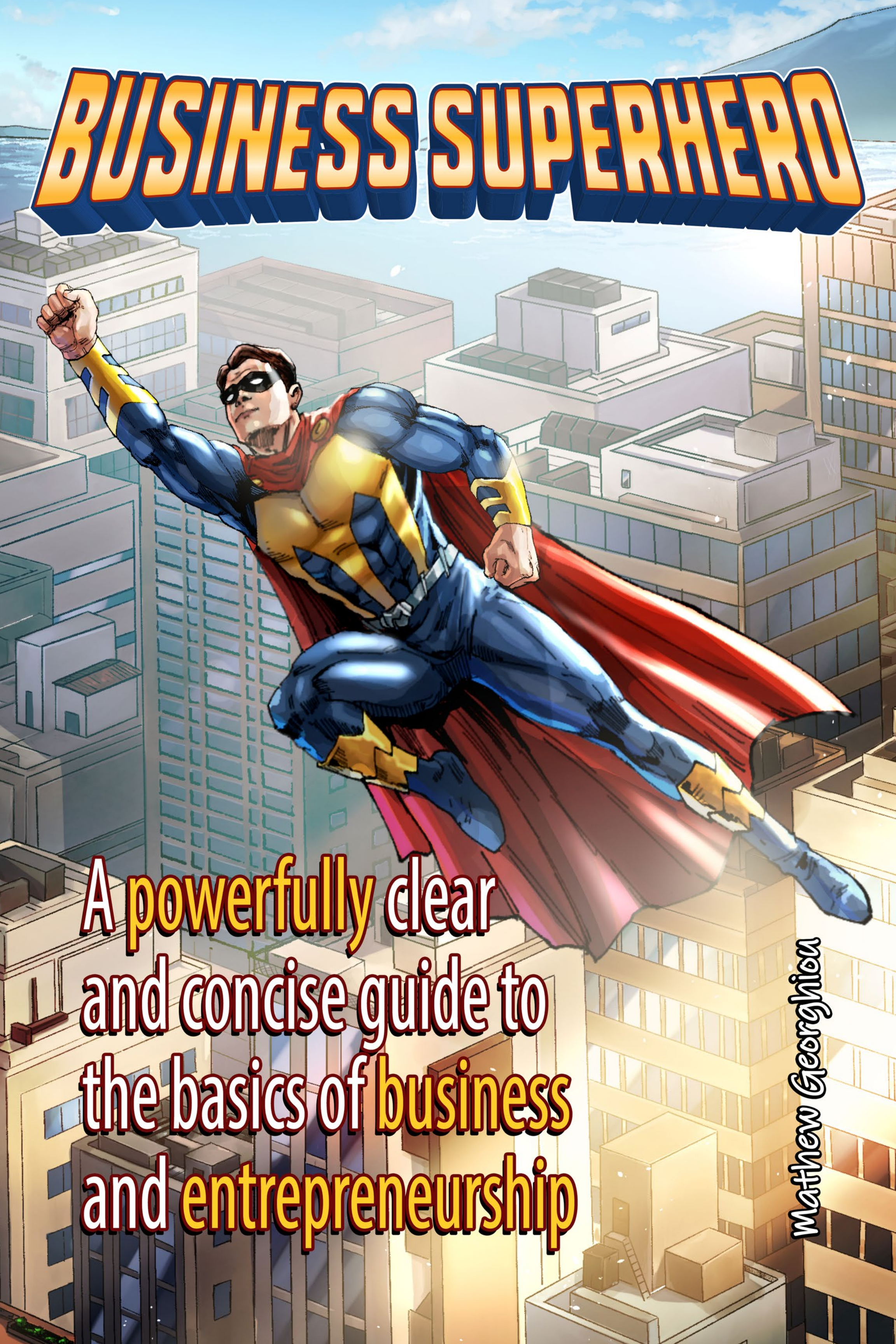

BUSINESS SUPERHERO

A powerfully clear and concise guide to the basics of business and entrepreneurship

Mathew Georghiou

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by Mathew Georghiou

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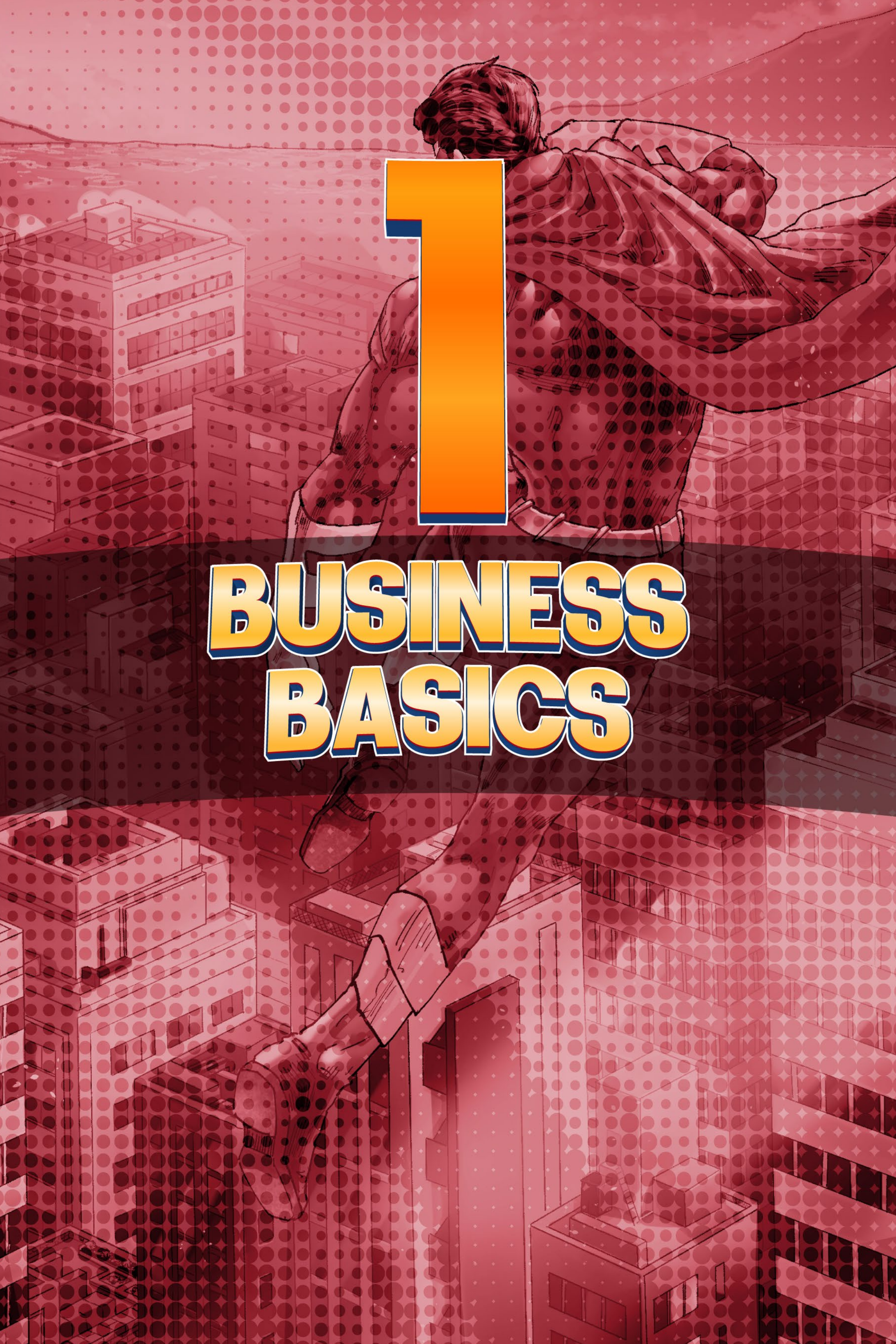
BUSINESS BASICS



Businesses and Products

A **business** is an organization that sells goods or services.

Good

A tangible item that can be used once or multiple times. Ownership of the good is normally transferred to the person who purchases it. Examples are cars, shoes, pens, and computers.

Service

An action that someone does for you. A service is intangible. Examples are car repair, haircut, teaching, legal and medical services.

The term **product** is often used to mean goods or both goods and services. In this document, it will be used to mean both goods and services.

Complete the table below.

PRODUCTS	TANGIBLE OR INTANGIBLE
GOODS	____________________
SERVICES	____________________

Some businesses make the products that they sell. Some businesses make the parts used to make other products. And, some businesses sell the finished product.

Example:

- Ford designs and makes automobiles.

- The parts that make up an automobile are made by hundreds of other businesses. These businesses are called **suppliers**, because they supply the parts. Ford assembles automobiles using these parts.
- Ford then ships the automobiles to **dealers**. The dealers sell the automobiles to people. The people who buy and use a product are called **consumers**.
- Ford dealers sell consumers both goods (the automobiles) and services (automotive repair).

Complete the table below by entering *consumers*, *suppliers*, or *dealers* in the correct cell.

SUPPLY PARTS, INGREDIENTS, RAW MATERIALS	SELL AUTOMOBILES	PURCHASE AND USE AUTOMOBILES
______________	______________	______________

Stores and Resellers

Dealers may also be called **resellers**, because they re-sell a product that was made by another business or person. Products that are commonly sold by resellers include furniture, clothing, smartphones, televisions, and groceries. Amazon and Walmart are resellers.

Not every business sells products through resellers. Some businesses sell their products directly to the consumer. This is called **direct sales**. Examples are computers, restaurants, artisans, banks, law firms, and accountants.

Some businesses use both direct sales and resellers. For example, Apple sells its products on its own website, in its own stores, and through other retail and electronics stores and telecommunication companies.

A **store** is a place where consumers can view and purchase products. The term usually refers to a physical location that you can visit, but sometimes it may refer to an online store, website, or software app.

A business can also do direct sales by selling in a print catalog, through postal mail, or with its own salespeople who call, email, or visit people.

Complete the table below by entering *reseller*, *direct sales*, or *store* in the correct cell.

PLACE WHERE CONSUMERS CAN VIEW AND PURCHASE PRODUCTS	SELLING DIRECTLY TO CONSUMERS	BUSINESS THAT SELLS PRODUCTS MADE BY OTHERS
____________________	____________________	____________________

Customers and Consumers

Consumers are individuals or organizations that purchase and use a product. Consumers are also called **customers**, but there is a difference between the two terms.

A **customer** is an individual or an organization that purchases a product. The difference between a consumer and customer is that a consumer is the person or organization that uses the product. This is also sometimes called the **end-consumer**.

A customer may or may not be the person or organization that uses a product. A consumer may be both the customer and the end-consumer, but a customer may or may not be an end-consumer.

In the Ford example, all of the many suppliers that provide parts to make the automobiles consider Ford their customer. Ford purchases their products (the automotive parts) and therefore is their customer. But, Ford does not use the parts – instead, Ford assembles automobiles and then ships them to dealers who then sell them to the end consumers. To the parts suppliers, Ford is the customer but not the consumer. The consumer is the person or organization that drives the automobile.

When Ford purchases furniture to use in the company offices, Ford is both the customer and the consumer to the furniture company.

Customers and consumers can be individual people or organizations. Organizations include companies, governments, schools, hospitals, and other groups. These are often called business or **organizational customers**, and they have different reasons for buying than individual users, and may buy in larger quantities.

Complete the table below by entering *customer*, *consumer*, or *organizational customer* in the correct cell.

USES A PRODUCT	NOT AN INDIVIDUAL CUSTOMER	BUYS A PRODUCT BUT MAY OR MAY NOT USE THE PRODUCT
________________	________________	________________

Business Creation

The creation of a business usually starts with an idea. An idea to make and/or sell goods or services. Anyone can start a business at any time.

An individual can do some activities, similar to a business, without formally registering as a business. But, certain types of activities require that a business be registered with the government.

Profit Versus Not-For-Profit

Profit means to make money. More specifically, it means to achieve financial gain – a surplus of money. With profit, this means to create more money than you started with.

Review the examples in the table on the next page and complete the final example.

MONEY IN	$100	$1,000	$500
MONEY SPENT	$70	$800	$400
PROFIT MONEY IN – MONEY SPENT	$30 = $100 - $70	$200 = $1,000 - $800	$ ________

A business can be **for-profit** or **not-for-profit**.

For-Profit
A business that is intended to create profit for its owners to use as they choose. The owners may choose to use the profit money to grow the business, start a new business, or improve their personal lifestyles or savings.

Not-For-Profit
Sometimes spelled as **nonprofit**, this is a business that is intended to support a social cause. This may include charity, medical research, local community, industry association, or other initiative.

With a nonprofit, any profit that is generated by the business must be used to further the mission of the business. Profit cannot be given to the owners of the business, because a nonprofit does not have owners. Instead, a nonprofit is managed by a person or group of people who act as members or directors. Their responsibility is to ensure that the nonprofit uses its money and resources to support its mission.

Normally, nonprofits are not called businesses, even though, technically, they may be businesses. A more commonly-used term is **nonprofit organization**.

Business, Company, and Corporation

The terms **business**, **company**, and **corporation** are often used to mean the same thing, but there are differences.

Business can broadly refer to the act of doing business – the exchange of goods and services. While this exchange does mean "doing business," it does not always mean that business is being done as a company or a corporation.

The words **business** and **company** are often used to mean the same thing, but a person doing business selling items at a local market may not consider themselves a company. A food truck may not consider the business a company.

To some, the word **company** suggests an organization that is created and structured to do business. Some definitions go further to suggest that company means the same as corporation.

Corporation is a legal term used to describe a specific form of business registration. A corporation is an entity that has been created to conduct business – for profit or nonprofit – and is effectively recognized as a person under law.

A corporation has one or more owners (called shareholders) and does not legally represent a particular person, because it is an entity of its own.

Corporations are normally required to have a specific term included in their legal names to identify their status. Examples from various countries include: Incorporated (Inc.), Corporation (Corp.), Limited(Ltd.), LLC, PLC, GmbH, AG, SARL, SA SL, AB, Oy.

