

PERSONAL FINANCE
and
Small Business Ownership

PRESENTED BY

STEVE COPLON

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Introduction

The purpose of this seminar on Personal Finance and Small Business Ownership is to give returning citizens a better chance of success by helping them to change the way they think about their personal finances, so that they become more aware of how money works in their lives, so that they will plan ahead making right decisions, reducing the amount of stress in their lives and not reverting back to old ways of thinking that got them in trouble in the first place.

The importance of having enough money and knowing what that amount of money is to support one's lifestyle is one of the main themes of this seminar. Whether one's income is derived from being self employed or from working as an employee for a company other than your own, the income that flows into the personal budget works the same way.

It is my sincere hope that this seminar helps each participant to a better life with less financial stress. For those that go into small business ownership, I hope that the approach to managing your own business offered in this seminar helps you reach great levels of success.

Good luck in managing your personal budget!



The Flame is Extinguished



The Flame is Extinguished

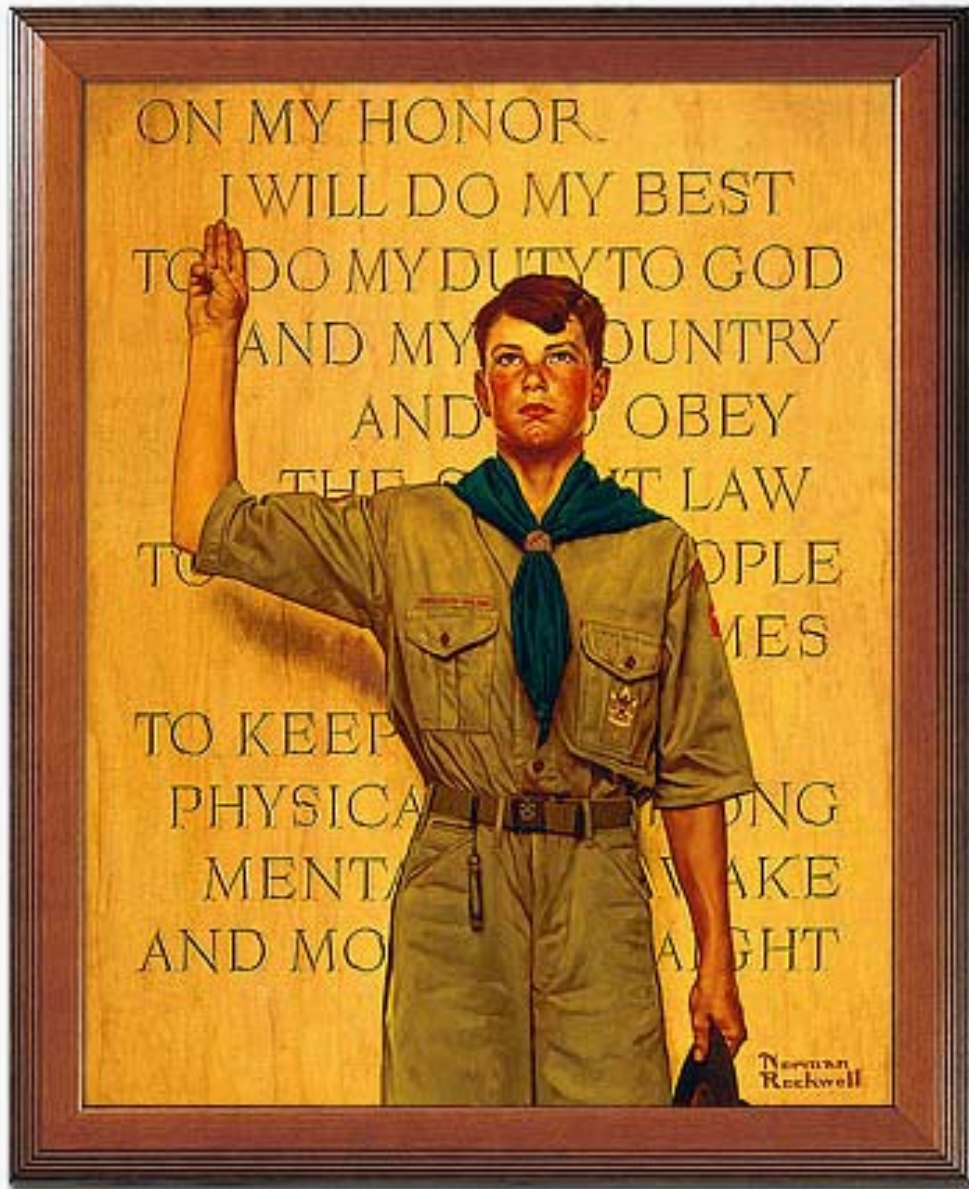


Managing Your Business is Like Swiss Cheese



It can be full of holes

Going into business for yourself is a very serious undertaking. If it does not succeed you could lose everything.



