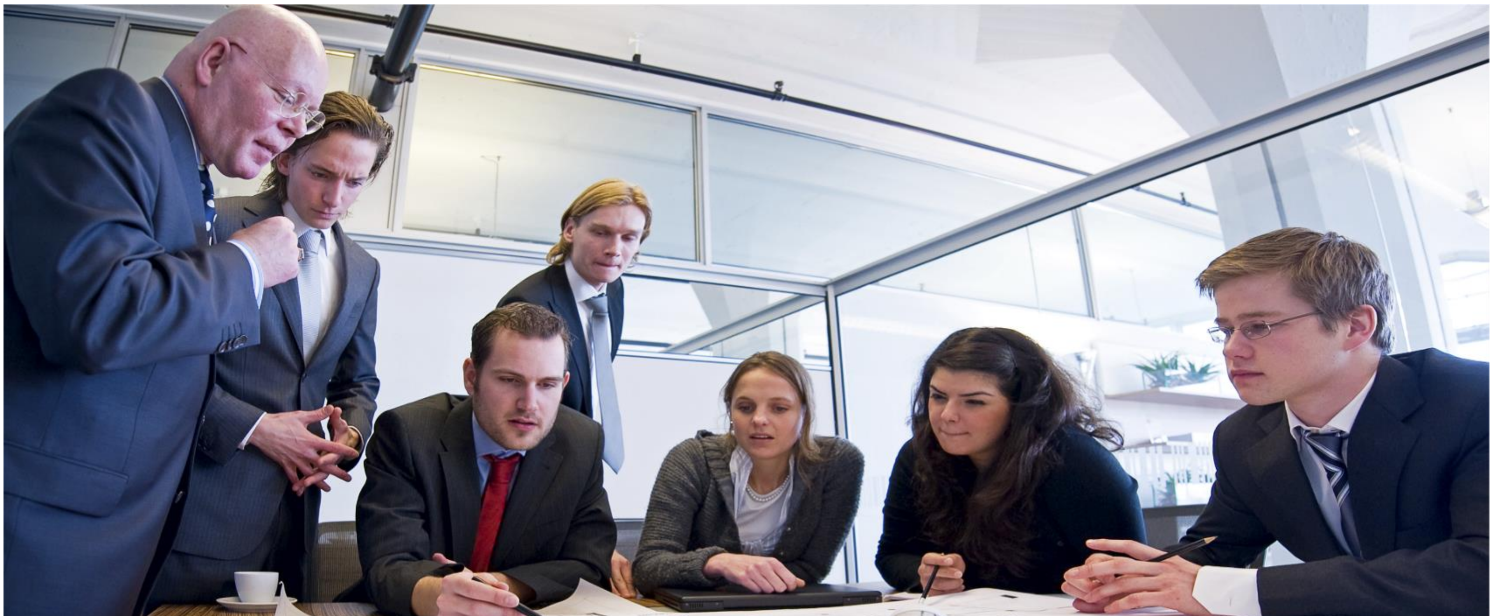

UNIT-13 Starting A Business

Learning Outcomes

By the end of this unit the learner will be able to:

- ✓ Explain the nature and meaning of entrepreneurship and its relationship to creativity and innovation.
- ✓ Analyze the stages in the entrepreneurial process.
- ✓ Assess the feasibility of a small business opportunity
- ✓ Develop a business plan

Unit 13

Starting a Business

Getting a business off the ground is no easy task. Numerous questions await you as to what kind of products or services you will offer, how much you'll charge for them, what type of marketing strategy you will execute, and how you'll manage your cash flow – you will need to sit down and solve all these mysteries before you make a penny.

In any successful business operation the secret ingredient is planning. Before you plan to set up your own business, you must make sure you have a sound business mindset, some unique business ideas, and excellent management skills. Without these, you're likely to pack your bags before you even get there.

There are two kinds of businessmen in a new business venture: an entrepreneur and a corporate entrepreneur. Entrepreneurs are individuals who establish a new organization without the benefit of corporate support while corporate entrepreneurs are new-venture creators working in big companies.