All corporations are businesses, but not all businesses are corporations.

2

MANAGEMENT & ENTREPRENEURSHIP

Managing a Business

Managing a business means making the short-term and long-term decisions that are needed to operate the business and make it financially successful.

Most businesses sell goods or services – often called **products**. They may produce the product, or they may resell or distribute a product created by another organization.

Products are sold to consumers. Consumers are the people or organizations that use a product. They pay money for the product and that money goes to the business that offers and/or makes the product. To the business, this money is called **revenue** or **income**.

The objective of a business is to generate more money than it spends. This is called **profit**. You must manage the various functions of your business to achieve your desired profit.

To achieve your desired profit, you should define a strategy for your business and then make decisions that adhere to your strategy. Monitor your progress and adjust your strategy when needed.

Review the examples in the table below and complete the final example.

REVENUE FROM PRODUCT SALES	$200	$1,000	$500
MONEY SPENT TO MAKE AND SELL PRODUCTS	$150	$600	$300
PROFIT	$50 = $200 - $150	$400 = $1,000 - $600	$ ________

Entrepreneurship

An entrepreneur is a person who starts and operates a business, while assuming the risks and rewards. This is one common definition, but there are varied opinions about how broadly or narrowly this definition should be applied.

Most entrepreneurs own and run small businesses, such as a retail store, gas station, flower shop, software developer ... the possibilities are endless.

Sometimes, small businesses turn into very large businesses. Walmart, Amazon, Apple, and many other companies were all started by entrepreneurs who launched small businesses that turned into global companies.

Becoming a successful entrepreneur is not easy. You need a good idea, dedication, sometimes money, and always a great deal of hard work and effort. Some say luck may also contribute to success.

The Entrepreneur

You pursue newly discovered, fleeting opportunities. You seek freedom, financial reward, creativity, and control of your own future. You are clever and resourceful.

Your supporters depend upon you and cheer your success, often as bystanders, but sometimes with an offer of a hand up. Meanwhile, the naysayers anticipate your failure, yet you remain one step ahead.

In the distance are visions of victory and cries of defeat from fellow entrepreneurs.

Against the odds, you remain determined and focused. You've invested your heart, energy, and savings to achieve your goal.

The risks and sacrifices are many. So are the rewards. You are an entrepreneur!

Why Entrepreneurship?

The word **entrepreneurship** is the act of being an **entrepreneur**. An entrepreneur does **entrepreneurship** and acts **entrepreneurially**.

Entrepreneurship is important in society. Entrepreneurs create businesses, which provide jobs and income to people in a local community or around the world. Businesses solve small and large problems, provide much-needed goods and services, and pay taxes that help the government function.

Entrepreneurship also enables individuals to exercise their freedom to pursue opportunities and a life of their choosing.

There are many reasons why someone would want to run and take on the risk of operating a business. The most common reasons include being your own boss, setting your own work schedule, being part of something that you own, having control of your destiny, and perhaps even the possibility of generating enough wealth to gain financial freedom. There are many other reasons as well.

There are many challenges associated with being an entrepreneur. For example, since you own the business, if it does not do as well as you expect, you are still responsible for it. You may have to work many hours each day managing and dealing with problems that arise. You may not even make enough money to pay yourself a salary. If your business is not successful, you may lose all the money you invested in it, as well as some of your personal assets.

Running a business is a risky proposition with many advantages and disadvantages.

Who Can Be an Entrepreneur?

Anyone can be an entrepreneur. Age, gender, or race does not decide who can be an entrepreneur.

A person determines if they want to be an entrepreneur by having an interest in starting and running a business, and the willingness to take the initiative, risk, and leadership responsibility associated with this endeavor.

There is no pre-set profile of an entrepreneur that you must match. Entrepreneurs do not look or think alike. They can be as different as any two individuals can be.

Only you can decide if being an entrepreneur is what you want to be. Understanding entrepreneurship will help you in whatever you do.

Success in Entrepreneurship

Measuring success in entrepreneurship is not a simple task. Each entrepreneur evaluates success differently.

For example, someone may consider a business successful only if the business generates good profits, regardless of the other issues involved in operating the business. Others may consider a successful business one that treats its customers and employees very well and generates just enough revenue and profit to get by.

There are many entrepreneurs who may not be financially wealthy, but consider themselves successful.

There are many factors, both tangible and intangible, that need to be considered when measuring success in entrepreneurship.

Tangible Factors

- Revenue and profit
- Business growth and reach
- Market share
- Length of time in business
- Ownership value and personal wealth

Intangible Factors

- Brand value
- Customer satisfaction and loyalty
- Employee morale
- Contribution to community
- Personal time available for family and friends
- Personal stress
- Sense of freedom and control
- Overall learning experience
- Personal satisfaction being an entrepreneur

Each individual will apply a different level of importance to each of the factors above when determining the success of their own entrepreneurship experience.

Evaluating Success

Following are more detailed explanations of the success factors.

Profit

Profit means to create more money than you started with. A business must generate profits in order to survive in the long term. It is common for new businesses to lose money in the first few years. Initial losses, or having losses in other years, does not mean the business will not be successful. However, over time, the trend must be to generate ongoing profits, otherwise the business will run out of money and have to shut down.

Review the examples in the table below and complete the final example.

REVENUE FROM SALES	$400	$1,000	$500
COST OF OPERATING THE BUSINESS	$350	$500	$200
PROFIT	$50 = $400 - $350	$500 = $1,000 - $500	$ ____________

Profit for the business owners can also be generated by selling the business at the right price. Review the examples in the table below and complete the final example.

INVESTMENT MADE IN THE BUSINESS	$500	$600	$1,000
SELLING PRICE OF THE BUSINESS	$800	$1,000	$2,000
PROFIT	$300 = $800 - $500	$400 = $1,000 - $600	$ ____________

Maximizing profit is not always the best strategy. You can achieve profit in the short term by cutting corners or doing things that may not be sustainable in the long term. For example, a business that reduces the quality of its product to save money, may find that customers will stop purchasing. A business that underpays its employees may show more profit in the short term, but employee morale may become so low that operations will be inefficient and employees may eventually quit.

Achieving and maintaining profit is a difficult balancing act.

Revenue

Revenue is the money given to a business by customers purchasing its goods and services. A business that has high revenue has demonstrated that it offers a product that is desired by consumers. Review the examples in the table on the next page and complete the final example.

PRODUCT SELLING PRICE	$10	$50	$100
QUANTITY OF PRODUCT SOLD	5	20	50
REVENUE	$50 = $10 x 5	$1,000 = $50 x 20	$ ____________

But, generating revenue without profit can be problematic. For example, a business can offer a product at an unusually low price, thereby attracting significant sales and revenue. But, if the business loses money with each sale, it may eventually run out of money. The only way to keep such a business operating is to raise money by borrowing or by selling shares.

Review the examples in the table below and complete the final example.

PRODUCT SELLING PRICE	$10	$10	$20
COST TO MAKE AND SELL PRODUCT	$9	$11	$22
PROFIT	$1 = $10 - $1	-$1 = $10 - $11	$ ____________

Proving that a business can sell products and generate revenue is a valuable achievement. And, even if the business may have difficulty achieving profit, it may be an attractive business for someone to purchase and make profitable using a different strategy.

Equity

Equity means the value of a business. Business value is generated in one of two ways:

- Generating profit – and keeping that profit in the business, instead of distributing it to the owners (shareholders).
- Raising money by selling shares in the business.

Review the examples in the table below and complete the final example.

VALUE OF BUSINESS	$10	$10	$20
NEW PROFIT FROM SELLING PRODUCTS	$2	$5	$4
NEW VALUE OF BUSINESS	$12 = $10 + $2	$15 = $10 + $15	$ ________

Review the example in the table below and complete the final example.

VALUE OF BUSINESS	$20	$20	$50
MONEY RAISED SELLING SHARES	$3	$5	$6
NEW VALUE OF BUSINESS	$23 = $20 + $3	$25 = $20 + $5	$ ________

The two achievements above will increase the **financial** value of a business. But, there are other ways to increase the value of a business, including:

- Growing revenues
- Increasing the number of customers
- Types of customers
- Products and processes that are difficult to duplicate
- Patents and trademarks

Each of the achievements above, and some others, can increase the **goodwill** value of a business, which means the business will be more valuable even though the financial numbers (like equity) may not show this value.

Market Share

The percentage of customers or sales a business wins in comparison to other businesses of the same type is called **market share**. A business with high market share may dominate its competitors, and can increase the value of the business.

Review the examples in the table on the next page and complete the final example.

NUMBER OF CUSTOMERS	100	100	100
PURCHASE FROM BUSINESS A	70	50	30
PURCHASE FROM BUSINESS B	30	50	70
MARKET SHARE BUSINESS A	70% = 70 ÷ 100 x 100%	50% = 50 ÷ 100 x 100%	$ __________

Brand, Reach, and Growth

Brand is how people feel about your business or product. An entrepreneur who creates a product that people feel good about and may be known widely, and even admired, could be considered a success for the entrepreneur. And, the more people that are reached and influenced by the business can enhance this success.

Consider how you feel about these well-known brands …

Mercedes-Benz

Coca-Cola

Walmart

Customer Satisfaction and Loyalty

Without customers, a business has no sales. A customer that uses a product and is pleased with it is sometimes described as a **satisfied customer**.

Satisfied customers return and buy again, and may also tell their friends and promote a business through **word-of-mouth** – which is like free advertising, and often the best type of endorsement a business can receive.

A customer that repeatedly buys from the same business, and is reluctant to change, is called a **loyal** customer.

A customer that is unsatisfied with a product may or may not express their dissatisfaction to the business, but they are less likely to return to the business. And, they may share their unhappy experience with others, which will negatively affect the business.

A business that has achieved high customer satisfaction and loyalty has a significant advantage.

Complete the table below by using the terms defined above.

PLEASED CUSTOMER	CUSTOMER THAT REPEATEDLY BUYS FROM SAME BUSINESS	TYPE OF FREE ADVERTISING
________________	________________	________________

Employee Morale

Running a successful business means hiring and training an efficient workforce. Insufficient employees or a workforce with low morale can result in lost sales and unhappy customers.

Morale represents the emotional well-being and attitude employees have towards their work, work environment, and employer. Employees who enjoy their jobs and related benefits will have higher morale than those who do not.

Happy employees tend to work harder, more efficiently, and interact with customers in a more positive manner.

For a business to maintain good employee morale, it takes effort and money. This investment of time and money is a cost for the business, but it may have a positive effect that helps make the company more successful.

Time in Business

Many businesses fail or are shut down within the first few years of starting. Surviving and keeping a business running for a length of time can be considered a success.

Community

A business directly and indirectly contributes to the community in which it operates. Businesses create jobs, provide incomes, purchase goods and services, and keep or bring in money to the local community. They also pay taxes to help fund government.

All of this is made possible by the initiative and risk taken by the entrepreneur who starts the business

Even a business that fails financially will have made a positive contribution to the local community.

Personal Wealth

A successful business returns some level of personal wealth to the owners. This may be through a higher salary for owners that work in the business, a payout of company profits (dividends), or a financial gain if the business is sold.

Many businesses fail and the owners end up losing money. With businesses that are successful, it often takes years before a business can earn enough profit or value to generate wealth for the owners. And, even when that happens, many business owners will allow a business to keep its profits so that they can be used to operate and grow the business further.

Stress and Personal Time

An entrepreneur is exposed to tremendous pressures by being responsible for everything in a business. This is particularly true of new businesses that may have limited financial and human resources.

Entrepreneurs are challenged with finding a balance between business and personal commitments. Starting and growing a business can require significant personal time and focus, and an entrepreneur may sacrifice sleep, nutrition, exercise, family time, and other important life activities.

Business and personal-life challenges can create emotional **stress** for the entrepreneur. Stress is a physical, chemical, or emotional factor that causes physical or mental tension. Stress has been linked to increased chance of illness.

In the short term, most entrepreneurs can survive periods of high stress. In the long term, stress will impact the entrepreneur's ability to manage the business successfully.

An entrepreneur who is frequently ill, or sick for a long period of time, may not be able to devote enough focus on the business. This may result in the slowing down, closure, or premature sale of the business.

Stress can be reduced through a number of ways, including:

- Increasing personal time
- Better nutrition
- Exercise
- Deep breathing
- Reduced work hours
- More sleep
- Taking a vacation

By keeping stress at a low level, an entrepreneur can improve productivity, clarity of thinking, health, and happiness.

Freedom, Learning, and Personal Satisfaction

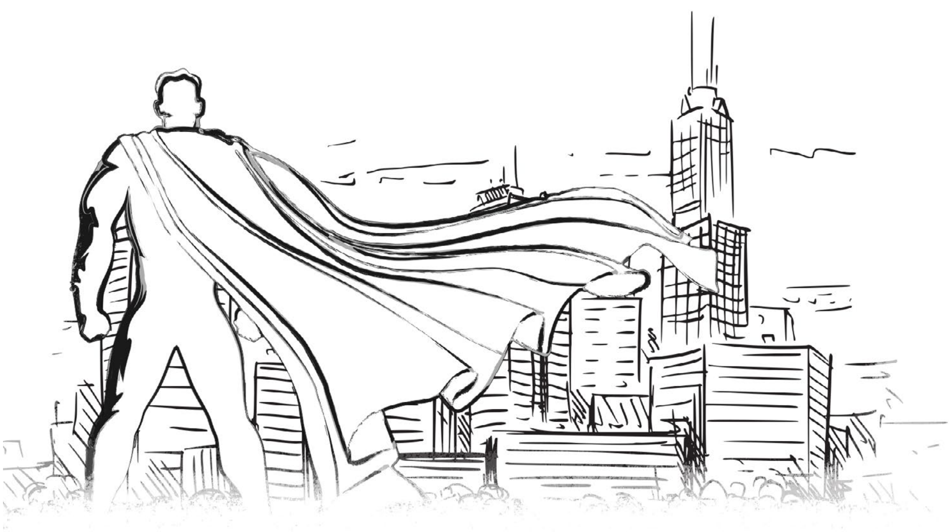
Entrepreneurship enables individuals to exercise their freedom to pursue opportunities and a life of their choosing. This can create a feeling of empowerment for the entrepreneur.