If you are going
into business
you better

**BE
PREPARED**

OVERVIEW

To present a management tool that can help manage your business to success, by better understanding the **relationship of the variables** that work together within your business.

PURPOSE OF TODAY'S PRESENTATION

To identify at least one area of your business that you realize you need to know more about, which by having a better understanding would make your business more successful.

- **Basic Approach to Business – The personal side and the business side of a small business owner’s life is tied closely together.**
- **The goal of the business should be to provide the vehicle to satisfy the owner’s personal goals.**

- Business must create enough income to owner to meet personal budget requirements.
- The main goal of the business is to fund the owner's lifestyle.

- During start-up phase of business or ramp-up phase when business is operating at negative cash flow, working capital of business is used for cash out needs.
- If business doesn't reach stabilization before working capital runs out, additional funding is necessary to keep business in operation. This additional funding usually comes from additional capitalization or loans.

- In most cases, the business has various loans for property, plant and equipment. There could be additional loans for working capital and inventory as well.
- The business may or may not be able to obtain additional credit from its bank to borrow the additional funds it seeks.

- If it cannot obtain approval from the bank for additional credit, the owner is forced to use personal resources to fund the business.
- As these resources diminish, the credit worthiness of the owner lessens.

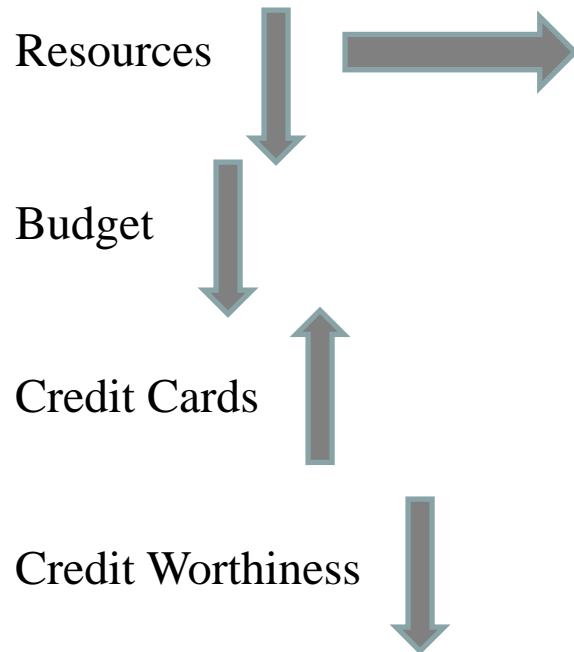
- If the Business does not stabilize the owner may resort to using personal credit to fund the business.
- Credit card debt mounts quickly.

- As the credit card debt mounts and personal resources are diminishing the personal budget requirement becomes more and more difficult to meet.
- Bills start to get paid later and later.
- Before long, personal credit suffers and the ability to obtain any financing for the business becomes very difficult, since in small businesses the owner normally most personally guarantee all bank loans.