The table below lists some of the extraordinary entrepreneurs who founded their companies famously successful. It can be noted that all of the following founders started in their 20s.

Company	Founder(s)
Microsoft	Bill Gates and Paul Allen
Netscape	Marc Andreessen
Dell Computers	Michael Dell
Gateway 2000	Ted Waitt
McCaw Cellular	Craig McCaw
Apple Computers	Steve Jobs and Steve Wozniak
Digital Equipment Corporation	Ken and Stan Olsen
Federal Express	Fred Smith
Genentech	Robert Swanson
Polaroid	Edward Land
Nike	Phil Knight

Lotus Development Corporation	Mitch Kapor
Facebook	Mark Zuckerberg

Fig: 13.1

Source: ***J. A. Timmons, New Venture Creation, 6th Ed., p. 7 (2004)***

Entrepreneurs start their own firms because of the challenge, the profit potential, and the enormous satisfaction they hope lies ahead. People starting their own businesses are seeking a better quality of life than they might have at big companies.

Advantages of Owning a Business

Some main advantages of owning a business are outlined below:

- **Control.** The authority to make decisions rests with you. As a boss, you have the power to direct all activities of your business.
- **Creative Freedom**. Without the restriction imposed by set policies and the need to go through channels, your ideas and talent can be freely expressed.
- **Profits.** The more successful your business is, the more money you can make. Whereas employees' salaries generally depend on budget approvals, yours is directly linked to your performance.
- **Job Security.** Because it's your business, you can't be fired, laid off, or forced to retire.
- **Pride**. You gain the satisfaction that comes from knowing you have built your business into a successful operation through your own efforts.
- **Wealth.** Owning a business gives you the opportunity to build wealth, creating an asset that you can borrow against, sell, or pass on to the next generation.

Disadvantages of Owning a Business

Some main disadvantages of owning a business are outlined below:

- **Investment at Risk.** If the business fails, you could lose your entire investment. In addition, your personal assets may be jeopardized.
- **Long Hours.** Keeping your business going is rarely just a 9:00 to 5:00 proposition, especially in the beginning. Be prepared to put in many 12-hour days to make it work.

- **Fluctuating Income.** Instead of reliably receiving a steady pay check, you depend on income that is subject to the ups and downs of the business.
- **Responsibility.** The freedom to make decisions carries the burden of standing by them. If anything goes wrong, ultimately you're the one who's responsible.
- **Pressure.** There's always the pressure to please your customers, meet your payroll, and satisfy the demands of your creditors.
- **Regulations.** You must abide by federal, state, and local laws, as well as the safety stipulations imposed by your insurance carrier.

Do the advantages of owning a business outweigh the disadvantages? That's something only you can determine. Just as some individuals can be happy only when working for themselves, others prefer to work for an employer. In planning your own business, it's important that you keep sight of your own needs and wants. Will owning a business enable you to satisfy them at a price you're willing to pay?

Do I Have What It Takes?

Do you have what it takes to own and operate your own business? It isn't a matter of how smart you are; it's more a matter of personality and behaviour. Researchers have found that individuals who possess certain characteristics are more likely to succeed as business owners than those who lack these characteristics. Although there's not total agreement as to the characteristics that are most important, those frequently cited include:

- **Motivation**
- **Confidence**
- **Ability to make decisions**
- **Human relations skills**
- **Communications skills**
- **Technical ability**
- **Vision**

If you possess the required characteristics of a business man and have a sound business idea at hand, put up the business and make it official and legitimate. It is on the legitimacy of the business where the people's judgment of company's acceptance, appropriateness, and desirability is stemmed. Making the business official also helps the new firm acquire other resources such as top managers, good employees, financial resources, and government support.

Start-up Costs

Costing is regarded as the process of collecting, analyzing, summarizing and evaluating various alternative courses of action involving costs and advising the management on the most appropriate course of action based on the cost efficiency and capability of the management. With that, it can be noted that though starting a business will really incur costs, going through the right cost management will actually provide financial cost efficiency for the starting business.

Also, an entrepreneur must be able to identify the different types of costs in a business. By the careful classification of these costs, a business can analyse its performance and make better-informed decisions.