The various small and large successes that are achieved may also provide personal satisfaction and a sense of meaning in their lives.

2. Management and Entrepreneurship

Entrepreneurs are constantly learning through their experiences. This is particularly true of new entrepreneurs. There is no end to the knowledge and skill that can be gained as an entrepreneur, including:

- Critical thinking
- Problem solving
- Managed risk taking
- Leadership
- Team building
- Planning
- Organization
- Decision making



Managing Risk

Starting and operating a business has significant risk. Risk is the likelihood that the business will fail and the entrepreneur will lose the time and money invested in the business.

Businesses frequently fail because there are many factors that need to work out favourably in order to achieve success.

Operating a business involves taking and managing risk. It requires decisions to be made with imperfect knowledge. Budgets are set, employees hired, and inventory purchased all on the expectations of what may happen.

Nothing is certain – now or forever. Even long-established industries have collapsed due to unpredicted changes in technologies or economic environments.

A successful business owner or manager must be willing to take risks. They must also understand how to take acceptable risks, and know when to avoid risk – making all these decisions on incomplete information.

Risk is not the same as gambling. Entrepreneurs are risk-takers, but not necessarily gamblers. With most gambling, you have little or no control or influence over the result. Buying a lottery ticket or tossing dice has fixed odds of failure and success that you cannot change. In business, risk is something that can be evaluated and often reduced with the right strategy.

Business owners and managers take these calculated risks based on their expectations for potential returns (financial gain). All businesses want some sort of return for their efforts, and the higher the risk taken, the greater the return expected.

Review the examples in the table below to see how the risk should match the expected return.

MONEY INVESTED	\$100	\$100	\$100
RETURN	10% = \$10 LOW	25% = \$25 MODERATE	100% = \$100 HIGH
TOTAL	\$110	\$125	\$200
RISK	LOW	MODERATE	HIGH

Upside and Downside

Two terms often used in entrepreneurship are **upside** and **downside**.

Upside refers to the rewards that can be earned if successful.

Downside refers to the losses that may be experienced through failure.

Entrepreneurs run towards the upside opportunity, while other people run away from the downside risk.

Experience and Decision Making

There are countless books, websites, videos, and experts that say they can lead you to success in operating a business. It is important to recognize that there really are no resources available which an entrepreneur can use to find the right answer for every challenge that will be encountered.

Business challenges may appear similar, but there is always the context of how and when potential solutions may be applied.

Nearly every decision an entrepreneur makes has both positives and negatives in some way. For example, providing higher pay to an employee may make that employee happier and more productive, but it will also increase the costs of the business. When deciding what equipment to purchase, is it better to purchase the less-expensive used equipment that could be unreliable, or the new and more-expensive equipment that includes a warranty?

Every decision has consequences – some of which may be known or unknown. The best an entrepreneur can do is try to choose the decision that provides the best balance. While an entrepreneur can seek advice from many sources, it is research, planning, and experience that ultimately assure that the best decisions are made.

3

OWNERSHIP

Business Ownership

The creation of a business usually starts with an idea. An idea to make and/or sell goods or services. Anyone can start a business at any time. But, how is business ownership determined?

With a **nonprofit organization**, no one actually owns the organization. The people who start the organization assign directors or members to be responsible for the organization. These directors and members may change over time, based on rules set up when the organization is created.

With a **for-profit business**, the person or people who start the business own the business. They are often called the business **founders**.

If one person starts the business, that person will own 100% of the business. If two people start a business, they will agree on how the ownership will be divided. They may agree to evenly divide the ownership to own 50% each. Or, they may agree that one of the founders will own 70%, while the other will own 30%.

Any combination is possible and the ownership percentage should align with the amount of effort, risk, and money that the owners are individually contributing.

An owner of a business – specifically, a corporation – is called a **shareholder**. This is because ownership in a corporation is established by owning a percentage – or **share** – of the business.

- A business can be divided into any number of shares.
- A business can have one share owned by one person – which means they own 100% of the business.
- If a business has 10 shares owned by one person, that person also owns 100% of the business. Or, the 10 shares can be separated where one person owns 7 shares (70%) and another person owns 3 shares (30%).
- A business can have millions of shares.
- A person does not have to work in the business to be a shareholder or founder of the business.
- Shares are also called **stock**.

Review the examples in the table below and complete the final example.

NUMBER OF SHARES	100	100	100
SHARES OWNED BY PERSON A	70	60	50
SHARES OWNED BY PERSON B	30 = 100 – 70	40 = 100 – 60	___________

3. Ownership

To demonstrate ownership in a business, shareholders may be issued a paper document called a **stock** or **share certificate**. Below is a Facebook share certificate. Share ownership is primarily recorded electronically, so issuing printed share certificates is not as common as it used to be.

Buying Ownership in a Business

Businesses often raise money to fund their operations by selling a percentage of ownership in the business. This is done by selling shares in the business.

For example, a business might offer to sell 10% of the ownership in the business for $10,000. The business will then use that money to fund its operations. And, the person or organization who purchased the shares (the shareholders) will be able to share in the profits generated by the business.

- If the business generates $20,000 in profit this year, these shareholders may earn a share of the profits equal to 10% or $2,000. When a business pays out profit to the owners, it is called issuing a **dividend**. Not all businesses issue dividends.

- If the business is sold for $150,000, these shareholders may be entitled to 10% or $15,000 of this money.
- Note that when a business sells shares to raise money, this new money goes to the business, not to the shareholders or anyone else.

The financial benefits of being a shareholder in a business are actually more complex than described above.

Review the examples in the table below and complete the final example.

PROFIT EARNED BY A BUSINESS	\$100	\$100	\$100
PROFIT ISSUED AS DIVIDENDS	\$40	\$70	\$50
PERCENTAGE OF BUSINESS OWNED	10%	10%	10%
AMOUNT EARNED BY SHAREHOLDER	\$4 = 40 x 10%	\$7 = 70 x 10%	\$ ________

Selling ownership in a business is not the same as taking out a loan. A loan is when money is borrowed and has to be repaid, usually with interest (an additional fee). Many businesses borrow money to fund their operations instead of selling ownership. Borrowing money is much less complicated than selling ownership.

Selling ownership also means that the shareholders will have some say in the business, often with the right to vote on important issues, including who runs the company and how profits are used.

Money raised by selling ownership in a business does not have to be repaid like a loan. Instead, the shareholders benefit by potentially sharing in the future profits of the business operations or when the business is sold.

Selling ownership in a business is also called selling **equity** in the business.

To sell shares in a business, the organization has to be registered as a for-profit company. A nonprofit business or organization cannot sell shares. The for-profit business has to be registered as a corporation.

Private Versus Public Company

Every business starts as a **private** organization. Private means that the internal operations and finances of the business can remain confidential to the owners and managers of the business and certain departments within government. They do not have to disclose this information to the public or anyone else.

When a business wants to raise money by selling shares, it has to follow certain government regulations. These regulations outline how a company can raise money and who it can raise money from.

The regulations are designed to protect the public from investing in businesses that do not have proper structure and shareholder rights.

One requirement is that the business has to be registered as a **for-profit corporation**. When a business is registered as a corporation, the company starts as a **private** – not public – organization.

Additional regulations significantly restrict how a company can raise money, effectively only allowing the business to reach out to a small number of potential investors.

If a company wants to be able to widely promote its sale of shares and allow anyone in the general public to purchase its shares, then the business must become a **public company**. Although, some regions allow a company to remain private for certain types of equity-based crowdfunding campaigns.

A public company is required to disclose its financial information to the public. This information can no longer be kept confidential, as it can in a private company. By making financial and other information public, people can better assess the value and risk of purchasing shares in the business. To clarify, a public company can still keep much of its internal business information confidential.

Once a company is public, it can buy, sell, and trade its shares more easily and widely. This is often done by listing the company on a **stock exchange**.

A stock exchange, often called a **stock market**, is a physical or online marketplace where shares of companies can easily be bought and sold (traded) by the public.

An important feature of the stock market is where the money goes when shares are traded. When a company wants to raise money, it issues new shares to investors who buy the shares. This money goes directly to the company. But, when an existing shareholder sells shares to another person, the money goes to the shareholder who sold the shares.

4 STARTUP

The Idea

Every business starts with an idea to make and/or sell goods or services. Ideas are easy, but executing an idea successfully is very difficult.

There are many questions to be considered at this stage:

- What is the problem being solved or need being served?
- Is the idea viable as a business – will the business generate a positive return on investment?
- Is this a new type of business, a business similar to others, or a franchise business?
- What type of people and experience are needed to run the business?
- Will you start (found) the business on your own or partner with others (cofounders)? What contribution will each partner make and what percentage of ownership will each receive?

- Do you have the financing needed to start and operate the business?
- What are your personal goals for undertaking this endeavor?
- Are you prepared to take on the risk and sacrifices needed?
- Will you have to quit a money-earning job? How will that affect your personal life and finances? Can you start the business part time without leaving your job?

Most ideas do not have the potential to become viable businesses. An idea could have good business potential, but there may already be entrenched competition that will be difficult to overcome. Or you may not have the right experience and resources needed to achieve success.

Business Model

To determine if a business idea is viable, a number of factors have to be considered. The most important are as follows:

Product
What are the features and benefits of the product? If the product is a good, can it be made? Some goods may be too difficult, too costly, or impossible to manufacture.

Differentiation
Determine how the product will be different than competing products or options. This could be by price, features, quality, or other factors. The product and its differentiation describe the **value proposition** offered to customers.

Addressable Market
Determine the number of consumers that are likely to purchase the product and how much money can be made from these sales. This must also account for sales of competing products and other options.

Marketing and Distribution
Determine how consumers will be made aware of the product and how they can purchase and receive the product.

Costs
Determine the costs of making, marketing, and providing the product and all the other costs associated with operating the business. Subtract these costs from the potential revenue that can be generated to determine if profitability is possible.

The factors above form what is called the **business model** for the business. An idea that is investigated more closely to determine a potential business model will often reveal challenges that may be too difficult to overcome. If profitability cannot be achieved, then the idea is generally not worth pursuing as a for-profit business.

Most people do not get past the idea or business model stage. That may be fine, as it is better to avoid starting a business that is sure to fail.

Mission, Vision, and Values

A business should identify what it wants to achieve and how it plans to do so, using brief and simple terms.

A **Vision Statement** is a phrase that describes the future state of the business, if it is successful.

A **Mission Statement** describes how the business will achieve its vision.

A Vision Statement uses broad and wishful thinking, while a Mission Statement is more specific and measurable.

Examples:

Vision Statement
To be the leading manufacturer of widgets in North America.

Mission Statement
To manufacture the lightest and most reliable widgets in the automotive industry.

Notice that in the Vision Statement, the term *leading* is not defined – it could be revenue, innovation, or other factor. The Mission Statement is more specific, using terms *lightest* and *most reliable*, which are specific differentiators that can be measured when compared to competing products.

With the example above, the business strives to be the *leading manufacturer* by making the *lightest* and *most reliable* widgets. The business may have chosen this strategy because competing widgets may be too *heavy* or *unreliable*. Another approach may be to manufacture the *least expensive* widgets.

Consider a restaurant with one Vision and two possible Mission Statements to choose from:

These examples show how a business could achieve the same vision by pursuing a different mission. Both missions are easily measured and can help guide the business owner to stay true to the selected strategy.

If a competing restaurant expands its children's menu or builds a large play structure, then the mission calls for the business owner to consider doing the same in order to stay in the lead. Or, the business owner may decide that a new vision and mission should be pursued.

As time passes, things change, markets develop, and new information is discovered. This may prompt the business owner to adjust strategy – and perhaps make a significant shift in vision and mission – this is sometimes called a **pivot**.

Values are the core principles or standards that guide the way the people in a business operate. They may include beliefs and attitudes with how people should behave towards each other, suppliers, and customers, and the ethical standards by which the business strives to abide.

Values form the foundation for decision making within the organization. Vision and Mission Statements may change over time, but values generally do not. Values may not always be documented, but they are evident by observing how the people within a business act, internally and externally.

Business Name

Every business needs a name. The name of your business can give a significant amount of information and emotion about your business. The name is how the business will be recognized and remembered by your potential customers.

A business name can be long or short, descriptive of what your business does, or not. It is up to you.

Consider these business names and if the names are representative of the business they are in…

Red Bull NIKE LEGO ELMER'S

BANK OF AMERICA

Microsoft CARFAX VEHICLE HISTORY REPORTS

If you will be doing business in a multicultural region, it is also important to keep in mind that the name you choose should translate well into other languages.

If you operate a franchise, however, the name of your business will take on the same name as the franchise, like the examples below.

McDonald's MIDAS Holiday Inn

Although, with a franchise, you do not have a choice in names, having the name of a popular franchise may give you instant recognition with consumers. This is called **brand awareness** or **brand recognition**.

Brand Awareness can be very valuable for attracting customers, because the more people who know about a business, the better. But, Brand Awareness can also be negative for a business that is thought to sell low-quality products or services, or treat customers or employees unfairly.

When choosing a business name, it is important to be careful not to choose a name that is too similar to one that is trademarked. A **trademark** is a combination of letters, words, sounds, or designs that distinguishes the goods or services offered by one organization from those of others in the marketplace. Trademarks can be registered with the government to prohibit competing businesses from using similar Trademarks that may cause confusion with consumers.

Logo

A logo is a unique visual identifier that distinguishes your business. Similar to a business name, a logo can impart a significant amount of information and emotion about your business, and how it will be recognized and remembered by your potential customers.

A logo can become so well known that people can instantly identify the name of the company it belongs to. For example, the Nike swoosh or McDonald's golden arches.

A logo normally includes text (the name of the business) and a graphic. Sometimes, a logo does not include a graphic image, instead, the text is stylized – this is called a **wordmark**.

