Start Up Lancashire

Social Enterprise

Toolkit

Workbook 4

Finance: Start Up Costings and Budgeting Setting

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Selnet
Social Enterprise Lancashire Network

Disclaimer

Any information pertaining to the law, legislation and regulation is provided in good faith.

You are advised to seek professional advice or consult with the relevant body to discuss the legal position as it relates to you and your enterprise before deciding upon your final course of action. Such bodies will include: Companies House, Charity Commission, HMRC.

The information supplied was checked in December 2012 and may be subject to change, especially legislative and monetary values, so you are advised to check for updates.

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Introduction

This workbook has been written to run in conjunction with business adviser support and developed for the 2013/14 Start-up Lancashire programme part funded through European Regional Development Fund (ERDF).

The workbook has been developed to support SUL "Social Enterprise Toolkit".

It is aimed at the entrepreneur(s) or community group starting a social enterprise business. It has been designed to help you understand the financial implications of setting up a social enterprise and what they mean to you.

In our experience, the majority of social enterprise start-ups are led by one or more people who intend to work and earn a living out of the business. They often give up paid employment to run the business.

We cannot cover all the different employment options but in general, if you are setting up an incorporated company then you will be a director and as such an 'employee' of the company.

In this workbook we refer to your income as "Drawings" and expect yourself and the business to cover Tax and N.I. under a PAYE basis.

There could be an option for you to be self-employed within the business so you may need to take professional advice on how this would work best for yourself.

There could be director dividends payable, especially in a Community Interest Company and share options if you are a company limited by shares. We are not addressing any of these areas in this workbook and recommend you seek professional advice.

Social enterprises are often referred to as the third sector and not-for-profit organisations. Throughout this guide we are choosing to refer to them as businesses and use business terminology, e.g. profit instead of surplus. They are businesses and just like any business, they have to make a profit. In the current economic climate with more commissioning opportunities from the public sector, third sector organisations need to take more commercial approaches in order to survive.

How to Use this workbook

It is not necessary to read this workbook cover to cover. Follow the index links on the next page to read the sections that are of interest to you and your organisation.

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Starting Up

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When you are setting a start-up budget, the issues you need to consider include:

- Your own personal situation, especially if as with many entrepreneurs, you are looking to earn a living out of the business.
- How much money you need to set up the business.
- How you will raise any finance required.
- How much cash the business will generate.
- How much you will need to spend each month once you begin trading.
- When will your sales exceed your income?

Your Personal Survival Budget

We are calling this a survival budget because for many people who start a new business, they will be unlikely to be able to guarantee the levels of earnings they had when they were in a salaried position. It is usual to expect to take less out of the business in the early days to give it the best chance of growth.

The budget considers what the minimum is you could live on and that will be your starting point in deciding whether to make the leap from any security within your current situation. Setting up a business is probably one of the hardest things you will ever do, but it can be the most rewarding!

Remember that in this first exercise you are only calculating your personal expenditure, not any expenses the business may incur. Ensure that you include all of the items that you have the responsibility to pay for in your household. If you have any other items of expenditure that do not appear on the list, include them in the 'other' box.

The budget is based on your expenditure per month; so if there are bills that you pay weekly, quarterly, or annually, remember to multiply/divide them by the appropriate amount.

Consider your own financial circumstances, and how those circumstances may change when you leave employment to work in a new social enterprise.

If your earnings drop for a period how would this affect any benefits that you are currently entitled to, such as housing/council tax benefit. Similarly, if your income rises what will the effect be, will they stop? If you are not sure what benefits you may be entitled to, seek advice from a Welfare Rights Advisor.

It is important to ensure that your business will generate sufficient surplus for you to live off. The form below is designed to calculate your total monthly personal outgoings to establish the minimum monthly income you personally can survive on.