The main three classifications of costs are:

- **An Opportunity Cost** is the financial benefit instead of the next best alternative use of money. The opportunity cost of buying a new piece of machinery might be compared with the benefits of spending the money on a new advertising campaign.
- **Variable Costs** respond to the changes in proportion to the amount of output produced.
- **Fixed Costs** are the indispensable and dormant costs of the business such as land and building.

1. **Direct Costs** are costs which can be identified directly with the production of a good or service; e.g. Raw materials.
2. **Indirect Costs** are costs which cannot be matched against each product because they need to be paid whether or not the production of goods or services takes place; e.g. Rent.

The Business Plan

Irrespective of the kind of business you start, you will definitely need a business plan. A successful business carries two main things, excellent mind and effective plan. In order to create an effective business plan, you need to know the basics of each component laid out within.

- **Overview**

  Though this comes first in your plan, but you write it in the end. This is basically a summary of what you have covered in your plan in a nutshell for people to understand at a glance what your plan is all about.

- **About your Business**

  This section will cover details and an overview of your business. It covers the kind of products and/or services that you wish to offer. Remember not to use business jargon as it will only complicate things if your message sent across is not fully understood.

  However if you need to use technical language, make sure you include a table within that section highlighting what those terms mean in layman language. However it is recommended you use simple English and error-free text.

- **Demographic Information**

  This section will highlight your target market. Therefore, you must exhibit your target demographics for people to know who your prospective client base is. This information can be obtained either from the internet or from an expert market research analyst.

- **Marketing Information**

  This section highlights your marketing strategy. Include all the strategies that you wish to use and explain how they will be used and the effect it will create on your business.

- **Financial Information**

  This is known to be the most important part of your business plan, therefore, make sure you organize it correctly as this could make or break your new business startup dreams! This section alone has five important aspects that need to be covered.

  - ✓ **Investment**

    This section is used to prove to others that you’re willing to invest in your own business and require financial assistance from them. You should however estimate to invest at least 30% cash investment.

  - ✓ **Loan Request**

    Here you must detail out how much money you need to borrow and how that money will be used. Remember, this is not a section to keep it brief. Be as elaborate as possible. You may include quotations wherever applicable.

  - ✓ **Other Investments**

    Here you should highlight the number of people who have agreed to invest with you in the startup of your business. Equity participation should also be included here.

- ✓ **Projected Income**

  This section works only on estimates. You will need to come up with a reasonable projected income that you will make and this can be made easier with the demographic research that you carry out. Remember to keep the numbers realistic and achievable.

- ✓ **Repayment Plan**

  This is the section that every investor wants to see. Based on this they will make their decisions of whether to support you financially or not. Therefore make sure your repayment plans are realistic and don’t forget to include interest rate calculations.

- **Business Workforce**

  This section should highlight all the people that you will have employed or involved within your company. Their successes, rewards, certification, work history and references should all be included in this section. Be sure you clearly mention the roles that they will bear within your company.

- **Index**

  This will basically act as a road map to your business plan. In simple terms, it is your Table of Contents and you can put all the supplementary information in this section.

The Business Plan describes all the elements involved in starting the new venture. It describes the venture and its market, strategies, and future directions. It often has functional plans for marketing, finance, manufacturing, and human resources.

Creating a business plan shall help in determining the feasibility of the enterprise, guide in the planning and organizing, and help in obtaining financial resources.

Outline of a Business Plan

i. **Executive Summary**

1. Description of the Business Concept and the Business
2. The Opportunity and the Strategy
3. The Target Market and Projections
4. The Competitive Advantages
5. The Economics, Profitability, and Harvest Potential
6. The Team
7. The Offering

ii. The Industry and the Company and its Product(S) or Service(S)