Similar to a business name, care should be taken not to use a logo that is Trademarked.

Your logo should be used on all business communication materials, including letterhead, business cards, and on the storefront. Having a consistent design with all materials helps build **brand identity**, as shown below.

Legal Structure

Every business must be legally registered with the government and must follow the required regulations. The three most common types of legal structures for businesses are sole proprietorship, partnership, and corporation.

Each type has advantages and disadvantages, and careful consideration is necessary when selecting the appropriate structure. In some cases, the structure of a business can be changed in the future.

Sole Proprietorship

A sole proprietorship is owned by one person.

Advantages

- The simplest legal structure and the least expensive to set up.
- There is minimal paperwork required to register.
- All business decisions are made exclusively by the owner – called the **sole proprietor** – consequently it tends to be the most flexible business to run.
- The sole proprietor is personally responsible for everything, including debts, and the profits or losses of the business are reported as part of the owner's personal tax return.

Disadvantages

- Unlimited liability – the sole proprietor is personally liable for all business liabilities. If the business cannot pay the bills or gets sued, the owner could lose his or her personal assets (savings, automobile, house, etc).
- It may be more difficult to raise money. Usually, banks and investors prefer to provide financing to partnerships and corporations. And, the business can only request debt financing – selling ownership equity

is not an option because a sole proprietorship does not have any share structure – it is an individual person not a company.

- The business can suffer if the owner becomes ill for an extended period of time.
- Very profitable businesses may have to pay higher taxes, because of the personal tax laws.

Partnership

A partnership is similar to a sole proprietorship but owned by two or more people. The owners form an agreement about ownership percentages and responsibilities. The profits and losses of the business are divided and shared according to these percentages, and included on each partner's personal tax return. There must be at least one general partner – who, like a sole proprietor, is personally responsible for all liabilities.

Advantages

- The business will have the combined resources and skills of more than one person.
- All business decisions are made exclusively by the partners.
- The partners are personally responsible for everything, and the profits or losses of the business are reported as part of the partners' personal tax returns.

Disadvantages

- Unlimited liability – the partners are personally liable for all business liabilities. If the business cannot pay the bills or gets sued, the owners could lose their personal assets (savings, automobiles, houses, etc).

- Business decisions can be more difficult when two or more partners must agree.
- If one partner cannot continue the relationship, then the partnership becomes automatically dissolved, and a new agreement must be written if the business is to continue. This can incur significant business and administration costs.
- Depending on the structure of the business, a partnership may or may not have shares that can be sold like a company.
- Very profitable businesses may have to pay higher taxes, because of the personal tax laws.

Corporation

A corporation is an entity that has been created to conduct business – for profit or nonprofit – and is effectively recognized as a person under law. A corporation has one or more owners and – unlike a sole proprietorship or partnership – does not legally represent a particular person, because it is an entity of its own.

Corporations issue shares of stock to their owners (called shareholders). There can be one shareholder, or the corporation could sell its shares to millions of shareholders.

This is the only legal structure which has limited liability. This means that the company, as a separate entity, is legally liable for its own actions and debts – not the owners.

To clarify, the owners (shareholders) can still lose money they invested in the business, but if the business cannot pay the bills or is sued, the owners cannot (normally) be held liable.

Company profits and losses are not added to the owners' (or shareholders') personal tax returns – the corporation submits its own corporate tax return. The company can decide to share part of its profits with its employees and/or it can pay dividends to its owners, the shareholders.

Advantages

- Limited liability – the shareholders' personal assets are not in jeopardy if the business fails.
- There are certain corporate tax advantages that are not available to a Sole Proprietorship or Partnership.
- Financing may be more easily obtained.
- A Corporation will continue even after the death or withdrawal of one of the founding members.

Disadvantages

- Registering a corporation is more complex and costly.
- Owning a corporation with shareholders requires that financial and business reporting be done.
- The company is ultimately owned by the shareholders. If a single person or group owns more than 50% of a company's voting shares, then they have control over the company. They could even vote to fire the founders.

Although a corporation has limited liability, there are instances where the board of directors has been held liable for the actions of the company. In addition, it is common with small companies for lenders to require personal guarantees for loans, which essentially ties the personal liability for the debt back to the guarantor.

Summary of legal structures…

	SOLE PROPRIETORSHIP	PARTNERSHIP	CORPORATION
SIMPLEST AND LEAST EXPENSIVE TO SET UP	✓		
ALLOWS FOR MORE THAN ONE OWNER		✓	✓
SEPARATE ENTITY			✓
LIMITED LIABILITY			✓

Seed Financing

Financing means money. **Seed financing** is the money needed to start a new business. This money is used to cover startup costs, like business registration, equipment, permits, insurance, building renovations, and more.

Money may also be needed to buy product inventory and cover operating expenses until the business becomes profitable. This operating money is called **working capital**. The total of startup costs plus initial working capital equals the amount of seed financing needed.

Seed Financing = Startup Costs + Working Capital

Types of seed financing include debt, equity, and grants – each is described in detail under ***§ Financing***. Below is an example of seed financing for a hot dog stand business.

Startup Costs		Working Capital
Cart (Used)	$1,000	Propane
Equipment	$250	Hot Dogs, Buns, Toppings
Signage	$100	Utensils, Napkins
Insurance	$150	Wages for help
Permits	$175	
Total	$1,675	Estimate $500/week

Seed Financing = $1,675 + $500/week x 10 weeks = $6,675

Sources of Financing

When seeking seed financing to start a new business, entrepreneurs can explore the sources listed below – each is described in detail under ***§ Financing***.

- Love Money
- Government
- Angel Investors
- Venture Capital
- Banks and Other Lenders
- Customers and Strategic Partners
- Public Markets

Due Diligence

The people being asked to give or loan money to a business or buy shares in the business will conduct due diligence before making their financing decision.

Due diligence means reviewing and researching the business and its owners and founders. A variety of information may be requested, including a business plan, financial statements, share structure, market information, and more.

Confidentiality

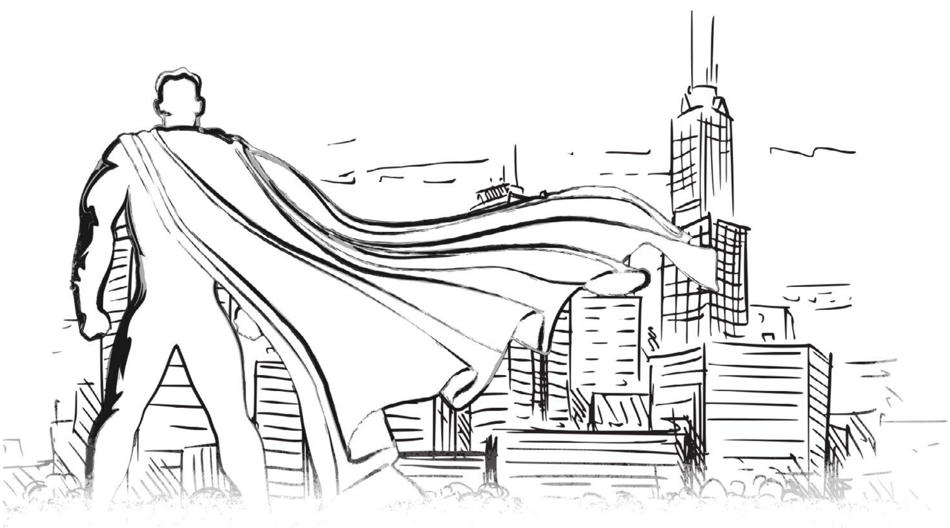
Business owners must frequently determine which confidential business information they may be comfortable sharing with people inside and outside the company. A business is not obligated to share its confidential information unless required by law or regulation.

Sharing confidential information may be necessary to accomplish business tasks, establish partnerships, secure financing, and more. Normally, confidential business information should only be shared on a need-to-know basis.

Business owners should conduct due diligence before sharing confidential information to make sure that disclosure is necessary and that it will be with a trusted person or organization.

Businesses often use a **non-disclosure agreement (NDA)** to protect their confidential information. An NDA is a legal contract where one or more parties agree not to disclose confidential information that they have shared with each other.

When and how to use an NDA depends on the circumstances of when confidentiality protection is needed.



Business Location

The best location for a business will vary depending on the type of business. For some businesses, choosing the right location can be the difference between success and failure.

For example, a manufacturing, research, or similar business that does not interact directly with consumers may not need to be located in a high-traffic area. A more suitable location would be one that provides lower rent and taxes, easy commute access for employees, and less expensive shipping and receiving.

With a business that interacts directly with consumers, such as a restaurant or retail store, being located in a high-traffic area can be very advantageous. Understanding local traffic patterns, weather effects, and the profile of consumers who live and work nearby are important considerations when deciding on suitable locations.

A business that is operated by remote workers may not need a physical location. A mailing address for the business is always needed, but office space may not be.

Location selection is also limited by local zoning regulations. Most municipalities identify zones in their towns and cities where businesses are allowed to operate.

Site Selection

Once a location is selected for a business, the next step is to select the site or building which will house the business and its workers. Issues to consider are:

- Purchase or rent (lease) cost and the terms for the purchase or lease.
- Utilities – energy and communications costs.
- Renovations needed (called leaseholds if renting the space).
- Parking for employees and customers.
- Maintenance, security, garbage pickup, landscaping, and snow-clearing responsibilities.

Equipment Selection

Equipment for a business includes items common to most businesses, such as furniture, telephones, and computers. There is also equipment specific to the type of business, as described in the examples below.

Restaurant
Cash register, dishes, pots and pans, oven, grill, deep fryer, refrigerator, freezer.

Clothing Store
Cash register, display shelves and racks, hangers, mirrors, security devices.

Furniture Manufacturing
Woodworking equipment, paint machines, forklift, large storage shelves, safety gear.

When purchasing equipment, there are four primary considerations:

Cost
Cost is an important factor in all purchases. Consider that the least expensive option may not always be the best choice. Something that may seem like a good bargain today, could turn out to be more costly in the long run if it has other drawbacks.

Capacity
With manufacturing equipment, capacity determines how quickly an item can be produced. With a restaurant or retail outlet, equipment capacity determines how many customers can be served at any one time. Purchase enough capacity to avoid losing sales during time with high demand. But, higher-capacity equipment can be more expensive, so finding the proper balance is necessary.

Reliability
Equipment that does not work properly can cause problems if

products cannot be produced and sold. Consider the expected reliability of the equipment that is being purchased. Used equipment may cost less, but may break down sooner or require costly repairs. Newer equipment may be more expensive.

Design

With manufacturing equipment, consider if the design provides for efficient use by the operator. With a retail store, the design should be consistent with the visual theme and identity of the business.

Selecting the appropriate equipment for a business can directly affect the success of the business.

Permits and Licenses

When starting a business, administrative work is necessary. It is important to file and receive all the required documents and approvals in a timely manner.

Regulations and requirements vary for each type of business and the location of that business – country, state or province, and municipality. It is the business owners' responsibility to find out exactly what is required for the business by contacting the appropriate authorities.

A business owner cannot claim to not have known about a requirement. If proper processes are not followed, the business owners could be fined, sued, and the business could be shut down.

Examples of permits and licenses:

Business Registration
All new businesses must register with the government.

Tax Registration
Tax registration with the government may be required, depending on the location of the business and in what regions of the world it does business.

Supplier
A permit may be required for selling goods.

Import and Export
A permit may be required for bringing physical goods into the country or exporting them out of the country.

Food Service
Required for food service businesses to maintain safety for public health.

Fire Safety
A permit required for new business locations to verify that fire-safety regulations are met.

Health and Safety
Businesses that employ workers who could be injured on the job must meet certain regulations to protect workers.

Environmental
Businesses that work with materials or processes that could impact the environment may be required to adhere to certain regulations to protect the environment.

Utilities
Establishing energy and telecommunications services at a designated office or building requires coordination with utilities companies.

Insurance
Certain types of insurance may be required for the business to operate properly. Insurance coverage may include fire, theft, business interruption, general liability, professional liability, health and life insurance, and more.

Zoning Regulations
Most municipalities identify zones in their towns and cities where businesses are allowed to operate. Businesses must be sure to locate within designated zones.

Intellectual Property

Intellectual property (IP) is comprised of ideas, designs, creations, and inventions. Individuals and businesses can register their IP with the government to help protect the IP from competitors who may try to duplicate the IP. Countries treat IP differently – laws and protection will vary. Common types of IP are described below.

Trademark
A trademark is a word, symbol, design, or a combination of these, used to distinguish the goods or services of one person or organization from those of others in the marketplace. For example, the word Coca-Cola is a registered

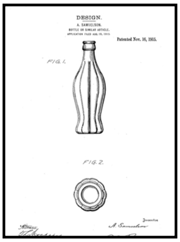
trademark of the Coca-Cola Company. The symbol ® is used to identify a registered trademark. The symbol ™ is used to identify a trademark that has not yet been registered.

Copyright

A copyright applies to all original literary, dramatic, musical, and artistic works. For example, if you write an original book, then you own the copyright to that book and no one else has the right to copy it without your permission. The symbol © is used to identify copyrighted work.

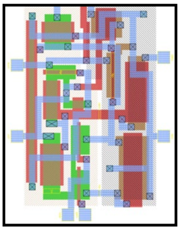
Patent

A patent applies to new inventions or processes that offer innovative and useful functions. For example, if you invent a new kind of mousetrap, you can apply for a patent to help protect your invention from being exploited by others.



Industrial Design

An industrial design is the shape, pattern, or ornamentation applied to a manufactured article. This may include things such as the shape of a piece of furniture or the ornamentation on the handle of a tool.



Integrated Circuit Topography

Integrated circuit topographies are the three-dimensional configurations of electronic circuits embodied in integrated circuit products or layout designs. Examples include things such as computers, smartphones, and televisions.

IP is complicated and, while it can provide some protection to the registered owner, it is up to the IP owner to take action on anyone that infringes on their intellectual property rights. But, such action may be time-consuming, expensive, and may or may not result in the desired outcome.