Table 1

Items of expenditure	Monthly £
Rent/Mortgage	
Council Tax	
Water rates	
Electricity/gas	
Telephone – landline - internet - mobile	
Housekeeping (food, cleaning materials etc.)	
Clothing	
TV license	
Entertainment	
Newspapers, magazines etc.	
Hobbies – subscriptions/memberships	
Car tax & insurance	
Car running expenses (fuel & maintenance)	
Other travel	
Childcare	
Pensions & savings	
Personal loan repayments	
Credit card payments	
Class two national insurance contributions	
Other:	
Total expenditure:	

Now that you have established your average monthly expenditure, the next step is to identify any income that you may already have, or possibly claim for, to help meet this expenditure. Again remember that this is a monthly budget. Depending on your personal circumstances, you may receive some, all or none of the items below:

Table 2

Estimated income outside self employment	**Monthly £**
Income from family/partner (if this contributes to the expenditure you have listed)	
Part time work	
Maintenance/allowance payments	
Pension	
Family Allowance	
Tax Credits	
Childcare Tax Credits	
Other benefits (e.g. disability living allowance):	
Other income:	
Total income outside self-employment	

To give a new business the best chance of survival, it is best to minimise your drawings as much as possible in the first year to avoid getting into debt. For this reason we establish the minimum drawings that you could take from the business and 'survive'. This is calculated by subtracting the total income (above) from the total expenditure (on the previous page). What remains will be the minimum amount that you could draw from the business per month in order to survive.

Table 3

Minimum drawings calculation	**Monthly £**
Total Expenditure	
Total income outside self-employment	
Total expenditure minus total income **(minimum monthly personal drawings)**	

NB. In some cases, your income may exceed your expenditure. This occurs when there is already enough income coming into the household to cover all the bills, and drawings from the business are not 'necessary'. In this case it is best to set very low drawings to allow the business a healthy cash flow.

Start-up Costing's

Every business has start-up costs, which can be the single highest level of expense the business will incur. It is extremely important to get this right and, if possible, not to cut corners because the necessary finance is not available (easier said than done!). Cutting corners can result in poor quality or even present a health and safety problem. On the other hand, don't get too carried away, ensure that any costs you are listing are absolutely essential.

It is extremely important to be realistic when calculating your start-up costs and to ensure that you allow for all costs. Typically, start-up costs would include equipment, website, stock, stationery, marketing materials, insurance, rent and staff recruitment, etc.

When you start to write your business plan you will use this comprehensive list of start-up costs. See Selnet's supporting **"How to Write a Business Plan" Workbook**.

When compiling this list bear in mind that we are talking about the actual amount you will need to start up and open the doors for business. You may for example need to pay one month's rent in advance, but you will not need the full years rent in month one. You may however need to allow for working capital during the first few months of trading, whilst sales are building.

Look out for costs that can be spread over a period of time e.g. your insurance costs may not have to be paid in full but on a standing order basis.

You should also make a list of any equipment and stock that you already own and its value. This will show that you have already made a commitment to the business start-up and can be useful in leveraging additional funding.

Table 4 Items already acquired for business start up

Equipment	**Value in £**
Stock	

Table 5 **Business Start-up Requirements**

Use this table to help you calculate your business start up requirements. Remember some costs can be spread, so make a note of this in column one of the tables in the appropriate section.

Business start-up costs	**£**
Equipment	
Sub-Total	
Transport (car insurance, mot, fuel, business trips, etc.)	
Sub-Total	
Advertising (leaflets/flyers, newspaper ads, etc.)	
Sub-Total	
Premises (rent, rates, fixtures & fittings, refurbishment, etc.)	
Sub-Total	
Opening Stock	
Sub-Total	

Professional fees (legal, accountancy, licenses, cost of training etc.)	
Sub-Total	
Other (equipment hire, delivery, stationery, marketing, recruitment, insurance, utility connection, etc.)	
Sub-Total	
Total Start-up Requirements	

These figures will be used in the cash flow forecast.

Other things to consider:

Office Space

In the Social Enterprise Toolkit we discussed the options of working from home or renting office space, or even sharing an office with another organisation.

In your business plan you will consider the capacity issues around the space available, in terms of growth and expansion opportunities in the future.

- Are you going to work from home initially and then expand to an office or unit?
- Will you need space for storage of stock and equipment?
- How will you secure/insure this space and do items require special conditions e.g. temperature, ventilation?
- Will you need more space with an increase in staff?

When assessing the amount of space you will need in your business, take into account housing equipment, storage of raw materials and stock, administration and filing, workspace and a reception area if applicable.