- ✓ The Industry
- ✓ The Company and the Concept
- ✓ The Product(s) or Service(s)
- ✓ Entry and Growth Strategy

iii. Market Research and Analysis

- ✓ Customers
- ✓ Market Size and Trends
- ✓ Competition and Competitive Edges
- ✓ Estimated Market Share and Sales
- ✓ Ongoing Market Evaluation

iv. The Economics of the Business

- ✓ Gross and Operating Margins
- ✓ Profit Potential and Durability
- ✓ Fixed, Variable, and Semi-variable Costs
- ✓ Months to Break Even
- ✓ Months to Reach Positive Cash Flow

v. Marketing Plan

1. Overall Marketing Strategy
2. Pricing
3. Sales Tactics
4. Service and Warranty Policies
5. Advertising and Promotion
6. Distribution

vi. Design and Development Plans

a) Development Status and Tasks
b) Difficulties and Risks
c) Product Improvement and New Products
d) Costs
e) Proprietary Issues

vii. Manufacturing and Operations Plan

a) Operating Cycle
b) Geographical Location
c) Facilities and Improvements

d) Strategy and Plans
e) Regulatory and Legal Issues

viii. Management Team

a) Organization
b) Key Management Personnel
c) Management Compensation and Ownership
d) Other Investors
e) Employment and Other Agreements and Stock Option and Bonus Plans
f) Board of Directors
g) Other Shareholders, Rights, and Restrictions
h) Supporting Professional Advisors and Services

ix. Overall Schedule

x. Critical Risks, Problems, and Assumptions

xi. The Financial Plan

- Actual Income Statements and Balance Sheets
- Pro Forma Income Statements
- Pro Forma Balance Sheets
- Pro Forma Cash Flow Analysis
- Breakeven Chart and Calculation
- Cost Control
- Highlights

xii. Proposed Company Offering

a) Desired Financing
b) Offering
c) Capitalization
d) Use of Funds
e) Investor's Return

Appendixes

Source: J. A. Timmons, New Venture Creation, 5th Ed., p. 374 (1999) by Jeffrey A. Timmons

Guidelines for Successful Planning

The following guidelines should help you to master the planning process and to become more proficient at preparing, updating, and using business plans.

1. **Set Aside Sufficient Time for Careful Planning**. Recognizing the need to plan is one thing; allocating the time to do it can be another. Call it "planning phobia" or simply "procrastination." Whatever the case, if your business is to succeed, you must devote significant time to planning.
2. **Determine in Advance what you want to Accomplish.** What is the purpose of your planning effort? Whether it is to prepare a business plan for a new venture, to update an existing plan, or to obtain financing, by identifying your specific goals for planning, you can focus your attention on the key issues or activities that need to be addressed.
3. **Make sure you have Access to the Necessary facts.** Information is what fuels the planning process. To plan effectively, your information must be relevant, accurate, and up-to-date. This means having access to internal information, such as accounting records and sales reports, and external information, such as industry trends and consumer buying habits.
4. **Coordinate your Planning Efforts with the Efforts of others.**Make sure that each person involved in the planning process knows what everyone else is doing. To avoid working at cross purposes—with you pursuing one planning objective while a partner or employee is pursuing another—you must coordinate your efforts. This is the only way to maintain harmony and ensure that the various goals set for the business are compatible.
5. **Keep an Open Mind.** To achieve the best results as a planner, avoid getting locked into one approach to a problem or situation. Give different strategies a chance to develop and explore various possible courses of action. Above all, let yourself be creative. Rather than starting out with a preconceived idea of what your business should or should not do, take time to consider the alternatives.
6. **Solicit Input from Others.** Don't be afraid to ask for advice and to get other people's viewpoints. As your business grows, these diverse insights will become increasingly important. The planning process works best when the people responsible for creating the business plan collaborate with those who will be called upon to implement it.
7. **Review your Business Plan.** Once you complete your business plan, go over it to see that it clearly depicts your business and adequately states your intentions for the business. Before implementing it, make sure that it will help you to achieve your objectives.
8. **Update the Plan.** Many business experts recommend updating a business plan every six months. That way you can determine whether the plan is continuing to meet the needs of your business. As circumstances change or as new information becomes available, update the plan accordingly.
9. **Make the Plan Accessible.** All too often, business plans are kept from the very people who need to see them. Keeping proprietary information from your competitors makes sense; keeping it from your own people does not. For key employees to fully contribute their talents and abilities to the business, they must know what it stands for and where it's going.