Business Advisors

Nearly all businesses require professional or expert advice to properly operate and reduce potential risks. The business owner must seek out business advisors who match their needs. Business advisors include:

Accountant
Helps with bookkeeping, taxes, and other financial issues.

Lawyer
Helps with business law, business registration, share structure, employee and customer contracts, trademarks, and more.

Banker
Helps with banking and financial services.

Insurance
Helps with insurance policies, such as fire, theft, business interruption, general liability, professional liability, health and life insurance, and more.

Other types of advisors and consultants may also be helpful, depending on the needs of the business.

5

BUSINESS PLAN

Overview

Once the business idea and business model have been determined, the next step is to develop a **business plan**.

A business plan is a document that describes, with some detail, how the business founders, owners, and managers plan to achieve success.

Purpose

A business plan has three main purposes:

1. For the entrepreneur to go through the process of carefully considering all aspects of the business that are needed to achieve success. Going through this process makes it easier to discover risks, challenges, and opportunities and how to navigate the business successfully. This process also helps identify the viability and potential of the business.
2. As a tool for communicating with investors, partners, and employees. All these stakeholders need to have a clear understanding of the business in order to work together to make it successful.
3. For the business management to monitor and measure success based on the path set out in the business plan.

Format

A business plan normally covers at least the first year of operation, and most often up to 3 years. Some business plans attempt to project up to 5 years.

Most business plans range from just a few pages to 20 or 30 pages and will include a one-page **summary** at the front (called the **executive summary**).

Normally, only the summary is sent to potential collaborators. The full business plan is sent after there is agreement to explore further.

A slide deck may also be prepared that has the primary elements of the business plan summary. This is called a **pitch deck**. The pitch deck is most often used in presentations, as shown below.

An **elevator pitch** may be prepared that summarizes the business in a few sentences. The elevator pitch is used in face-to-face conversations or included in email or other messages. The term *elevator* comes from the idea that the pitch should be concise enough to be said in a brief elevator ride with someone you just met.

Key Topics

Business plans, executive summaries, and pitch decks tend to include the same key information about a business. The order in which the information is presented may vary. Below is a list of topics that are usually included.

Business Description

What the business wants to achieve and how it plans to do so, using brief and simple terms – this could be the Mission and Vision statements.

The Opportunity

The problem being solved or need being served by the business. Profile of the consumers that are being targeted and potential sales that can be generated.

The Product

Description of the product (goods or services) and price structure.

Competition

Competing products and businesses and how the new product and business is different enough to win sales.

Marketing and Sales Strategy

How the business will reach consumers and convince them to buy.

The Team

Professional biographies of the founding team and key managers.

Funding Requirements and Exit Strategy

Amount and type of financing needed. If seeking equity investment, include an exit strategy describing how investors will make money.

Financials

Financial statements that show the current and future projected state of the business. This includes Balance Sheet, Income Statement (Profit & Loss or P&L), and Cash Flow. Collectively, these financial statements are sometimes called **pro forma** financials.

6
MARKET DEMAND

Marketing

Marketing is sometimes described as:

Selling the right product (goods or services)
… to the right people
… at the right price
… at the right place
… with the right promotion
… at the right time.

A market is all the people who might buy a particular type of product and the amount of money collectively spent on the purchases.

A market can be divided into smaller groups, called **market segments**, of similar potential buyers.

6. Market Demand

Market segments might be set up by geographic region, age, gender, economic status, language, family status, or many other descriptive groupings that help guide marketing and sales programs to reach these various groups of potential customers.

Market Demand

Market demand is the amount of money that is spent by consumers to purchase a type of product.

When you know the market demand, you can estimate the number of product units that can be sold to consumers, as shown in the table below using this formula:

$$\text{Product Units Sold} = \text{Market Demand} \div \text{Product Price}$$

MARKET DEMAND	$100	$20,000	$150,000
PRODUCT PRICE	$2	$20	$1,000
PRODUCT UNITS SOLD	50	1,000	150

6. Market Demand

Complete the table below with additional examples.

MARKET DEMAND	$50	$40,000	$300,000
PRODUCT PRICE	$10	$20	$1,000
PRODUCT UNITS SOLD	$ ________	$ ________	$ ________

Potential Revenue

Money your business receives by selling products is called **revenue**.

Revenue is calculated by multiplying the number of products sold by the product price, as follows:

Revenue = Price x Units Sold

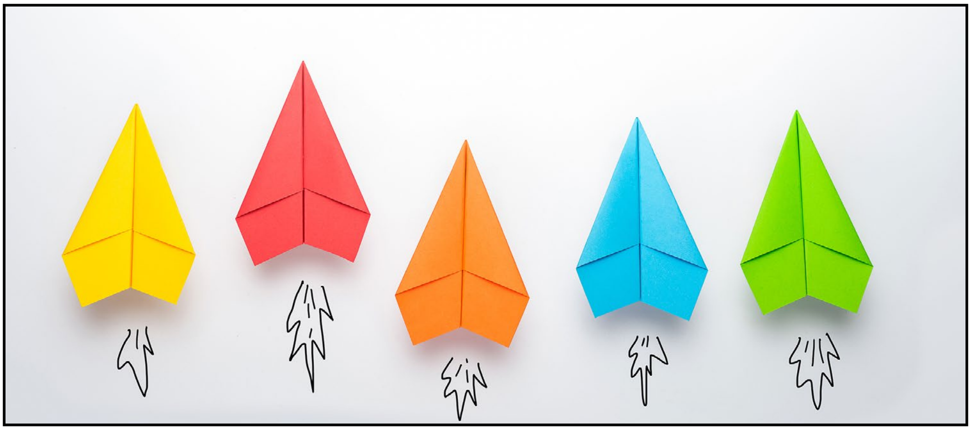
PRODUCT PRICE	$2	$20	$1,000
PRODUCT UNITS SOLD	50	1,000	150
REVENUE	$100	$20,000	$150,000

Complete the table below with additional examples.

PRODUCT PRICE	$3	$30	$1,500
PRODUCT UNITS SOLD	50	1,000	150
REVENUE	$ ________	$ ________	$ ________

Competition

Your ability to make sales and meet the market demand depends on a number of factors, one of which is competition.



If two competing companies are offering similar products at the same price, then it is likely that some consumers will buy one product while some consumers will buy the other.

6. Market Demand

The table below shows two competing products selling the same number of product units.

MARKET DEMAND	$100	
PRODUCT PRICE	$2	
PRODUCT UNITS SOLD	50	
	PRODUCT A	**PRODUCT B**
PRODUCT UNITS SOLD	25 = 50%	25 = 50%

The table below shows Product A selling many more units than Product B.

MARKET DEMAND	$100	
PRODUCT PRICE	$2	
PRODUCT UNITS SOLD	50	
	PRODUCT A	**PRODUCT B**
PRODUCT UNITS SOLD	40 = 80%	10 = 20%

Product Differentiation

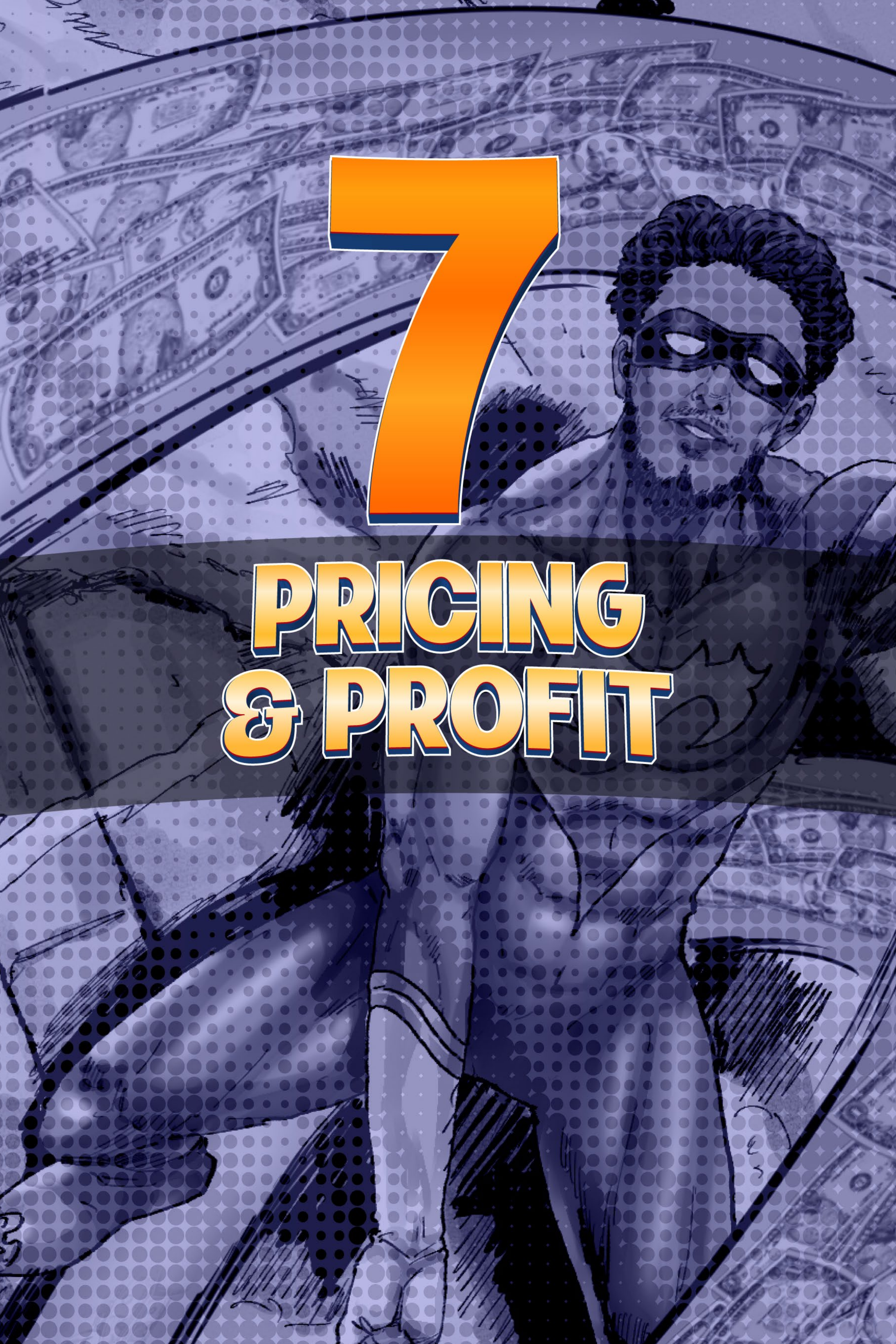
Why would Product A sell more than Product B? This could happen for one or more reasons:

- Better price (price is same in the example above)
- Better features
- Better quality
- Better brand
- Better marketing
- Better placement (easier to find)
- Available product inventory (available, not out of stock)

What does better mean? Better means that one product matches the needs of consumers better than the other.

7

PRICING & PROFIT



Pricing and Profit

Price is the money a customer gives to a business to buy its product. Setting the price of a product is an important and difficult decision.

How much should a sandwich cost? How about a car or a sofa? How should a business that sells such products price them?

Your answer to the above may be influenced by your own life experience. If you have purchased a particular product in the real world, you may have a price in mind. This is sometimes called **price anchoring**.

Be careful with price anchoring, because your own experience may or may not represent a comprehensive assessment of the marketplace. For example, location (country or region) may have certain products priced much higher or lower than in other regions or countries.

Variations in products can also greatly affect their cost. This is why certain restaurants can charge much higher prices for their food, while other restaurants compete on low price. Should a hamburger cost $5 or $20? It depends. Will consumers pay $20? It depends.

What does it depend on? It depends on the **consumer profiles**. These are the demographics and psychographics that define the needs and desires of a consumer.

And, it depends on the profitability needs of the business. The higher the price of a product, the more money that can be made on each product sold. But, as price increases, fewer products may be sold, which may reduce the total amount of money made on all products sold.

Discovering the perfect balance between price, units sold, cost, and profit can be complicated. These concepts are explored below.

Price

Price is the amount of money (revenue) you receive when your product is sold.

Cost of goods sold (COGS) is the cost to buy or make the products that you have sold.

PRICE	$10	$20,000	$500
COGS	$3	$8,000	$600
PROFIT	$7	$12,000	–$100

As shown in the table above, the price should be higher than the COGS in order to achieve a profit on each product sold. Otherwise, you will lose money on every product sold.

Complete the table below with additional examples.

PRICE	$50	$15,000	$700
COGS	$20	$8,000	$825
PROFIT	$ ___________	$ ___________	$ ___________

Gross and Net Profit

If the price is higher than the COGS, then you are making a **gross profit** on each product sold, but this does not fully account for all costs and actual profit. The tables above show gross profit.

Gross Profit = Price – COGS

Net Profit = Price – COGS – All Other Expenses

All Other Expenses includes costs for sales, marketing, operations, and more.

When setting the price for your product, you must account for COGS and all expenses required to operate your business, otherwise you may lose money.

PRICE	$10	$20,000	$500
COGS	$3	$8,000	$600
GROSS PROFIT	**$7**	**$12,000**	**–$100**
ALL OTHER EXPENSES	$8	$4,000	$250
NET PROFIT	**–$1**	**$8,000**	**–$350**

As shown in the table above, when all other expenses are included, only one of the products has positive net profit.

Complete the table below with additional examples.

PRICE	\$50	\$15,000	\$700
COGS	\$20	\$8,000	\$825
ALL OTHER EXPENSES	\$12	\$8,000	\$200
NET PROFIT	\$ ________	\$ ________	\$ ________

Calculating Costs

To determine profitability, you must calculate all costs to make and sell your product.

NUMBER OF PRODUCTS MADE	100
COST OF GOODS	\$6,000
SALES & MARKETING	\$5,000
OPERATIONS	\$2,000
ALL COSTS Add the three costs above	\$13,000
COST PER PRODUCT ALL COSTS divided by NUMBER OF PRODUCTS MADE	\$130 \$13,000 ÷ 100
PRICE	Should be higher than \$130

Complete the table below with additional examples.