Equipment

This refers to general office equipment and also specialist equipment for the business's activities, i.e. gardening equipment, play and games equipment.

Plan your equipment requirements carefully. Do you need a colour photocopier capable of handling large production runs or would a simpler black and white single sheet printer suffice? Does everyone need a laptop/PC?

There is little point in investing money in lots of equipment that will rarely be used and takes up space within the workplace. Also consider that you may not be in a position to buy 'top of the range', brand new equipment when you first start –consider leasing.

More and more social enterprises are looking at ways to share office services to reduce costs. Is there another local organisation that has some of the equipment that you need now and again that you could use for a small cost?

Second hand/overhauled equipment, with guarantees, from reliable sources could be an option as could service and maintenance agreements or leasing equipment.

- Is the equipment absolutely necessary?
- What equipment will you require should you expand to provide further services?
- Who will operate it and will they require training and/or a licence?
- What insurance and maintenance will be required for the equipment?
- Should you lease or purchase?
- Have you got the space?

Staff

This is you and/or other directors looking to earn a living out of the business and any staff you may employ.

Think carefully about the most beneficial role for your staff to play. Employing people is costly to a small business, so are there other options?

Could people be employed on a sessional basis?

Could you recruit volunteers?

Stock

You may not need to carry stock; it depends on the type of business you are.

However, for businesses that do, storing and ordering sufficient stock is crucial to the efficient running of a small business and satisfying customer needs. It can be difficult when starting a new business to estimate the demand for certain products, but your market research should assist you in refining the range and level of stock you should carry to start with. Storing and timing the re-ordering of stock becomes easier once you have established a regular customer base. Customer demand and continual market research will enable you to make more informed decisions about stock. Remember the following points:

- Stock ties up cash, so careful planning is crucial, only order what you need to cover short periods of time to begin with.

- Identify a number of reliable suppliers (market research) who offer credit terms and next or same day delivery, this will assist in controlling stock and cash.
- If you do make mistakes you may need to reduce the price and be prepared not to make any profit in order to get rid of stock and free up some of your cash and storage space.

Think about your stock levels:

- How much cash can you afford to tie up in stock?
- How quickly can your suppliers deliver?
- How regularly will you need to re-order?
- How frequently will you change/update your stock lines?
- Will you stock high turnover / low profit items or high profit / slow turnover items?
- Will you have any special storage requirements for stock e.g. temperature, valuables?
- Will you require a license to store stock e.g. hazardous substances, livestock?

Once the costs and financial projections have been established in the business plan the enterprise will know how much initial funding will be required. This will need to cover set up costs, and ongoing overheads for any anticipated shortfall in revenue.

Table 6: Funding your business start

Sources of funding	**How much?**
Own capital: (cash or value of equipment etc. see table 4)	
Bank capital:	
Other loans:	
Grants:	
Other:	
Total Start-up Funding	

Note: the total in tables 5 and 6 should be the same

Summary

We have calculated how much you will need to earn out of the business for your efforts.

We have calculated how much money you need to equip the business to get it 'off the ground' and all the immediate running costs and expenses.

So that's the money going out, next we need to see how much income or turnover the business could generate in its first year towards these expenses.

Sales Forecasting

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Social enterprises and 'sales'

The obvious social enterprises that 'sell' are community shops, pubs and cafes but many social enterprises may not consider that they 'sell' anything. They deliver services that support people and communities.

Another way of looking at sales is as income, revenue or in calculating turnover.

A social enterprise often has mixed income streams from contracts or grants and maybe some fee-paying services.

Example: A social enterprise that provides training/support to young people may have a contract with their local authority to deliver the training or they may charge for it by the session or they may have a one-off grant from a funder. If they charge per session they will issue receipts for cash sales. If it is a contract they may be paid a proportion up front and the remainder upon agreed results. Therefore they will issue invoices at agreed stages to receive their income. If it's a grant they will have the money in the bank before they start the service and it will be recorded as income.

These are all sales and when forecasting you will consider all of the many ways that you can generate sales.

Before you start trading you can only make informed estimates, once you have some trading history then you can start to re-forecast based on more realistic figures.