10. **Use the Plan.** Most important of all, use your business plan. A plan that's gathering dust on a shelf or that's buried in a filing cabinet cannot do any good to you. If your plan really is going to be the blueprint for a successful business, you must put it to work.

Go Official

Apart from just deciding on your products, services, marketing plans and organization there's something else most businessmen dread; and that is whether to go official and register your business with the appropriate agencies or not.

Remember that the challenge comes only when you build and run your new business. You will need both confidence and guts to get your business rolling as planned. Your mind will be filled with all sorts of questions and you will note that not all the questions have a proper set of answers.

That is normal to feel because some of the questions you may have in your mind may be those that you've never asked anyone or been asked by anyone simply because neither you nor anyone else have tried the idea before.

Starting your own business means making your own decisions, but you will need to trust yourself with the decisions that you make, you will need to develop a great business sense, and you will need to be judicious when taking the advice of other people. Of course it is not easy to maintain the balance and the harmony but you will get better with experience as you host your own show.

How to Determine your Costs

Its time you decide how much money you will need to start up your new business concept.

List Everything Down

Make a list of everything that you will need to get your business running and then attach price values to them. You may get an advisor to assist you with this.

1. **Sales Forecast and Budget**

   Forecast sales for two years based on market research and then plan your budget accordingly. Your budget should be realistic and must have room for enhancement or any unforeseen events.

2. **Expense Forecast**

   Much like sales forecast, here you will need to determine the amount of expenses that you will incur in, say two years, and that will help you plan your budget accordingly. Don't include unnecessary expenses as you're starting up, keep it to a minimum but leave room for unforeseen expenses.

3. **Cash-Flow Statements**

   This statement shows you all the projected cash inflows and outflows along with your company's net cash flow every month. In order to get a somewhat accurate number as to the amount of money required for a business startup, you need to run a collective net cash flow line below the monthly net cash flow line.This will show you the negative cash flow that you have generated in that particular month. If you use more cash than you take in from the customers, this is known as a negative cash flow.

The first few months of your business can experience negative cash flow and that is very normal. Just add up your highest negative figures to the total of your startup expenses and you'll get the estimated amount required for business startup.

Setting the Price

In setting the prices for your products and services, among the facts to be considered are the reactions of your customers, the stiffness of the competition, and the state of the economy.

You may decide to go head-to-head with competitors on prices by matching them, or to undercut them, or to charge higher prices.

The strategy you choose is crucial to your pricing. Take care also not to overlook the state of the economy. Unemployment, inflation, interest rates, government policies, and levels of investment all have an effect on consumer spending and therefore on your prices.

You must also consider another factor: profit. If your prices are so low that they fail to cover your expenses, or so high that an insufficient number of people want to buy from you, the result is a loss of profits. Your goal is to meet the demands of customers, keep an eye on competitors and the economy, and assure yourself of satisfactory profits.

Pricing and Customers

Part of knowing what prices to charge comes from knowing your customers. Affluent customers generally demand high-quality merchandise, personalized service, and an exclusive and attractive environment in which to shop. In exchange for these amenities, they are not only willing to pay more, but also expect to pay more. Low-income customers, on the other hand, are willing to settle for less quality and service and a no-frills, discount-house environment in exchange for lower prices. In each case the price is what counts.

Pricing and Competition

Keeping tabs on competitors' prices helps you to assess your own pricing strategy. Are yours higher or lower than the competition? If your prices are higher, you're probably losing out on sales. If your prices are lower, you may be making more sales but passing up additional profits.

Here are some of the sources of information you can use to stay in touch with competitors' pricing strategies:

Customers: Observe your customers' shopping habits, and listen to what they have to say, so that you can get a pretty good idea of how your prices stack up against the competition.

Suppliers: Because your suppliers are also their suppliers, this is another source of competitive information. Don't forget that the information flows both ways. Your competitors can tap into the same source to find out about you.