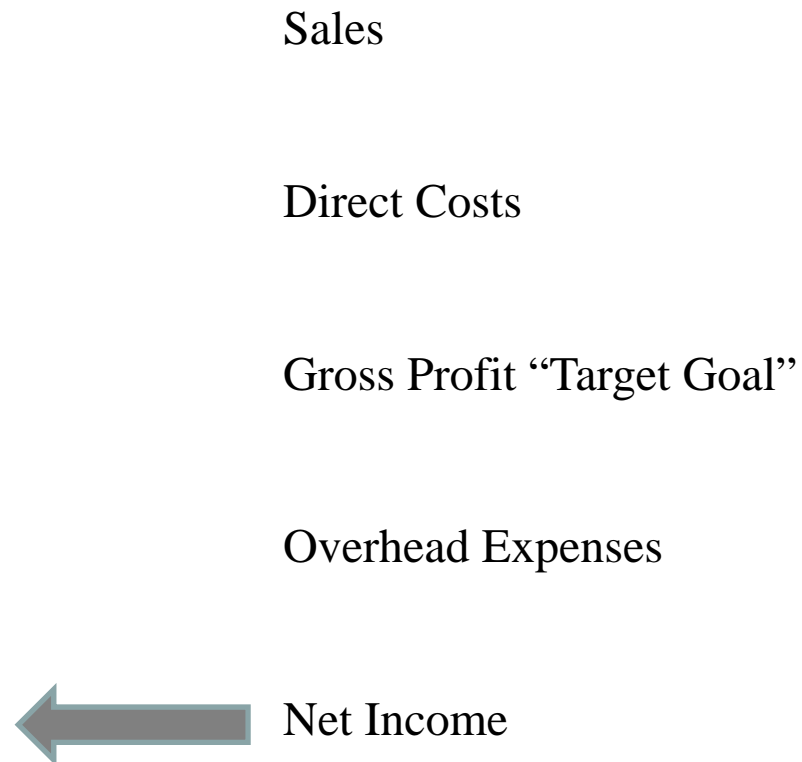
- Once the owner's resources and credit are gone, if the business is not operating with positive cash flow and unless there is some other major source of income, the business will fail.

The Personal and Business Relationship

Personal



Business



- What is the answer to avoiding this dangerous path to failure?

The following approach will give the business owner the **best** chance at success:

1. Prepare a complete business plan **BEFORE** starting your business
2. Know the personal budget needs that the business most fund
3. Properly capitalize your business
4. Protect your personal resources
5. Avoid credit card debt
6. Keep your personal credit intact

The Key to Personal Finance

- Knowing how much money that is in your pocket is really yours and how much belongs to someone else.

The Secret to Personal Finance

The secret to personal finance is knowing how much money that is in your pocket is really yours and knowing how much is already obligated to someone else.

This guy gets out of prison, and he never liked to use banks before he was in because he couldn't keep his account reconciled. He was always bouncing checks, had service charges, and he never knew how much money he had. He was a cash in the pocket kind of guy. He has a construction job, because he can't get a much better job, because he's been in prison and people don't want to hire him.

He doesn't have a bank account of his own, so on Friday afternoon he goes to his employers bank with mud on his construction boots to cash his \$175 paycheck. The bank charges a \$7 service charge to cash his check. That's a sin right there. Banks never used to charge an employee to cash a check drawn off of the employer's bank account. That's what they are doing now. It's a really rough economy out there.

So he cashes his check and he has \$168 in his pocket. It is burning a hole in his pocket. He get's out of the bank, goes to the 7-Eleven next to the bank, buys a six pack of beer, smokes, baseball cap and by Sunday night he's spent another \$35 or \$40 and he has \$120 left of his \$175.

Monday morning when he gets up, he's got \$120. What I did not tell you is that he has a \$145 cutoff notice with VEPCO. He has not paid his electric bill for two months, and they are going to cut off his electricity unless he pays the \$145. He was going to go on his lunch hour to pay the bill. This guy is really inconveniencing his family having the power cut off. Even if he does not have a family, he is digging himself a deeper hole. He will have to pay a reconnect fee, making the situation even worse.

So where is this guy going to get the \$25 that he needs to pay his VEPCO bill, to keep his lights on? **WRONG ANSWER! THAT IS WHAT GOT YOU HERE IN THE FIRST PLACE!**

What he should have done on Friday afternoon when he was at the bank was ask the teller for an extra envelope, written VEPCO on the outside and put \$145 in the envelope then put it in his other pocket so that he would have the money to take to VEPCO on Monday.

You need to plan ahead. You can't just go day by day. You can avoid pressures by thinking and planning ahead. The secret to personal finance is knowing how much money that is in your pocket is really yours and knowing how much is already obligated to someone else.

What must the business itself do to operate successfully so that it may fund the owner's goals?

- There is a very simple formula that if followed will guarantee that the owner will reach the desired level of success.

