

Finance

Strategies for Success

Startup Management (IPIRI 63749B), Aleš Špetič, 2023

Learning Objectives

Empowering Entrepreneurs with Financial Literacy

- **Strategic Link Between Finance and Business:** Explore how finance serves as a strategic driver for decision-making and business growth.
- **Key Financial Concepts:** Income statements, balance sheets, and cash flow projections.
- **Financial Planning and Forecasting Techniques:** Develop skills in creating comprehensive financial plans and accurate forecasts to guide decision-making.
- **Financial Management and Control Strategies:** Explore budgeting, expense control, and key financial metrics for effective financial management.

Introduction

Importance of Finance in Startup Management

- **Why Finance Matters in Startups?**

- Finance is the lifeblood: It fuels operations, growth, and innovation.
- Strategic decision-making: Finance guides critical choices for sustainable development.

- **Key Aspects of Financial Importance**

- Resource Allocation: Finance ensures optimal use of limited resources.
- Risk Mitigation: Financial planning helps identify and manage risks effectively.
- Strategic Growth: Finance is the backbone of expansion and market penetration.

- **Financial Visibility**

- Investor Confidence: A robust financial plan attracts investors and stakeholders.
- Adaptability: Financial insights enable quick adjustments to market changes.
- Sustainability: Financial health is crucial for long-term viability.

Navigating the Financial Landscape

Components of Financial Management in Startups

- **Financial Statements**

- Income Statements: Revealing profitability over a specific period.
- Balance Sheets: Providing a snapshot of assets, liabilities, and equity.
- Cash Flow Projections: Anticipating future cash movements.

- **Financial Planning and Forecasting**

- Comprehensive Financial Plans: Mapping out financial goals and strategies.
- Accurate Forecasts: Guiding decision-making with reliable projections.

- **Financial Management Strategies**

- Budgeting: Allocating resources effectively.
- Expense Control: Monitoring and managing costs.
- Key Financial Metrics: Metrics for evaluating and optimizing performance.

Business Performance Recording

Differences to Out of Pocket Economy

- **Cash accounting** records the transactions when cash exchanges hands.
- **Accrual transactions** are recorded as they happen.
- **Investments and amortisation/depreciation:** learn how businesses measures investments and expenses.
- **Variable vs. fixed costs:**
 - variable cost are vary proportionally to units of sales or production
 - fixed costs are always there

Financial life of a Business

Starting a company - Student Mulled Wine Stand



We want to start a business, but we don't have any money to start it with. So we need investors:

- We create a **corporation** - a legal entity separate from the individuals that run or own it.

	Shares	Funds	
Founders	1000	0	66.6%
Investors	500	500 €	33.3%

Financial life of a Business

Initial funding



The investors bought shares for 1€ and the business has 1500 shares, so the business is now worth 1500 €.

We need more money for the **working capital**, so we borrow 250 € @10%.

	Shares	Funds		
Founders	1000	0	66.6%	
Investors	500	500 €	33.3%	
Bank	0	250 €		

Financial life of a Business

Initial Balance Sheet - Statement of Current Affairs



	Start
Assets	1750 €
.. cash	750 €
.. fixed assets	0
.. inventory	0
.. goodwill	1000 €
Liabilities	1750 €
..debt	250 €
Shareholders Equity	1500 €

Financial life of a Business

Buying things to work with



stand

wine, spices,
sugar, water, cups

	Start
Assets	1750 €
.. cash	250 €
.. fixed assets	300 €
.. inventory	200 €
.. goodwill	1000 €
Liabilities	1750 €
..debt	250 €
Shareholders Equity	1500 €

Financial life of a Business

Buying things to work with



		Comments
Sales	800 €	800 cups / 1€
Costs	-790 €	
.. Cost of Goods Sold	-200 €	
.. Depreciation	-60 €	
.. Labor	-530 €	total labor cost
Earnings Before Interest and Taxes (EBIT)	10 €	
	1.3%	margin
Interest	-25 €	10% interest on the loan
Pretax Earnings	-15 €	LOSS!!!!
Tax	0	

“Profit”

No Profit,
No Taxes

Financial life of a Business

Buying things to work with - Income Statement



“Profit”

An accounting way of measuring for wear and tear of equipment.

No Profit,
No Taxes

		Comments
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Costs		
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Financial life of a Business

Scaling the business



We plan to expand (more stands, more sales per stand, increase of prices 5% per event).

	Year 1	Year 2	Year 3	Year 4	Year 5
#of stands	1	2	3	4	7
Cups per stand	800	840	882	926	972
Cups Sold	800	1680	2646	3704	6804
Price charged	1 €	1,05 €	1,10 €	1,15 €	1,20 €
Sales	800 €	1764 €	2911 €	4260 €	8165 €

Financial life of a Business

Growth!