NUMBER OF PRODUCTS MADE	100	5,000
COST OF GOODS	$2,000	$5,000,000
SALES & MARKETING	$2,000	$1,500,000
OPERATIONS	$1,000	$1,000,000
ALL COSTS Add the three costs above	$ ________	$ ________
COST PER PRODUCT ALL COSTS divided by NUMBER OF PRODUCTS MADE	$ ________	$ ________
PRICE SHOULD BE HIGHER THAN	$ ________	$ ________

Cost-Plus and Market Pricing

There are two ways to price products: **Cost-plus pricing** and **market pricing**.

Cost-plus pricing means determining all the costs to make and sell your product and setting a price that is a set amount above this amount.

ALL COSTS	$30	$10,000	$700
20% DESIRED PROFIT	$6	$2,000	$140
PRICE	$36	$12,000	$840

Complete the table below with additional examples.

ALL COSTS	$40	$12,000	$500
20% DESIRED PROFIT	$ ________	$ ________	$ ________
PRICE	$ ________	$ ________	$ ________

Market pricing means determining what consumers are willing to pay for your product and setting the price to this amount.

ALL COSTS	$30	$10,000	$700
CONSUMERS WILLING TO PAY	$40	$11,000	$950
PRICE	$40	$11,000	$950

Complete the table below with additional examples.

ALL COSTS	$40	$12,000	$500
CONSUMERS WILLING TO PAY	$52	$14,000	$750
PRICE	$ ________	$ ________	$ ________

Selling Price Versus Retail Price

The **retail price** is what consumers pay for your product. Consumers are the people who will actually use your product.

Some businesses do not sell directly to the end consumer. Instead, they sell their product to a reseller or distributor, who then sells the product to the end consumer.

The **selling price** is the money the reseller or distributor pays you for your product. The reseller or distributor will then sell your product at a higher price — the **retail price** — to the end consumer.

If you are selling your product to a reseller or distributor, your pricing and profit calculations must include the difference between the retail price and the selling price. This difference in price is sometimes called the **reseller discount**, **commission**, **wholesale price**, **wholesale discount**, or other similar term.

RETAIL PRICE	\$30	\$10,000	\$700
SELLING PRICE	\$21	\$7,000	\$560
DIFFERENCE RESELLER DISCOUNT	30% = \$9	30% = \$3,000	20% = \$140

Complete the table below with additional examples.

RETAIL PRICE	\$20	\$5,000	\$1,000
SELLING PRICE	\$ ______	\$ ________	\$ ________
DIFFERENCE RESELLER DISCOUNT	20% = \$4	30% = \$1,500	40% = \$400

Cost-Plus Pricing with Reseller Discount

RETAIL PRICE	$50	$10,000	$700
RESELLER DISCOUNT	20% = $10	30% = $3,000	40% = $280
SELLING PRICE	$40	$7,000	$420
ALL COSTS	$30	$5,000	$300
PROFIT PER PRODUCT	$10 = 25%	$2,000 = 29%	$80 = 19%

Cost-Plus Pricing with Reseller Discount

CONSUMERS WILLING TO PAY	$50	$10,000	$700
RETAIL PRICE	$50	$10,000	$700
RESELLER DISCOUNT	20% = $10	30% = $3,000	40% = $280
SELLING PRICE	$40	$7,000	$420
ALL COSTS	$30	$5,000	$300
PROFIT PER PRODUCT	$10 = 25%	$2,000 = 29%	$120 = 29%

Price Expectation

The amount of money consumers expect to pay for a product depends on a number of factors. This includes the influence of price anchoring, need, brand, and most importantly – **consumer profiles**.

Consumer profiles are the demographics and psychographics that define the needs and desires of a consumer.

8

CONSUMER PROFILES

Consumer Needs

Consumers are the people or organizations who purchase and use your product.

Needs are the desired preferences of consumers. Consumers seek out and purchase products that match their needs.

When there are multiple products available, consumers will, generally, purchase the product that most closely matches their needs.

See the examples below.

CONSUMER NEED	Low-priced product	
	PRODUCT A	**PRODUCT B**
PRICE	$2	$5
CLOSEST MATCH TO CONSUMER NEEDS	✓	

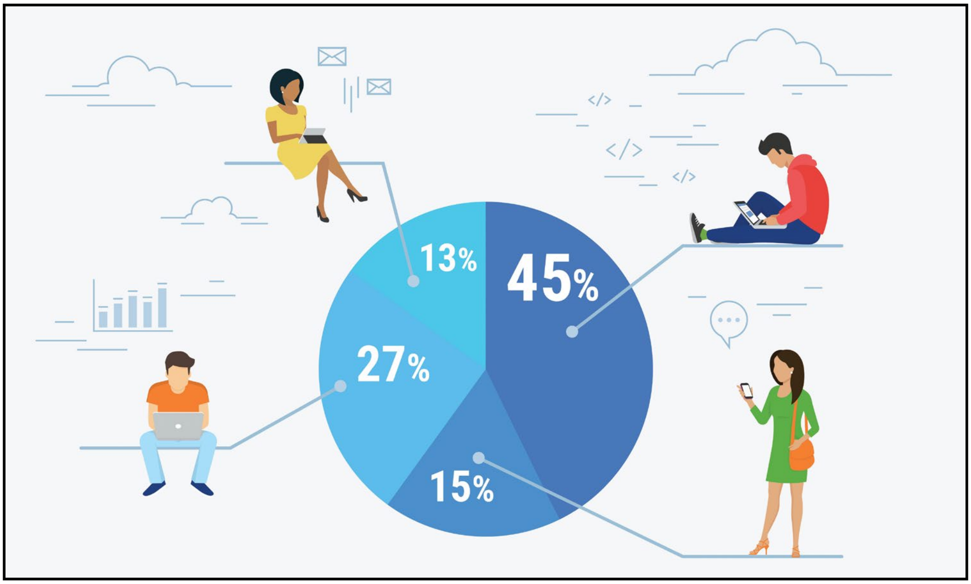
CONSUMER NEED	High-quality product	
	PRODUCT A	**PRODUCT B**
QUALITY	Moderate Quality	High Quality
CLOSEST MATCH TO CONSUMER NEEDS		✓

CONSUMER NEED	Moderate-quality product at a low price	
	PRODUCT A	**PRODUCT B**
PRICE	$2	$4
QUALITY	Moderate Quality	High Quality
CLOSEST MATCH TO CONSUMER NEEDS	✓	

CONSUMER NEED	Moderate-quality product	
	PRODUCT A	**PRODUCT B**
PRICE	$2	$3
QUALITY	Moderate Quality	Moderate Quality
CLOSEST MATCH TO CONSUMER NEEDS	✓	✓

In the final example above, both products match the consumers' needs. But, Product A may sell more than Product B because of the lower price.

Demographics and Psychographics



You can determine consumer needs by investigating consumer **demographics** and **psychographics**.

> **Demographics** include gender, age, income, location, and other statistical data.

> **Psychographics** are how a consumer thinks, including attitudes, aspirations, and other psychological criteria.

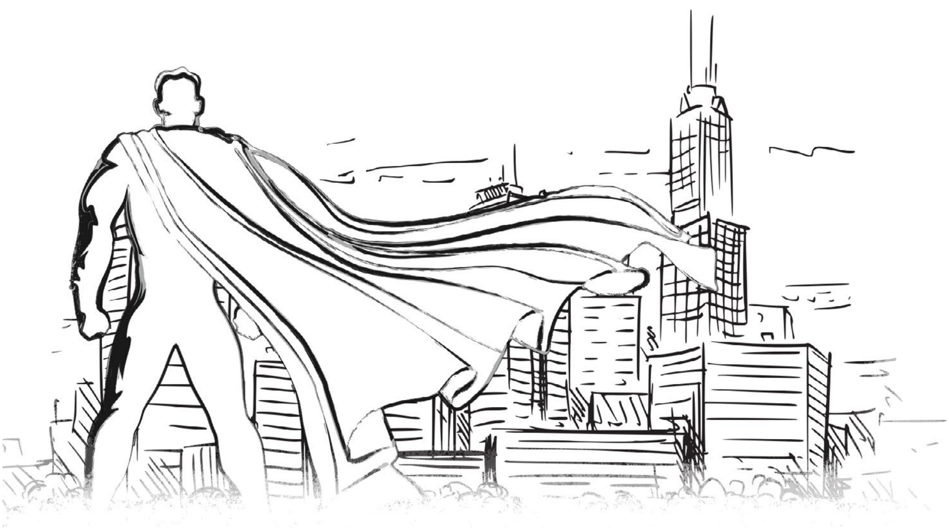
For example, if you sell an expensive luxury product, you may want to focus on consumers who have high income (demographics) and who desire luxury products (psychographics).

If you sell a sports fitness product, you may want to focus on consumers who play sports (demographics) and have a desire to stay fit (psychographics).

4 Ps of Marketing

Marketing is often summarized using what are called the 4 Ps:

Product	The features of the product.
Price	The price that consumers pay for the product.
Promotion	The effectiveness of the sales and marketing invested in the product, and the brand.
Place	The availability of the product where consumers are most likely to find and buy it.



8. Consumer Profiles

The table below shows an example of some of the factors that consumers will consider when purchasing a soft drink.

Price	A price-conscious consumer is more likely to purchase a lower-priced product.
Taste	A taste-conscious consumer is more likely to purchase a better-tasting product.
Health	A health-conscious consumer is more likely to purchase a product that offers the most health benefits.
Brand	A brand-conscious consumer is more likely to purchase a product with greater brand equity. Brand equity represents the brand awareness and brand loyalty you have created for your business. Brand awareness is how well-known your brand is versus the competition. It can be improved with advertising and sales promotion. Brand loyalty is the likelihood that a customer who has already experienced your product will purchase it again. It can be improved by getting repeat or new customers to purchase your product, with the hope that they will have a positive experience with the product.

Consumer Psychographics

In the soft-drink example above, each consumer has their own level of concern for the four factors shown.

For example, Consumer A may be 100% Price conscious, meaning they will always buy the least expensive soft drink. This can be represented with the pie chart below.

Consumer B may be 100% Health conscious, and seek out the healthiest product.

8. Consumer Profiles

Consumer C may desire a soft drink that has a good balance of Taste and Health and is willing to pay a higher Price for the product that best matches their needs. This might be represented by saying that this consumer has 50% concern with Health, 50% concern with Taste, and 0% concern with Price. A pie chart of this Consumer would look like the one below – notice that it adds up to 100%.

Combining all four factors shown in the table above for a particular consumer might look like the one below.

Notice that all 4 factors add up to 100%. Some factors, like Health and Taste, influence this consumer more than Price and Brand.

The product that most closely matches the consumer's needs will win the sale.

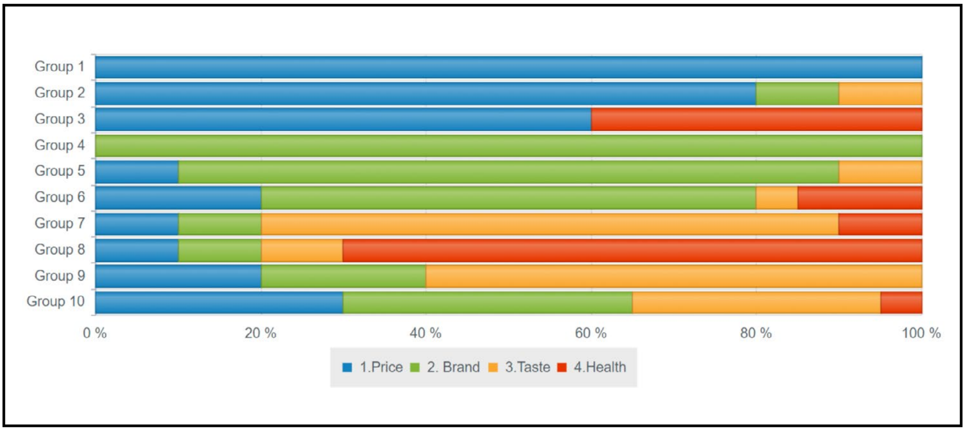
Consumer Groups

Most markets have a variety of consumers, each with different needs. From a marketing perspective, when looking closely at consumer needs, patterns tend to appear.

These patterns tend to identify consumers who have similar psychographics and group them together. These are called **consumer groups**.

Consumer groups are a collection of thousands or millions of consumer profiles into like-minded groups. This makes it easier for a business to target specific types of consumers.

For example, a market may have 10 consumer groups, each with different needs, as shown below.



Targeting Consumer Groups

Complete the table below to identify the psychographics of the given consumer groups from the chart above.

CONSUMER GROUP	PRICE	BRAND	TASTE	HEALTH
GROUP 1	100%	0%	0%	0%
GROUP 2	80%	10%	10%	0%
GROUP 3	_____%	_____%	_____%	_____%
GROUP 4	_____%	_____%	_____%	_____%
GROUP 5	_____%	_____%	_____%	_____%

A business that competes against other businesses to sell a soft-drink product to the consumers above should consider all 10 consumer groups to identify which specific groups the business will target.

Because the psychographics of each consumer group are so varied, it is too difficult for one product to properly match the needs of all 10 of the consumer groups shown above. Most companies will identify specific consumer groups to target and then define their product, price, place, and promotion to closely match the needs of those consumers.

For example, a business that targets consumer groups 1 and 2 above should attempt to sell a product at the lowest price in the market. Why? Because consumer group 1 is 100% concerned about Price, and consumer group 2 is 80% concerned about Price. To these groups, Price is the most important factor when choosing which product to buy. A product that is very healthy or tasty but much more expensive is not likely to appeal to these two consumer groups.

A business that targets consumer group 8 should focus on providing a product that is healthier than competing products. Such a product, if priced well, will also likely win sales from consumer group 3. And, possibly consumer groups 6, 7, and 10, which also have Health as a concern.