1. Identify personal needs. This represents **Net Profit**.
2. Budget all necessary **Overhead** required to operate business.
3. Add Budgeted Overhead to Desired Net Profit. This total is the **Gross Profit**. It is also referred to as the **Target Goal**. On a cash basis it is the Cash Flow Generated from Operations to Cover Overhead and Profit.
4. Determine the **Direct Cost Percentage** that you can realistically achieve in your business.
5. Calculate the **Sales** that the business must do at the Direct Cost Percentage to produce the targeted Gross Profit.

Manage From the Bottom Up

From Desired Profit to Required Sales

Example

- Desired Net Profit \$ 50,000
- Budgeted Overhead \$ 50,000
- Gross Profit or Target Goal \$100,000
- Direct Cost Percentage 50%
- Direct Cost \$100,000
- Targeted Sales \$200,000

GUARANTEED SUCCESS!

- If the business stays within its Overhead budget
- Does not exceed its Direct Cost Percentage
- And reaches the Targeted Sales Amount,
- Then it is **guaranteed** to meet the bottom line Net Profit Goal desired.

You must manage
ultimately
to a

Gross Profit Dollar Amount.

FAILURE!!

- Many small business owners have been asked at the proverbial cocktail party
“How is your business doing?”
- They have answered
“Great! In a couple of months we will probably be able to take a paycheck.”
- This is a business that is **failing**. No one ever succeeded simply operating at the breakeven point.
- Their personal resources are being diminished daily.

In a normal consulting engagement,
time would be allotted as follows:

1. Determining Owners Needs	5%
2. Identifying and Budgeting Overhead	10%
3. Establishing Direct Cost Percentage	10%
4. Reaching Sales Goals	75%
TOTAL TIME	100%

What is involved in each area?

- **Determining Owners Needs**
Owner must have good handle on personal budget.

Must know how much the business must provide to finance personal lifestyle. In many cases, return to investors and debt payments are added here.

- **Identifying and Budgeting Overhead**
Overhead is defined as that which the business incurs before any units are manufactured or produced. It includes all items that must be paid whether any sales are made or not made. It does not include any direct costs of production or any marketing or advertising expenses. These two expenses will be added in later. Overhead must be kept at minimum levels or Profits will be sacrificed.

- **Establishing Direct Cost Percentage**
This is the area where it is necessary to know Industry averages for your business. Labor efficiencies and purchasing procedures are closely studied. The actual processes of your business are examined.

- Reaching Sales Goals

This is the area where the most management time must be spent.

In-depth understanding of the market, competition and pricing are critical.

MANAGING TO YOUR GROSS PROFIT

- If the financial modeling has been done to target the Gross Profit amount that will cover Overhead Expenses and send the desired Net Profit to the bottom line, as long as that targeted amount is achieved, then success is guaranteed.

SALES ARE CRITICAL BUT NOT THE ONLY THING THAT COUNTS

Many businesses have achieved Sales goals but lost money.

Possible reasons for this are:

- Direct Costs are over the budgeted percentage
- Overhead Expenses are over budget
- Sales are in wrong profit center

Example of Not Knowing Your Costs

There is this little second grade girl who wants a \$50 Barbie doll. So she asks her parents “Mommy, Daddy will you buy me the Barbie doll?”

They can’t afford to buy the \$50 doll, it’s not Christmas or her birthday. They don’t have any extra money, They just can’t do it. Times are tight. There is a PTA bake sale coming up at her school so they say to her “Why don’t we sell cakes at the PTA bake sale and if we make \$50 we will buy you the Barbie doll.”

So they get a table in the hallway at the PTA bake sale and sell cakes. Their cost for each cake is \$6. They sell each cake for \$10. So they are going to make \$4 each time they sell a cake. They need to sell 12 ½ cakes to make the \$50 that they need but since they aren’t selling half cakes they need to sell 13 cakes to make enough money to buy the Barbie doll.

As soon as the little girl sells 5 cakes and has 5 ten dollar bills in her hand she starts jumping up and down happy saying “Oh goodie, goodie Mommy and Daddy. We can buy the Barbie doll now!”

She doesn’t have a clue about the costs. All she knows is that she has the \$50 that they need.

There are many, many businesses that operate just like that little girl. They don’t have a clue about their costs. All they think about are their sales.

If projected Sales are not enough to create the targeted Gross Profit, using the most realistic Direct Cost Percentage, what do you do?

- Re-examine Overhead and try to cut overhead expenses
- Re-examine Direct Costs and try to tighten up to lower costs percentage
- Decide what Marketing and Advertising expenses are necessary to increase sales to the necessary level.