Sales Forecast

The sales forecast gives you the opportunity to explain to potential funders and management that your figures have not just been plucked optimistically from thin air, but have in fact been arrived at through careful research and thorough analysis of the business and the market.

Forecasting can be daunting you have to make estimates and assumptions. However, your market research into competitors, customers and suppliers should give you a good indication of the likely sales to expect and the prices you will be charging so that there is rationale to your guesses and it establishes the feasibility of your business.

The sales forecast:

- Will assist you in completing your budget and cash flow forecast.
- Can also be used as a basis for setting sales targets for the following year.

Most businesses experience seasonal fluctuations that are led by consumer demand and create peaks and troughs, the busy times and quiet times throughout the year. You should consider carefully the likely seasonal fluctuations in your forecast as the business may be affected dramatically by the time of year. Other calendar events such as religious celebrations or school holidays may also be factors to consider throughout the year. Christmas may find you stretched to your limit whilst January and February may be extremely quiet. This may be something to think about with regard to your business start date.

Social enterprises are so varied in the goods and services they deliver that it is difficult to generalise about how they will operate. Some start with a commissioned grant and others enter a competitive market with a compelling offer.

They may use marketing techniques to launch the business and start under a blaze of publicity, which may mean that their sales are high for the first weeks and then even out to a steady rate. Some tend to lurch from one contract to another.

REMEMBER - High sales figures don't always lead to large profits

Use the checklist below to help you map out your sales forecast for your first 12 months of trading.

Checklist for sales:

- **Gradual build-up** of sales across the first year as reputation grows etc.
- **Existing customers**, or contracts already lined up
- **Seasonal fluctuations**, if applicable
- **Events**
- **Natural peaks and troughs**,
- **Repeat customers**
- **New customers**

When promotions are planned use your marketing plan - this should increase your sales. However, if your promotion involves a discount such as 10% off - remember to account for how this will increase the sales - but decrease the value of each sale.

Table 7 **Example Sales Forecast**

Month	What sales do you expect?	£ value of these sales	Why do you expect to get these sales?
1			
2			
3			
4			
5			
6			
7			
8			
9			
10			
11			
12			

Setting Budgets

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A budget is simply a financial plan for your business that covers a specific period of time. It is a key element of your business plan as it details the financial performance that you expect your business to achieve.

Many people have a fear of producing financial plans in case they get it wrong; however, the system of planning for your business is exactly like running a household budget. Just think of the financial plan in these simple terms:

How much you can make in the business and when; how much will it cost you and when?

Take a few minutes to consider these two scenarios:

- Your next month's cost of living
- Planning your summer holidays

For both of these typical occurrences the two things you need to consider are:

- Income and when it is likely to arrive
- Costs and when they will have to be paid

Another key consideration in business is how much profit you are likely to make, and therefore the potential for the business to be sustainable and develop.

Note: As we are going to refer to different budget costs and headings we have listed them below to show which costs generally relate to which heading.

Capital costs: This is usually a one-time expense for tangible goods such as a building, plant or equipment Items after which there will only be recurring operational or running costs. They can also be expenses for intangible assets such as trademarks and software development.

Capital introduced: This is usually cash or other assets introduced into the business by the owners.

Fixed Costs: also referred to as **overhead & administrative** costs or **Core** costs.

These are things likely to remain the same throughout the year e.g. rent, rates, lighting, heating, labour costs for personnel who support the business, insurance, maintenance, utilities, computer equipment, telephone rental, etc.

Variable costs: also referred to as **running costs.** These are things likely to change depending on levels of activity i.e. office supplies, petrol, cleaning, telephone calls.

Direct costs: These headings are the businesses variable costs but also relate to the direct delivery costs of an individual project/programme or service. Items include:

Personnel:	wages and salaries of full or part-time persons on the project.
Contract services:	consultant and service contracts, include fees and travel.
Supplies:	consumable supplies used on the project.
Equipment:	purchase and rental costs as well as maintenance and repair.
Travel:	all travel and meal costs related to project.
Communications:	telephone bills, postage, etc.
Publications:	printing, publishing or copying brochures, reports, reprints.
Other:	miscellaneous items not included elsewhere.
Indirect Costs:	The overhead costs that arise from the general support and management of a project/programme or service provided by the business, e.g. use of facilities, equipment, staff, line management, etc.