Price is Always a Concern

Even if a consumer profile has 0% for Price concern, this does not mean that the consumer is willing to pay anything for a product. Nearly all consumers have price concern, even if they are wealthy and can easily afford a product. Price is always a factor.

A consumer profile that has 0% for Price concern should be interpreted as meaning that these consumers put much more emphasis on everything other than price and they will purchase the product that best meets their needs, even if that product is quite a bit more expensive. But, not if the Price is exorbitantly or unreasonably expensive, as compared to other products in the market.

What does exhorbitant or unreasonable mean when it comes to Price? It depends on how closely the more expensive product matches the needs of the consumer and how much other competing products miss the mark.

If the more expensive product perfectly matches the needs of the consumer, while less expensive products completely miss the mark, then it is possible that the consumer will pay double or triple the cost of the other products that miss the mark.

CONSUMER NEED	100% Health	
	PRODUCT A	**PRODUCT B**
PRICE	$2	$2
HEALTH	Very High	Very Low
CLOSEST MATCH TO CONSUMER NEEDS	Perfect match and has no price difference. This product will capture most of the sales.	Does not match needs of consumer as well as Product A, yet is the same price. May only capture few sales.

But, the higher the price difference, the more likely that some consumers may compromise their needs and either choose the less expensive product … or choose not to purchase any product at all, preferring to wait until a product is available that better meets their needs. See the table below.

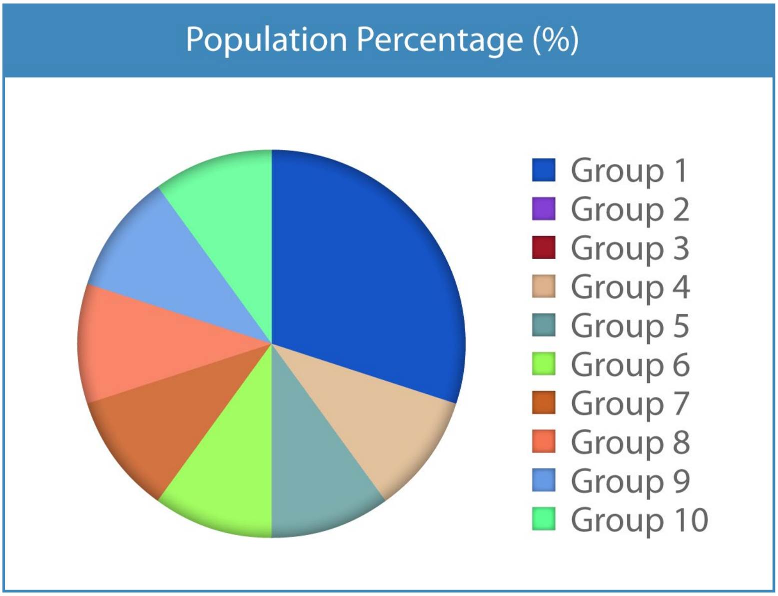
CONSUMER NEED	100% Health	
	PRODUCT A	**PRODUCT B**
PRICE	$4	$2
HEALTH	Very High	Very Low
CLOSEST MATCH TO CONSUMER NEEDS	Perfect match but price is double that of Product B. This product will capture a lot of sales, but will also lose sales to Product B and some consumers may choose not to buy anything.	Does not match needs of consumer as well as Product A, but the much lower price might still attract sales.

Market Size

When considering which Consumer Groups to target, another important factor is the **market demand** or **population percentage** of each individual consumer group.

These numbers show how much of the money spent in the marketplace is spent by each individual consumer group. This is important because it helps you determine if a consumer group is large enough to be profitable. If a consumer group only represents a small percentage of the market, there may not be enough potential sales revenue for your business to be successful.

Or, if more than one company targets the same consumer group, the market demand dollars spent by that consumer group will be split among different products, making it difficult for the companies to be profitable.



In the chart above, consumer group 1 (navy blue) is the largest of the 10 groups, which means group 1 spends the most money. It appears as though group 1 represents over 30% of the entire market.

Consumer group 2 (purple) is so small that it cannot be seen on the chart. Group 2 spends so little money that it may not be profitable for any business to target this group.

With group 1 being the largest of the groups, many companies may immediately target this group. But, keep in mind that if too many businesses target the same group, the market demand dollars spent by that group will be split among the competing products. Targeting smaller groups can also be a profitable strategy, if there are fewer competitors.

Market Data

Where does a business obtain market and consumer data like the type above?

Market data is collected through market research, which may include interviews, surveys, sales results, and other methods for collecting data.

Collecting accurate market data can be difficult, time-consuming, and expensive. Larger companies can afford to purchase or commision market research. Smaller businesses have to find it through more affordable sources, which may include industry associations, media reports, and government statistics.

While it would be ideal for every business to have access to accurate and easy-to-understand market data, the reality is that most businesses make decisions without the benefit of such data. This is one of the inherent risks of business.

9 STRATEGY

Strategy

Strategy is how a business plans to achieve its goals.

There are four steps for a successful business strategy:

1. Define the strategy
2. Make decisions that align with the strategy
3. Evaluate adherence to strategy
4. Adjust the strategy as needed

The 4 Steps

(1) Define the strategy

Defining your business strategy means identifying your primary business goal and then determining how to best achieve the goal.

For example, the primary goal may be **profit**. To be profitable, you have to sell a product at a price that is higher than your cost to make and deliver the product.

You may be competing against other companies offering similar products. You must differentiate your product in the marketplace. And, you must determine the features and price of your product, where you will sell it, and how much you will invest in promotion.

You should consider **consumer profiles** and identify specific **consumer groups** that you will target. You may choose to offer a high quality, high-priced product. Or, you may choose to be the moderate quality, lower-priced product. Or, somewhere in between. Your choice is your strategy.

Review ***§ Consumer Profiles*** *for more insight on this subject.*

Here is a simplified strategy for a soft-drink manufacturing business:

Objective = Net Profit

Pricing = Below Average

Production = Above Average

Taste = Low

Health = High

This suggests that the business strategy is to target consumer groups that want a healthy product, who do not care as much about taste, but also want a less expensive price.

With price below average, you expect that you will sell a high volume of product and therefore production must also be above average.

Complete the table below by identifying if each product feature should be *High*, *Medium*, or *Low* for a soft-drink business that is trying to achieve the strategy shown.

STRATEGY →	Very healthy product but somewhat expensive	Product that tastes great at an average price	Balance of taste and health at an average price
PRICE	___________	___________	___________
HEALTH	___________	___________	___________
TASTE	___________	___________	___________

The next step is to make decisions that align with your strategy.

(2) Make decisions that align with the strategy

Once you have defined your strategy, you must then use your budget money to invest in areas that will enable you to achieve your strategy.

In the example above, the defined strategy is to have a healthy product with no focus on taste. This means you should invest as much money as you think is necessary to have one of the healthiest products on the market, as compared with competing products.

When just starting out, you may not have as much information to know how healthy competing products are or will be, so you will have to make an educated guess at how much you should invest to be close to hitting your target.

For taste, you may want to make little or no investment, since that is not a focus of your strategy. Your budget money may be better used in other areas that align with your strategy.

Using a similar example as above, identify in the table below where your money should be invested. Enter *100%* or *50%* making sure each column adds up to 100%.

STRATEGY →	Very healthy product but somewhat expensive	Product that tastes great at an average price	Balance of taste and health at an average price
HEALTH	________%	________%	________%
TASTE	________%	________%	________%
TOTAL	100%	100%	100%

For production, you have to forecast how many product units you may sell, based on your stated strategy.

> *Review **§ Pricing and Profit** and **§ Market Demand** for more insight on this subject.*

(3) Evaluate adherence to strategy

Once you have actual business and market results, you may now have the data available to evaluate adherence to your strategy.

This means determining if the decisions you made achieved the results you expected. A business cannot assess the effectiveness of its strategy unless it is actually executing on its strategy.

For example, in the strategy above, health was a primary focus. Try to assemble data to determine how your product compares to competing products.

Did you achieve the healthiest product? If yes, then you are on target and adhering to your strategy. If no, then you have to make decisions to help you get there.

Same with taste. Taste was not a focus of your strategy. Have you invested the right amount of money in taste? Not too much?

The table below shows a strategy, the actual results, and whether the strategy is on target or not.

STRATEGY →	Product that tastes great at an average price	
PRICE	Below Average	✗
HEALTH	Average	✗
TASTE	Above Average	✓

Complete the table below by identifying if each item is *On Target* or *Off Target*.

STRATEGY →	Balance of taste and health at an average price	
PRICE	Above Average	___________
HEALTH	Average	___________
TASTE	Average	___________

How were sales? Were your forecasts on target or missed the mark? Did you produce too many or too few products?

Evaluate these and other results to discover if your decisions adhered to your strategy or not. If your decisions did not adhere to your strategy, then it is difficult to determine if the strategy is working or not.

(4) Adjust the strategy as needed

Once you are properly executing on your stated strategy, then the effectiveness of your strategy can be measured by the overall financial results.

Once you have determined adherence to your strategy, make adjustments to align even closer to your strategy and optimize your investments.

For example, take a closer look at health to consider if you may have invested more money than necessary. If your product is the healthiest in the market by a large margin, then perhaps you invested more than you needed to.

9. Strategy

See the example in the table below that shows the action that should be taken based on the results that have been revealed.

STRATEGY →	Product that tastes great at an average price	
PRICE	Below Average	ACTION: Increase Price
HEALTH	Average	ACTION: Reduce Investment
TASTE	Above Average	ACTION: Continue Investment

Complete the table below by identifying that actions that should be taken.

STRATEGY →	Balance of taste and health at an average price	
PRICE	Above Average	______________
HEALTH	Average	______________
TASTE	Average	______________

Determine if your strategy is working or not. If you have adhered to your strategy, but it's not working as well as you had hoped, then consider changing your strategy.

Keep in mind that your competitors are also thinking through this process and may adjust their strategies as well. Their decisions will affect the marketplace and your results. Try to predict what they may do as well, so that you can respond.

Business Strategy Tips

When determining a strategy, keep the following in mind:

- **Understand consumer behavior.**
  If you do not understand how customers make purchase decisions, you will not know how to best position your business to serve their needs.

- **Generally, a business will not have enough cash to be the best at everything** — in the case of a soft-drink business: price, taste, health, and brand. Choose a limited number of features to be the best at.

- **Know the market demographics/psychographics.**
  Consumer profile groups vary in size. Make sure you are targeting a large enough segment of the market to be profitable. For example, if you are running a soft-drink business and you are targeting taste-conscious consumers because your product is the taste leader, make sure this consumer profile group is large enough to make you profitable.

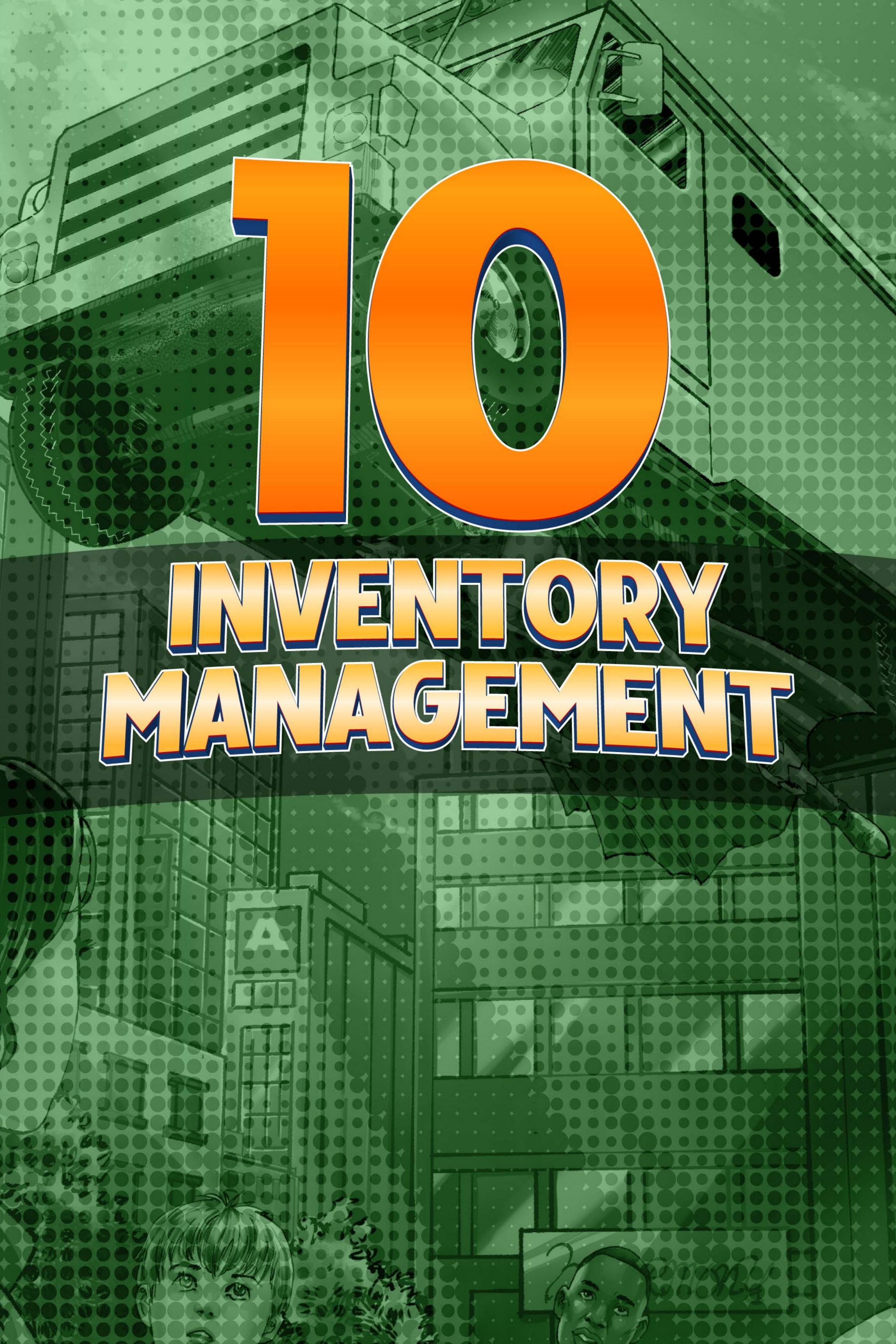
- **Price your products carefully.** Price your products high enough to cover all of your costs (production, distribution, reseller, research and development, sales and marketing), and add an amount of profit that is achievable based on your competitors' prices and product features.