Marketing and Advertising

- This last step is referred to as “**the Wild Card**”. It is an unknown that has much risk. **Marketing and Advertising expenditures are a form of an investment.** If the expenditures don't produce the desired results, the situation becomes worse.

The basic formula is modified by adding the Marketing and Advertising Expenses to the Overhead Expenses and Net Profit to establish the targeted Gross Profit Goal.

- Sales
- Direct Costs
- Gross Profit
- Marketing and Advertising Expenses
- Subtotal
- Overhead Expenses
- Net Profit

After all the goals have been set, it is imperative to monitor and track results closely.

- This will enable management to then do its job: keep the business on course toward success.
- Managing your business should be **Proactive**, not Reactive or Passive.
- Knowing your goals and managing to them requires constantly **staying focused** and **sticking to the plan**.

Terminology

- **Traditional Breakeven Point** – When you do enough Sales to cover all of your Direct Costs and Overhead Expenses and make a ZERO profit.
- **Breakeven Requirement** – The targeted Gross Profit that will cover Overhead Expenses and the Desired Net Profit.
- **Operating at a Loss** – When Sales are not enough to cover Direct Costs and Overhead Expenses
- **Working Capital** – Available funds used to meet current cash needs of a business

A business must have enough Cash to meet its obligations.

Some of the main obligations requiring cash are:

1. Payrolls
2. Payroll Taxes
3. Vendor Payments
4. Rents, Utilities, Telephone
5. Note Payments

The Most Important Thing
to Manage in Business

Cash Flow

You Need it to be Positive!

Sources of Cash

A business gets Cash from several sources.

Some of the primary sources are:

1. Sales Revenues
2. Accounts Receivable Collections
3. Lines of Credit
4. Loans
5. Capital Infusion

Cash Flow

- Cash Flow – The actual way that cash moves in and out of a business
- Cash Flow Problems – The difficult times when there is not enough money to cover obligations (or bills)
- Negative Cash Flow – When Cash In is not enough to cover Cash Out
- Solutions to Cash Flow Problems – Have enough funds in bank to cover Cash out needs

Steps in Eliminating Cash Flow Problems

- Operate at a Profit
- Use Lines of Credit
- Have Sufficient Levels of Working Capital
- Have Proper Capitalization

By projecting negative cash flow

- Working capital needs can be determined
- Amount of necessary lines of credit can be calculated in advance
- You can eliminate surprise
- You can take steps to modify your plan

Illustration of Managing to Your Gross Profit

**MANAGING TO YOUR GROSS PROFIT
ILLUSTRATION OF EFFECTIVELY MANAGING SEVERAL VARIABLES**

1st PROJECTION	<u>Retail Sales</u>		<u>Catalogue Sales</u>		<u>Restaurant Sales</u>		<u>Wholesale Sales</u>		<u>TOTAL</u>	
Sales	100,000	100.0%	200,000	100.0%	300,000	100.0%	400,000	100.0%	1,000,000	100.0%
Direct Costs										
Labor	20,000	20.0%	50,000	25.0%	90,000	30.0%	120,000	30.0%	280,000	28.0%
Materials	<u>35,000</u>	<u>35.0%</u>	<u>80,000</u>	<u>40.0%</u>	<u>90,000</u>	<u>30.0%</u>	<u>180,000</u>	<u>45.0%</u>	<u>385,000</u>	<u>38.5%</u>
Total Direct Costs	55,000	55.0%	130,000	65.0%	180,000	60.0%	300,000	75.0%	665,000	66.5%
Gross Profit	45,000	45.0%	70,000	35.0%	120,000	40.0%	100,000	25.0%	335,000	33.5%
Overhead									350,000	35.0%
Net Profit - Target \$50,000									(15,000)	-1.5%

Initial Sales projections using normal percentages for Labor and Materials will not generate targeted Net Profit

