\text{GP\%}} \times 100$

Is there sufficient profit to provide the required amount of drawings? Compare the two figures below:

£

Net Profit

Own drawings required