	Year 1	Year 2	Year 3	Year 4	Year 5
#of stands	1	2	3	4	7
Cups per stand	800	840	882	926	972
Cups Sold	800	1680	2646	3704	6804
Price charged	1 €	1,05 €	1,10 €	1,15 €	1,20 €
Sales	800 €	1764 €	2911 €	4260 €	8165 €
Costs	-790 €	-1600 €	-2432 €	-3280 €	-5832 €
.. Cost of Goods Sold	-200 €	-420 €	-662 €	-920 €	-1702 €
.. Depreciation	-60 €	-120 €	-180 €	-240 €	-420 €
.. Labor	-530 €	-1060 €	-1590 €	-2120 €	-3710 €
Earnings Before Interest	10 €	164 €	479 €	980 €	2333 €
margin	1,3%	9,3%	16,4%	23,0%	28,6%
Interest	-25 €	-25 €	-25 €	-25 €	-25 €
Pretax Earnings	-15 €	139 €	454 €	955 €	2308 €
Tax	0	-35 €	-113 €	-239 €	-577 €
Net Income (PROFIT)	-15 €	104 €	340 €	716 €	1731 €
per share	-0,01 €	0,07 €	0,23 €	0,48 €	1,15 €

25%

Financial life of a Business

Cash flow!

Additional Stands

	Year 1	Year 2	Year 3	Year 4	Year 5
CF Operations	45 €	224 €	520 €	956 €	2151 €
.. net Income	-15 €	104 €	340 €	716 €	1731 €
.. depreciation	60 €	120 €	180 €	240 €	420 €
CF from Investments	-300 €	-300 €	-300 €	-300 €	-900 €
.. capital expenditures	-300 €	-300 €	-300 €	-300 €	-900 €
CF from Financing	750 €				
.. debt	250 €				
.. equity	500 €				
Beginning Cash	0	495 €	419 €	639 €	1295 €
Change in Cash	495 €	-76 €	220 €	656 €	1251 €
Ending Cash	495 €	419 €	639 €	1295 €	2546 €



Financial life of a Business

State of affairs over the years - Balance Sheet



	Start	Year 1	Year 2	Year 3	Year 4	Year 5
Assets	1.750 €	1.735 €	1.839 €	2.179 €	2.895 €	4.626 €
.. cash	250 €	495 €	419 €	639 €	1.295 €	2.546 €
.. fixed assets	300 €	240 €	420 €	540 €	600 €	1.080 €
.. inventory	200 €	0 €	0 €	0 €	0 €	0 €
.. goodwill	1.000 €	1.000 €	1.000 €	1.000 €	1.000 €	1.000 €
Liabilities	1.750 €	1.735 €	1.839 €	2.179 €	2.895 €	4.626 €
.. debt	250 €	250 €	250 €	250 €	250 €	250 €
Shareholders Equity	1.500 €	1.485 €	1.589 €	1.929 €	2.645 €	4.376 €
.. earnings		-15 €	104 €	340 €	716 €	1.731 €

Financial life of a Business

Comparing the risks



	Start	Yield Y1	Yield Y2	Yield Y3	Yield Y4	Yield Y5	Risk
Debt	-250 €	25 €	25 €	25 €	25 €	25 €	low
Equity	-500 €	-5 €	35 €	101 €	239 €	577 €	high

Financial Planning

Introduction

- **Revenue Projections:** Forecasting income from sales and other revenue streams.
- **Expenses Planning:** Detailing anticipated costs across various categories.
- **Cash Flow Analysis:** Ensuring adequate liquidity to cover operational needs

Strategic Financial Planning Techniques

Going Beyond the Basics

- Rolling Forecasts
 - Periodic and regular planning for a number of periods
- Scenario Planning
 - Anticipate various business outcomes.

Rolling Forecasting

A Self Improving Framework

	I	II	III	IV	V	VI	VII
I	5	6	7				
II	4	5	8	9			
III		4	5	7	8		
IV			5	6	7	9	
V				7	6	8	10

Revenue Projections

Forecasting Sales

- **Analyse Past Performance:** Use historical data to establish a baseline.
- **Assess Market Conditions:** Consider economic trends, seasonality, and market growth.
- **Segment Revenue Streams:** Break down projections by product, service, or customer segment.
- **Incorporate New Initiatives:** Factor in new products, marketing campaigns, or market expansions.
- **Apply Sensitivity Analysis:** Create optimistic, pessimistic, and realistic scenarios.