The Annual Budget

Income

The sales forecast will estimate what income, sales or turnover the business believes it will achieve in the year.

Add any non-sales predicted income that you expect, e.g. membership, subscriptions, donations, fundraising etc.

Make a clear note of how you arrived at each figure and on any items you were not sure about. Without the notes you may look back at the figures in a few days and not remember the assumptions you made.

The first year's budget is the most difficult. A lot of guesses have to be made because there is no historic information.

Expenditure

It is very important to include all the likely areas of expenditure. Missing something out is the same as budgeting no expenditure on that item. Be realistic about costs and be prepared to delay or not to start the business if the budget doesn't stack up.

Start by making a list of all the expenditure headings (items) in the business. Include all the start-up items and their costs from Tables 5 & 6.

Estimate the likely amounts of expenditure against each heading.

Make notes on how each figure was arrived at. If it is a guess or broad estimate say so.

Similar items like salaries and employer's national insurance should be grouped together under the same heading.

Keep running cost headings separate from capital cost headings.

Note: *A general rule* - Underestimate your income and overestimate your expenses.

Apportioning fixed costs

Where you have specific programmes, e.g. a child-care programme or a support programme for young mothers or young people you should develop a budget for each programme to show the direct and indirect running costs for each. It may be a continuous service for the same beneficiaries/clients or it may run several times a year from different client groups.

You will need a methodology to add a % of the fixed overhead costs (those that can't be assigned to the indirect costs) to your service budgets.

If you have three programmes for example, then you may consider apportioning the shared overheads on an agreed % basis against each programme's budget depending upon the size and value of the contract and how much resources are required to deliver, e.g. one may contribute 50%, one 30% and one 20%. It will depend upon the value of the contracts and the resources required to service each programme.

Developing these budgets also relates to **setting the unit price**.

Note: A quick method of budgeting for you or employing a member of staff is to take their salary and add on approximately 25%. This will give you a basis to cover the on costs: employer's national insurance contributions, and pension if applicable, liability insurance and payroll function costs.

Full Cost Recovery (FCR)

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More social enterprises are looking at pricing services using FCR. We can't go into the accountancy methods of FCR in this workbook and would recommend you look at the various products/software that are around that will help you.

What is full cost recovery?

FCR means securing funding for, or "recovering", all of your costs, including the direct costs of projects and all your overheads. All businesses, whether voluntary, public or private, need to recover all of their costs, and ideally generate a surplus, or they cannot pay their employees, rent office space, offer products and services, or plan for the future and the continued development and delivery of services.

If you are not recovering the full costs of a project you are creating a deficit for your organisation. This deficit has to be met through additional fundraising or through subsidy from your unrestricted funds/savings.

Your unrestricted funds/savings are not limitless. If you are not achieving full cost recovery you are jeopardising the longevity of your organisation and hence the services you provide.

Why has full cost recovery become so important?

- Pressure on funding.
- Funders require greater transparency.
- Need to calculate costs accurately when contracting.
- FCR is a mechanism to allocate overhead costs to projects that is easy to understand and acceptable to funders.
- The cost allocation principles of FCR are endorsed by the Charity Commissioners, HM Treasury, a panel representing the voluntary sector that includes funders and are consistent with the Statement Of Recommended Practice.

Funders get:

- Stable organisations and services.
- Better services.
- No cross-subsidisation.

Principles of full cost recovery:

- Materiality.
- Average costs (rather than marginal costs).
- No cross-subsidisation.
- Use of cost drivers (any situation or event that causes a change in the consumption of resources).

However, there are still issues within some contracts where commissioners set a fixed % allowance towards company overheads, i.e. not more than 9% irrespective of the size of the contract. This can and does cause problems for some businesses as they cannot fully cover the associated costs in delivering the contract.

Show the draft budget to people who are part of your business. Make sure you talk to those responsible for delivering specific parts of the service.

Has anything been left out? Are extra headings needed? Missing out a heading is the same as giving that item a budget of £0. It is better to guess than leave something out altogether. At the same time would the budget be simpler if several headings were grouped together?