Advertising: By following competitors' promotional campaigns, you can keep track of pricing changes and obtain current information about the quality and service being provided.

Competitors' Catalogs and Price Lists: When these are available, they are an excellent source of information, particularly because the prices are not only current but also conveniently arranged for easy reference.

Price Checkers These shoppers are employed by you to go out and gather information about competitors' prices. While pretending to shop, they actually record the prices of various key items.

Pricing and the Economy

Customer shopping habits reflect the state of the economy. During a recession or depression, customers are at their most price conscious. Worried about the high cost of living, threats of unemployment, and cutbacks in credit, they want to make every penny count. As the economy improves, customers become more optimistic about the future and are more willing to pay higher prices. When the economy is at its peak and business is booming, customers offer little resistance to rising prices.

As a business owner, your ability to recognize these fluctuations in the economy and to adjust your prices accordingly adds to your competitiveness.

To keep your prices in line with customers' expectations, you may add or drop products and services, raise or lower quality standards, change your markups, or put together some combination of these.

Pricing and Profit

Your prices should be set at a level sufficient to reimburse you for the cost of the goods or services sold, cover your overhead costs, and provide a profit. The amount of profit you receive will be dependent on your gross margin, or markup. This is the difference between the cost and the selling price of the goods sold. The higher the markup, the greater your profit per sale However, this doesn't necessarily mean that your overall profits will be higher. Why? Because higher markups usually result in reduced sales. This explains why discount stores are able to make healthy profits despite lower-than-average markups. Their sales volume is higher.

Pricing Methods

There are a number of pricing methods to choose from, ranging from the simple to the complex. Here are three of the most commonly used methods:

1. **Competitive Pricing.** Prices are set at or below the competition's. Costs are made to conform to the prices that have been set.
2. **Standard Markup Pricing.** A standard markup is computed and then added to the cost of the goods or services sold. Some businesses apply a single markup across the board, while others have different markups for each sales category.
3. **Cost-Oriented Pricing.** Prices are set individually, based on the cost of the goods or services sold, the overhead, and the desired profit.

Of the three methods, cost-oriented pricing is the most accurate but also the most complex and time-consuming because each product or service is evaluated separately. A standard markup saves time by eliminating the need to do individual computations. For a store that carries hundreds or thousands of merchandise items, this can make a big difference. Competitive pricing is the simplest method of all. Prices are virtually preset, being based on what's acceptable for your industry.

Common sense and a little experimentation will soon tell you which method or combination of methods works best for you. If you're in a highly competitive industry where the key determinant of sales is the price, you'll have little choice but to use the competitive pricing method. For businesses with extensive inventories, time considerations alone will dictate that some sort of standardized markup be used. The cost-oriented pricing method is normally used by businesses offering one-of-a-kind products or specialized services.

Staffing

The most valuable asset of any business is its people. Land, buildings, merchandise, and equipment may dominate a balance sheet, but they don't make a business successful; people do. The best businesses have the best people—capable, creative, energetic people. To attract these people, you need both ingenuity and initiative, but the payoff in productivity is worth it. Staffing your business with the best people available should be one of your highest priorities.

The steps you must take before you hire anyone are to:

- Analyze each job
- Prepare job descriptions

- Check recruitment sources
- Use application forms
- Conduct interviews
- Verify information.

After the hiring decision is made, you have to;

1. Provide job orientation
2. Provide training
3. Evaluate performance
4. Compensate employees
5. Monitor employee turnover.

By following these steps, instead of waiting for fate to send you perfect employees or complaining about your current employees, you can control and direct the staffing process.

Running an Ethical Business

As just noted, it's important for you to consider the ethical standards by which you choose to run your business.

Some issues to address in developing your code of ethical business standards are:

a. Hiring/promotion criteria—Equal opportunity, nondiscriminatory, merit-based.
b. Treatment of workers—Safe environment, harassment-free, concern for individuals.
c. Worker responsibilities—Perform assigned tasks, use time well, show ingenuity.
d. Business property use—Safeguard property, use for business purposes.
e. Conflicts of interest—Follow policy on gifts, gratuities, contracts, and hiring.
f. Treatment of customers—Provide quality work and products, fair prices.
g. Customer relations—Respond to customers' needs, respect privacy.
h. Vendor relations—Negotiate contracts in good faith, honor commitments.
i. Competitor relations—Uphold industry standards and compete fairly.
j. Social responsibilities—Obey laws, contribute to society, protect the environment.