Revenue Projections

Pessimistic Scenario



- Reflects slower growth in stands and modest price increases.
- Total Revenue Growth (Years 6-10): ~8-12% annually.
- Focus shifts to cost control to maintain profitability.

	Year 6	Year 7	Year 8	Year 9	Year 10
# of Stands	8	9	10	11	12
Cups/Stand	1.020 €	1.030 €	1.050 €	1.060 €	1.070 €
Price/Cup	1,25 €	1,30 €	1,35 €	1,40 €	1,45 €
Total Cups Sold	8.160 €	9.270 €	10.500 €	11.660 €	12.840 €
Total Revenue	10.200 €	12.051 €	14.175 €	16.324 €	18.618 €

Expenses Projections

Pessimistic Scenario



	Year 6	Year 7	Year 8	Year 9	Year 10
COGS	2040 €	2.421 €	2.835 €	3.262 €	3.708 €
Depreciation	420 €	450 €	480 €	510 €	540 €
Labor Costs	4.800 €	5.400 €	6.000 €	6.600 €	7.200 €
Total Expenses	7.260 €	8.271 €	9.315 €	10.372 €	11.448 €

Revenue Projections

Optimistic Scenario



- Projects aggressive expansion and robust sales growth.
- Total Revenue Growth (Years 6-10): ~25-30% annually.
- High profitability potential but requires significant reinvestment.

	Year 6	Year 7	Year 8	Year 9	Year 10
# of Stands	12	15	18	21	25
Cups/Stand	1.100 €	1.150 €	1.200 €	1.250 €	1.300 €
Price/Cup	1,40 €	1,45 €	1,50 €	1,55 €	1,60 €
Total Cups Sold	13.200 €	17.250 €	21.600 €	26.250 €	32.500 €
Total Revenue	18.480 €	25.013 €	32.400 €	40.688 €	52.000 €

Expenses Projections

Optimistic Scenario



	Year 6	Year 7	Year 8	Year 9	Year 10
COGS	3300 €	4.313 €	5.400 €	6.563 €	8.125 €
Depreciation	630 €	750 €	900 €	1050 €	1250 €
Labor Costs	7.200 €	9.000 €	10.800 €	12.600 €	15.000 €
Total Expenses	11.130 €	14.063 €	17.100 €	20.213 €	24.375 €

Revenue Projections

Optimistic Scenario



- Assumes steady expansion with moderate sales and price growth.
- Total Revenue Growth (Years 6-10): ~15-20% annually.
- Margins improve due to economies of scale.

	Year 6	Year 7	Year 8	Year 9	Year 10
# of Stands	10	12	14	16	18
Cups/Stand	1.050 €	1.100 €	1.150 €	1.200 €	1.250 €
Price/Cup	1,30 €	1,35 €	1,40 €	1,45 €	1,50 €
Total Cups Sold	10.500 €	13.200 €	16.100 €	19.200 €	22.500 €
Total Revenue	13.650 €	17.820 €	22.540 €	27.840 €	33.750 €

Expenses Projections

Realistic Scenario



	Year 6	Year 7	Year 8	Year 9	Year 10
COGS	2625 €	3.300 €	4.025 €	4.800 €	5.625 €
Depreciation	525 €	630 €	735 €	840 €	945 €
Labor Costs	6.000 €	7.200 €	8.400 €	9.600 €	10.800 €
Total Expenses	9.150 €	11.130 €	13.160 €	15.240 €	17.370 €

Analysis

Analysing Scenarios



	Year 6	Year 7	Year 8	Year 9	Year 10	Average Margin (%)
Pessimistic	2.940 €	3.780 €	4.860 €	5.952 €	7.170 €	33,9%
Realistic	4.500 €	6.690 €	9.380 €	12.600 €	16.380 €	41,2%
Optimistic	7.350 €	10.950 €	15.300 €	20.475 €	27.625 €	46,8%

Benefits of Effective Financial Planning

Why plan?

- Improved Decision-Making
 - Financial planning provides a basis for informed decision-making.
 - Benefit from strategic financial decisions.
- Financial planning helps allocate resources efficiently.
- Impact on profitability and sustainability.