Check on the items you were not sure about. Is more information needed to improve the accuracy of the estimated figures?

When is the funding likely to be received and when are the activities likely to start? Will inflation affect the budget? It may vary from one heading to another.

Options and contingencies

Is the income less than the expenditure? If so, what are your plans?

What if you don't get the contracts you predict and you have a shortfall of income? Can activities be scaled down?

Would you cancel or postpone the business start-up or would you split the business development into different phases?

What will happen if some income is late?

Should you plan for other unexpected circumstances?

Capacity Planning

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Capacity Planning describes the operational aspects of running the business. You will consider the factors that may place limits or constraints on the business. These can be resources: **Time, Staff, Stock, Equipment, Space** and **Cash.** By considering such factors you will have a clearer picture of how the business will be managed on a day-to-day basis and what it can achieve within the resource levels.

This also relates directly to your sales and cash flow forecasts.

Capacity planning is a useful management tool and should be monitored on a regular basis to identify problem areas or areas of good practice that can be repeated elsewhere within the organisation.

Once you have established the levels of capacity consider the following situations:

- How will you cope when you reach a position of over capacity?
- If you are not reaching your targeted levels of capacity, what will you do?

You could consider the following:

- Advertising to increase demand.
- Extending the range of services or the variety of services offered.
- Subcontracting your service to other organisations.
- Short time working / Shift working / Overtime working.
- Increasing resources e.g. more people, space or equipment.

Setting a price for your product or service

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How much are you going to charge your customers for your product or service?

This is so fundamental to the success of every business, and yet for many social enterprises they feel they have limited control over their charges.

In the open marketplace the private sector will look at factors such as quality, value for money, uniqueness, differentiation and customer choice in pricing what they sell.

For many social enterprises their marketplace is in contracting with the public sector to deliver a range of services to benefit their target groups and communities. Areas like: debt counselling, support to disadvantaged families, rehabilitation of offenders, disabled people and older people to name but a few.

The commissioning arena is getting tighter. Less money requires 'more for less' and your business has to meet these challenges. Often the unit price is dictated by the contract and the business has to shape its costs accordingly if it wants to do the work. Many times social businesses report that they have to shape their service to fit a price and they have to cut their cloth accordingly. Some of the 'nice to do' things that they provided aren't possible and it can change the culture of a charitable organisation as they feel driven towards more commercial approaches.

However, commissioning opportunities are expanding and for businesses that can demonstrate their added value and have set up without a grant dependant model, they can find exciting new opportunities.

Pricing Principles

For some products/services pricing can be based on three critical points:

- What your product or service will be worth to your customers - its value.
- What it costs you to produce your product or provide your service.
- The price your competitors charge.

Your cost structure provides a basis for what you need to charge. But it will not necessarily show you what you can- and should charge.

Divide your business costs into two headings:

Variable (Direct) costs – these increase when your sales increase because they are the costs associated with delivering the product/service. The more you do the more it costs you.

Fixed costs – these largely remain constant, regardless of how much or little you sell (e.g. rent, salaries, business rates).

Note: As long as the price you sell at is higher than the variable cost, each sale will make a contribution towards covering fixed costs and making profits. Your business and financial planning is all about identifying how much you need to and can sell to cover all the business' fixed costs and leave you with something left over at the end of the period.

It is certain that you will face competition in some form so you could research the opposition and benchmark your potential pricing.

Depending upon your marketplace this may or may not be applicable. It is probably unwise to set your prices too much lower or higher without good reason.

- Too low and you will throw away profit.
- Too high and you will lose customers.

Cost-plus pricing

Take the cost figure for each product/service and add a mark-up.

Marking up

This is usually based on two elements:

- The mark-up you must add to the cost to make the desired profit, and
- The mark-up used by competitors.

The mark-up is usually expressed as a percentage of the cost.

If the final price looks uncompetitive, review the size of the mark-up.

Note: If you can't make the price competitive it may be that your cost base is too high, in which case you are going to have to do a serious review of your set up.

Different products and businesses apply hugely different mark-ups. For example, retail mark-ups include:

- Fridges: cost plus 25 per cent.
- Branded clothing: cost plus 135 per cent.
- Jewellery: cost plus 250 per cent or more.