Developing Your Promotional Strategy

A promotional strategy is a game plan for reaching your target

Market - the people most likely to use your product or service. At the simplest, themost direct level, your promotional strategy might consist of relying on a sign in front of your door and the word-of-mouth comments of your present customers. In some instances, if you're in a very small town, or if you offer unique products or services, or if you have a long-standing reputation, this tactic is sufficient. Normally, though, customers need more to go on before they are drawn to your business.

The goal of your promotional strategy should be to reach the greatest number of potential customers through the most economical use of your resources (money, personnel, and facilities). This entails using advertising and publicity to tune in to those channels of communication most widely used by your target customers. It also involves working within the limits of a budget to achieve the desired results.

Advertising

The advertising media generally favored are newspapers, magazines, radio, television, direct mail, Yellow Pages, outdoor advertising, and the Internet. Other media include transit, specialty, movie theaters, flyers, e-mail messages, and faxes. Each medium has its own unique characteristics and is capable of reaching large numbers of people.

Depending on your message, target customers, budget, and lead time, some will be better suited to your needs than others.

First of all, is your message simple and direct, or is it more complicated, involving a detailed explanation (a listing of the nutrients in your special health-food drink)? Does your message rely heavily on words, color, sound, or movement to make its point?

Second, is your target customer everyone (the mass market) or just a small segment of the market? The narrower your target, the greater the need to use selective media to reach it. Doctors, for instance, can be reached more effectively by means of a medical journal than a daytime soap opera.

Third, consider your budget. How much money can you spend?

Despite the suitability of a particular medium, if you can't afford it, there's no sense in building your promotional strategy around it.

Finally, what is your lead time? Do you want the advertisement to start this week, next month, or next year? Lead times vary with the medium, and if you need a quick start, that limits your selection.

The Internet

Internet Marketing Tips: Ten Things to Avoid:

1. Having poorly designed, boring Web pages.
2. Having too little user interaction.
3. Having slow pages that keep viewers waiting.
4. Including dated or incorrect information on your site.
5. Promising more than you can deliver.
6. Listing your business on inappropriate sites.
7. Failing to link your site to other sites.
8. Failing to use key search words that make it easy to find your site.
9. Failing to check the site regularly and respond to customers.

10. Failing to relate the site to your overall marketing program.

Other Advertising Media

Some of the other forms of advertising you may wish to consider are:

- **Business Cards.** Make contact with printed cards or use CD-ROM cards that provide multimedia presentations and website links.
- **Transit Advertising.** Display messages on the exteriors and interiors of trains, buses, and taxicabs.
- **Specialty Advertising.** Imprint your company's name or logo on such items as calendars, memo pads, pens, key chains, and T-shirts.
- **Flyers.** Hand them out to passersby or place on car windshields.
- **Theater-**Screen Advertising. Show ads during intermissions.
- **E-mail Messages and Faxes.** Send these to your prospects. But, make sure to get their permission first. Unsolicited e-mails ("spam") and faxes ("junk faxes") can cause negative feedback.

Preparing an Advertising Budget

In preparing their advertising budgets, the majority of businesses base their allocations on a percentage of annual past sales, estimated sales, or a combination of these. For example, 4 percent of £300,000 in sales equals an advertising budget of £12,000. Some of the reasons for this method's general acceptance are that it gives you more to go on than guesswork, it emphasizes the relationship between advertising and sales, and it's easy to use.

In determining the percentage of sales you want to invest in advertising, you should consider your business's needs, the competition, and the economic environment.

Further Reading:

- ✓ ***Start Your Own Business 2019: How to Plan, Fund and Run a Successful Business (Startups) by Ian Whiteling***
- ✓ ***Bright Marketing for Small Business (Start-ups Series) by Robert Craven***