Budgeting as Strategic Tool

Mastering the Budgeting

- What is Budgeting?
 - Budgeting is more than a financial plan—it's a strategic tool.
 - Align spending with strategic objectives - allocate resources.
- Budgeting Process
 - Gather information and analyse major revenue and expense streams item by item

Budget Sample



Category	Year 6	Year 7	Year 8	Year 9	Year 10
Revenue	13.650 €	17.820 €	22.540 €	27.840 €	33.750 €
Cost of Goods Sold (COGS)	2.625 €	3.300 €	4.025 €	4.800 €	5.625 €
Gross Profit	11.025 €	14.520 €	18.515 €	23.040 €	28.125 €
Labor Costs	6.000 €	7.200 €	8.400 €	9.600 €	10.800 €
Depreciation	500 €	600 €	700 €	800 €	900 €
Marketing & Other Costs	1.000 €	1.250 €	1.500 €	1.750 €	2.000 €
Professional Services	1.000 €	1.200 €	1.400 €	1.600 €	1.800 €
Premises Costs	1.500 €	1.800 €	2.100 €	2.400 €	2.700 €
Software Costs	300 €	350 €	400 €	450 €	500 €
R&D Costs	500 €	600 €	700 €	800 €	1.000 €
Operating Costs	13.425 €	16.300 €	19.225 €	21.900 €	25.325 €
Operating Profit	225 €	1.520 €	3.315 €	5.940 €	8.425 €

Effective Expense Control

Controlling what's Controllable

- **Regular Monitoring:** Establish a system for consistently monitoring expenses.
- **Budget Alignment:** Ensure that expenses align with the budget and strategic objectives.
- **Prioritizations:** Not all expenses are equal. Prioritize spending based on the impact each expense has on the core business functions and objectives.
- **Technology Integration:** Leverage technology to streamline expense tracking and management processes.

Analysis of the Forecast

Finding Problems

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
Revenue	800 €	1.764 €	2.911 €	4.260 €	8.165 €	13.650 €	17.820 €	22.540 €	27.840 €	33.750 €
EBIT	10 €	164 €	479 €	980 €	2.333 €	725 €	2.020 €	4.420 €	7.920 €	11.234 €
Tax (25%)	0 €	41 €	120 €	239 €	583 €	181 €	505 €	1.105 €	1.980 €	2.808 €
Net Profit	-15 €	104 €	340 €	716 €	1.731 €	225 €	1.520 €	3.315 €	5.940 €	8.425 €
Ending Equity	1.485 €	1.589 €	1.929 €	2.645 €	4.376 €	4.601 €	6.121 €	9.436 €	15.376 €	23.801 €
Share Value	0,99 €	1,09 €	1,29 €	1,76 €	2,93 €	3,07 €	4,08 €	6,29 €	10,25 €	15,87 €

Budget Sample



Category	Year 6	Year 7	Year 8	Year 9	Year 10
Revenue	13.650 €	17.820 €	22.540 €	27.840 €	33.750 €
Cost of Goods Sold (COGS)	2.625 €	3.300 €	4.025 €	4.800 €	5.625 €
Gross Profit	11.025 €	14.520 €	18.515 €	23.040 €	28.125 €
Labor Costs	6.000 €	7.200 €	8.400 €	9.600 €	10.800 €
Depreciation	500 €	600 €	700 €	800 €	900 €
Marketing & Other Costs	1.000 €	1.250 €	1.500 €	1.750 €	2.000 €
Professional Services	1.000 €	1.200 €	1.400 €	1.600 €	1.800 €
Premises Costs	1.500 €	1.800 €	2.100 €	2.400 €	2.700 €
Software Costs	300 €	350 €	400 €	450 €	500 €
R&D Costs	500 €	600 €	700 €	800 €	1.000 €
Operating Costs	13.425 €	16.300 €	19.225 €	21.900 €	25.325 €
Operating Profit	225 €	1.520 €	3.315 €	5.940 €	8.425 €

Key Financial Metrics

Evaluating Success with Metrics

- **Return on Investment (ROI)**

- ROI measures the profitability of an investment.
- A percentage of income relative to the investment.

- **Gross Margin**

- Percentage of revenue that exceeds the COGS.
- It helps to assess the efficiency of production and pricing.

- **Burn Rate / Runway**

- Burn rate as the rate at which a startup uses up its capital.
- Runway is the number of months that startup still has before using up the capital.

Conclusion

Finance

- **Mastering Key Financial Concepts:** Income statements, balance sheets, and cash flow projections are fundamental tools.
- **Financial Planning and Forecasting Techniques:** Accurate forecasting guides strategic decision-making.
- **Explore budgeting, expense control:** Effectively managing finances ensures stability and growth.
- **Expense Management and Optimization:** Differentiate between variable and fixed costs.
- **Key Financial Metrics for Evaluation:** ROI, Gross Margin, and Burn Rate provide actionable insights.

Assignment

Create financial plan

- Forecast the business for 12 months ahead (CF based).
- Use worse case and expected scenario.
- Calculate financial needs for the business

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