Margins

A margin indicates the percentage profit a business makes after applying a mark-up.

For example, if a business buys a product for £10 and marks it up by 50 per cent, thus selling it for £15, the margin is 33 per cent (the value of the mark-up, divided by the selling price, x 100).

Margins are good barometers of how important particular products or services are to the profitability of your business.

Flexible pricing

Aim high - It is easier to reduce prices than raise them.

If in doubt, try higher prices first.

- Be prepared to lower prices if the required sales volume is not achieved and your cash flow is under pressure.
- Low prices often go hand-in-hand with poor quality and service. Is this the image you want to create?
- Some companies can win more customers (as well as boosting their margins) by putting their prices up.
- For a start-up, competing on price is often a mistake. Low pricing is more often a strategy of big companies that cannot compete on service.
- What you will be able to offer is a string of benefits such as convenience, personal service, speedy delivery and specialist skills. That is why customers will buy from you.

Cash Flow Forecasting

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When you prepare your Business Plan you will prepare a cash flow forecast. At start up stage these can only be estimated projections. The figures in your cash flow forecast will be directly related to your sales forecast and market research should be supported by cash flow assumptions.

As a forecast, the cash flow is a useful tool to help you set your pricing structure and also monitor projected income and expenditure. The cash flow cannot be used as an indication of *profits*.

The cash flow differs from the sales forecast by showing the actual points at which cash comes into or goes out of the business; unlike the sales forecast, which shows when orders are placed and sales are made. You should also take into account any credit terms you will be receiving from your suppliers, credit terms you will be offering your customers and late payments. You should allow for all these things in your cash flow.

It is necessary to continue the process of forecasting your Cash flow throughout the life of your business, to anticipate when you are going to have cash in your bank and when you are going to have to make payments.

Forecasts can only ever be a best guess. It may be beneficial to produce three scenarios; worst case (pessimistic), realistic and achievable and best case (optimistic). Could the enterprise survive on the worst case?

Some costs you may already know, these will be the same headings that you used when setting budgets:

- You will use your sales forecasts.
- You will use your expenditure forecasts.
- You also need to include in your business plan a statement to cover:
    - Any sensitivity regarding the projections and assumptions made in the cash flow forecast.
    - Any reasons to doubt the projections. e.g. historical results.
    - When break-even will be reached.
    - What alternatives there may be and what your exit route will be.

Completing Your Cash flow forecast

Your Cash flow forecast is split into two parts, Income and Expenditure.

In the income section along with your sales figures you will record any other types of income such as grants and loans, as and when you predict that they will arrive.

Similarly for expenditure; for example, if you expect to spend £250 on rent in month one, then that amount is placed on the row for rent, in the month one column. Likewise, if you have indicated in your sales forecast that you expect figures in July and August to be high, you must account for any associated increase in stock purchases or direct wages.

Every transaction should be recorded in the month you realistically believe it will happen, when income will clear through your bank account, and when expenditure actually leaves your account.

Remember the influence of seasonal fluctuations or peaks and troughs, as discussed previously in sales forecasting. It is likely that your business will be subject to some sort of seasonal demand that can have a great effect on your predictions for your cash flow forecasts.

Note: If calculations include pence, round the figure up. If the pence is .50 or above e.g. £232.55 = £233. Round down if the figure is below .50 e.g. £232.10 = £232. The figures in your cash flow should always be rounded figures, not including pence.

Name:													

Cash flow Forecast Year 1

Month	1	2	3	4	5	6	7	8	9	10	11	12	total
Cash in													**£**
Sales													
Grants													
Loans													
Capital													
Total Income	(a)												
Cash out													**£**
Capital Equipment													
Drawings													
Stock													
Direct Wages													
Rent													
Rates													
Heat/Light													
Insurance													
Advertising													
Stationery													
Loan Capital													
Loan Interest													
Telephone													
Postage													
Hire of Equipment													
Professional fees													
Repairs & Renewals													
Motor/Travel													
Sundries													
VAT													
Total Expenditure	(b)												
Net Cash flow	(c)=(a-b)												
Bal before	(d)												
Bal carried forw.	(e)=(c+d)												

(C) Balance before (last month's Balance carried forward)