The Wildcard



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Materials	<u>42,000</u>	<u>35.0%</u>	<u>110,000</u>	<u>40.0%</u>	<u>99,000</u>	<u>30.0%</u>	<u>247,500</u>	<u>45.0%</u>	<u>498,500</u>	<u>39.1%</u>
Total Direct Costs	66,000	55.0%	178,750	65.0%	198,000	60.0%	412,500	75.0%	855,250	67.1%
Gross Profit	54,000	45.0%	96,250	35.0%	132,000	40.0%	137,500	25.0%	419,750	32.9%
Marketing/Advertising	5,000	4.2%	10,000	3.6%	5,000	1.5%	20,000	3.6%	40,000	3.1%
Subtotal	49,000	40.8%	86,250	31.4%	127,000	38.5%	117,500	21.4%	379,750	29.8%
Overhead									350,000	27.5%
Net Profit - Target \$50,000									29,750	2.3%

Carefully placed Marketing/Advertising dollars achieve positive results but Net Profit Target of \$50,000 is still not reached

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Direct Costs										
Labor	22,800	19.0%	68,750	25.0%	95,700	29.0%	168,000	30.0%	355,250	27.6%
Materials	<u>42,000</u>	<u>35.0%</u>	<u>105,875</u>	38.5%	<u>99,000</u>	<u>30.0%</u>	<u>252,000</u>	<u>45.0%</u>	<u>498,875</u>	<u>38.8%</u>
Total Direct Costs	<u>64,800</u>	54.0%	174,625	63.5%	194,700	59.0%	420,000	75.0%	854,125	66.5%
Gross Profit	55,200	46.0%	100,375	36.5%	135,300	41.0%	140,000	25.0%	430,875	33.5%
Marketing/Advertising	5,000	4.2%	10,000	3.6%	5,000	1.5%	20,000	3.6%	40,000	3.1%
Subtotal	50,200	41.8%	90,375	32.9%	130,300	39.5%	120,000	21.4%	390,875	30.4%
Overhead									340,000	26.5%
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Bold colored amounts represent changes in targets that management feels it can reach by close monitoring

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Direct Costs										
Labor	24,000	20.0%	68,750	25.0%	99,000	30.0%	165,000	30.0%	356,750	28.0%
Materials	<u>42,000</u>	<u>35.0%</u>	<u>110,000</u>	<u>40.0%</u>	<u>99,000</u>	<u>30.0%</u>	<u>247,500</u>	<u>45.0%</u>	<u>498,500</u>	<u>39.1%</u>
Total Direct Costs	66,000	55.0%	178,750	65.0%	198,000	60.0%	412,500	75.0%	855,250	67.1%
Gross Profit	54,000	45.0%	96,250	35.0%	132,000	40.0%	137,500	25.0%	419,750	32.9%
Marketing/Advertising	5,000	4.2%	10,000	3.6%	5,000	1.5%	20,000	3.6%	40,000	3.1%
Subtotal	49,000	40.8%	86,250	31.4%	127,000	38.5%	117,500	21.4%	379,750	29.8%
Overhead									350,000	27.5%
Net Profit - Target \$50,000									29,750	2.3%

Carefully placed Marketing/Advertising dollars achieve positive results but Net Profit Target of \$50,000 is still not reached

3rd PROJECTION	Retail Sales		Catalogue Sales		Restaurant Sales		Wholesale Sales		TOTAL	
Sales	120,000	100.0%	275,000	100.0%	330,000	100.0%	560,000	100.0%	1,285,000	100.0%
Direct Costs										
Labor	22,800	19.0%	68,750	25.0%	95,700	29.0%	168,000	30.0%	355,250	27.6%
Materials	<u>42,000</u>	<u>35.0%</u>	<u>105,875</u>	<u>38.5%</u>	<u>99,000</u>	<u>30.0%</u>	<u>252,000</u>	<u>45.0%</u>	<u>498,875</u>	<u>38.8%</u>
Total Direct Costs	64,800	54.0%	174,625	63.5%	194,700	59.0%	420,000	75.0%	854,125	66.5%
Gross Profit	55,200	46.0%	100,375	36.5%	135,300	41.0%	140,000	25.0%	430,875	33.5%
Marketing/Advertising	5,000	4.2%	10,000	3.6%	5,000	1.5%	20,000	3.6%	40,000	3.1%
Subtotal	50,200	41.8%	90,375	32.9%	130,300	39.5%	120,000	21.4%	390,875	30.4%
Overhead									340,000	26.5%
Net Profit - Target \$50,000									50,875	4.0%

Bold colored amounts represent changes in targets that management feels it can reach by close monitoring

**GOOD LUCK WITH YOUR
SMALL BUSINESS!!!**