- **Know your competition.** Understanding the strengths and weaknesses of your competitors enables you to better position your business. For example, if you are running a soft-drink business and you notice that a large consumer profile group is health-conscious but your competitors' products are weak in health benefits, then you may want to consider investing heavily to become the health leader.

- **If you are losing money,** it could be for one or more of these reasons: Price is too low; Did not produce enough units to sell; Your product is not as attractive as your competitors'; Too many companies are targeting the same consumer profile group; Insufficient sales and marketing efforts.
- **Consider being contrarian.** If most competitors are pursuing the largest consumer profile groups, the market may become too competitive for profitability (i.e., a big pie that is divided into too many small pieces). Consider pursuing smaller consumer profile groups where you may have minimal competition (i.e., a bigger piece of a small pie).
- **Timing and luck matter.** A great strategy may still fail due to bad timing and luck. You never know when an unexpected event may happen, or a competitor may drastically drop price or pursue some other market-changing strategy.

10

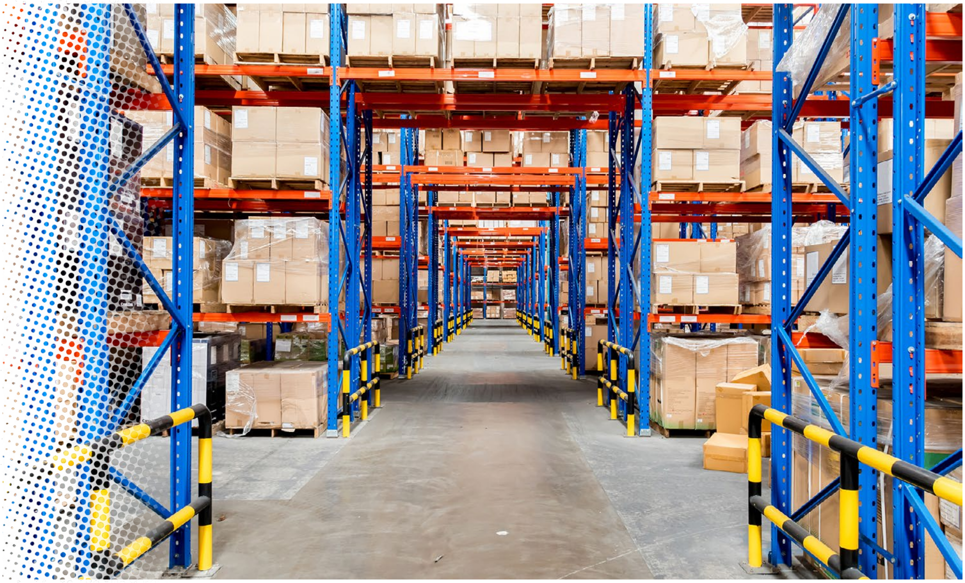
INVENTORY MANAGEMENT



Inventory

Inventory refers to the units of your product that are fully completed and ready to be sold.

Producing (making) products costs money. Having products stored in inventory, unsold, also costs money. Your business objective is to keep your inventory as low as possible, while not missing sales.



Review the table below that shows how unsold products remain in inventory.

UNITS PRODUCED	100	100	100
UNITS SOLD	0	70	100
UNITS IN INVENTORY	100	30	0

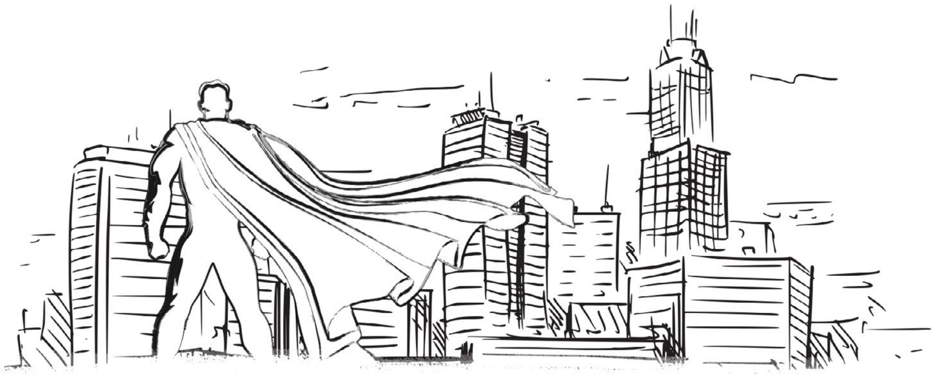
Complete the table below with additional examples.

UNITS PRODUCED	50	800	350
UNITS SOLD	35	650	350
UNITS IN INVENTORY	____________	____________	____________

Producing Too Few Units

If customers want to buy your product but you have no product units in inventory, then you will miss sales and the revenue from those sales. Review the examples in the table below.

UNITS PRODUCED	110	100
CONSUMER DEMAND	100	120
MISSED SALES	0	20
PRODUCT SELLING PRICE	$2	$2
MISSED REVENUE	$0 0 x $2	$40 20 x $2



Complete the table below with additional examples.

UNITS PRODUCED	500	500
CONSUMER DEMAND	300	550
MISSED SALES	________	________
PRODUCT SELLING PRICE	$3	$5
MISSED REVENUE	$ ________	$ ________

Producing Too Many Products

If you produce too many products, meaning more than required to meet the sales demand, then you will have products remaining in inventory.

There are costs and risks to having unsold products in inventory, including:

Cash Flow

The money it costs you to produce the unsold products is now tied up in those products. This money is not lost, as you still have sellable products, but the money cannot be used in other areas of the business.

For example, $10,000 spent to produce products that are unsold could have been used in sales, marketing, R&D, or other business function.

Carrying Costs

This includes costs associated with storing the product inventory, making sure it is secure and undamaged, insurance costs, potential depreciation in value of the product, and more.

For example, a car that is unsold for many months could lose much of its value when a new model year is released. Similarly, a smartphone loses its value when a newer version becomes available.

Spoilage

Nondurable consumer goods, such as food, will expire or spoil after a certain amount of time. The money invested in making a product that spoils before it is sold is completely lost.

The table below shows example costs.

UNITS PRODUCED	100	100	100
UNITS SOLD	0	70	90
UNITS IN INVENTORY	100	30	10
PRODUCTION COST PER UNIT	\$5	\$10	\$50
CARRYING COST PER UNIT	\$1	\$1	\$2
AVERAGE SPOILAGE 10%	10	3	1
COST OF INVENTORY	\$150 100 x \$1 + 10 x \$5	\$60 30 x \$1 + 3 x \$10	\$70 10 x \$2 + 1 x \$50

Complete the table below with additional examples.

UNITS PRODUCED	300	850	1,500
UNITS SOLD	250	780	1,200
UNITS IN INVENTORY	____________	____________	____________
PRODUCTION COST PER UNIT	$10	$20	$50
CARRYING COST PER UNIT	$2	$3	$5
AVERAGE SPOILAGE 10%	____________	____________	____________
COST OF INVENTORY	$ ___________	$ ___________	$ ___________

Forecasting

You should try to produce exactly the number of products you expect to sell. Meeting this objective is difficult because you have to forecast (predict) the future and the future is uncertain. This is one of the many risks in business.

To forecast sales, use current market data and historical sales to help determine estimates, as shown in the tables below.

The following examples use the market demand that you expect to win from the overall market. The following formula is used to determine how many units are expected to be sold:

$$\text{Units Sold} = \text{Market Demand} \div \text{Product Retail Price}$$

MARKET DEMAND YOU EXPECT TO WIN	$100	$500	$15,000
PRODUCT RETAIL PRICE	$2	$10	$150
UNITS EXPECTED TO BE SOLD This is how many you should produce	50	50	100

Complete the table below with additional examples.

MARKET DEMAND YOU EXPECT TO WIN	$200	$700	$40,000
PRODUCT RETAIL PRICE	$5	$25	$150
UNITS EXPECTED TO BE SOLD This is how many you should produce	________	________	________

The tables above demonstrate a method to determine how many products could be sold. You should also review past sales to determine how consistent your forecast is with past market data. Review competitor sales information to gain further insight into sales potential.


11
SALES &
MARKETING

Sales Versus Marketing

Sales and marketing are interlinked, usually done simultaneously, and may be indistinguishable at times. But, there are key differences between sales and marketing.

Marketing generally refers to the activities that need to be done to generate leads or prospects. Leads and prospects are terms used to describe people or organizations that may be likely to purchase your product or service. (Prospect is short for *prospective customer*.)

A person or organization is likely to purchase your product if they have a *need* for the product and the *money* to buy it. They must also have a *desire* to purchase, and that's where Sales comes in.

Sales are the activities needed to directly persuade a lead or prospect to actually buy a product or service.

Marketing generates the leads and sales turns them into purchases.

MARKETING	Generates Leads
SALES	Converts Leads into Sales

Market

A market is all the people or organizations who might buy your product or service, either from you or from a competitor.

A market can be broken down into smaller groups, called **market segments**, of similar potential buyers (sometimes called **consumer groups**).

The graphic below shows the market as the large circle divided into market segments or consumer groups of various sizes.

Market segments might be set up by geographic region, age, gender, economic status, language, family status, or many other descriptive groupings. These descriptions help you develop marketing and sales programs to reach these various groups of potential customers.

Review ***§ Consumer Profiles*** for more details.

Customer Types

Potential customers (prospects) and customers can be segmented into two types:

- **Individuals** who buy goods and services for themselves or for a friend or family member. These types of customers are called consumers or retail customers.

- **Businesses or organizations** that buy goods and services to use in making their own products or making their business run. These organizations include companies, governments, schools, hospitals and other organizations. These are business or organizational customers, and they have different reasons for buying than individual users.

Sales Methods

There are three basic ways to sell your products or services:

Direct Sales
The customer buys your product or service from your business:

- Selling in a retail store.
- Selling with a company sales force or telemarketing group.
- Selling through a company catalog or online.

Distribution Channels
The customer buys your product from another business, your company receives its money from selling to "middlemen," including:

- Selling wholesale to distributors or resellers.
- Selling through sales representatives and partner companies.

Combination
- Using both direct sales and distribution channels.

The table below shows some products and how they are sold.

	DIRECT SALES	DISTRIBUTION CHANNELS
APPLE iPHONE	Apple Stores and Website	Telecommunication Companies
APPLE WATCH	Apple Stores and Website	
COCA-COLA		Convenience Stores, Grocery Stores, Vending Machines, and other outlets
FORD AUTOMOBILES		Automotive Dealerships
TESLA AUTOMOBILES	Tesla Dealerships	

Once you understand where your potential customers are located and how they buy, selecting the right sales methods will be more obvious.

Promotion

There are three ways to promote your company and its products:

Product Line and Brand Advertising
Promotes the overall product line and brand to build awareness and generate sales.

Sales Promotion
Utilizes in-store displays, contests, and other sales tactics to reach the consumer directly.

Price Discount Advertising
Promotes a price discount (or sale) to boost sales. Price discounts are usually temporary and it is advisable to inform consumers about the sale.

Brand

Brand is how people feel about your business or product. The better they feel about you, the more likely they are to try your product and stay loyal to your business.

You cannot dictate how people feel, but you can influence this feeling with your brand personality, brand promise, tone of voice, visual identity, brand associations, and more.

Brand Personality
The *human personality characteristics* that are associated with a brand. For example, RedBull (energy drink) might be considered adventurous or brave, while Ben & Jerry's (ice cream) might be fun or playful.

Brand Promise
The promise for the kind of *experience* people will have with your company or product.

Visual Identity
Visible elements of a brand, including color, form, and shape. Includes color, logo, type, imagery, packaging design, and more.

Tone of Voice
Refers to the *written* word, not *spoken*. The language used, the way sentences are constructed, the order and

sound of words, and the personality communicated. It is not *what* a company says, but *how* it says it.

Brand Association
Relationship to other brands.

Brand is complicated and frequently misunderstood. Two measurable elements of brand are **brand awareness** and **brand loyalty**.

Brand awareness is how well-known your brand is versus the competition. It can be improved by advertising and sales promotion.

Brand loyalty is the likelihood that a customer who has already experienced your product will purchase it again. It can be improved by getting repeat or new customers to purchase your product, with the hope that they will have a positive experience with it.

Territories

Selling your product or service to more geographic **territories** increases your potential revenue opportunities, but comes with additional costs and challenges.

When selling a product or service, you should identify specific geographic territories that you will target. Even though your potential customers could be located anywhere in the world, it is not efficient to spread your sales and marketing investment too widely.

For example, if your product requires knowledge of the English language, spending money on promoting the product in countries where English is not widely spoken may not result in a good return on investment.

Different regions of the world may also have different needs and expectations for a product. This could be influenced by language, culture, economic factors, and more. Your product may or may not align to these needs as well as competing products.

The table below shows examples of products and the territories that may be best to target. Complete the table by indicating *Yes* or *No*.

	UPPER INCOME MOSTLY URBAN	LOWER INCOME MOSTLY RURAL
FITNESS EQUIPMENT	Yes	No
SOLAR PANELS	No	Yes
SPORTS CARS	________	________
FARM EQUIPMENT	________	________

Many countries also have their own monetary **currency**, which adds another complexity to your business as you have to determine the effects of the **currency exchange rates** on your potential costs and profitability.

Entering a new territory often requires additional investment to prepare your product and company to service the new region. And, your business will have different brand equity in each territory that you have to invest in separately to grow.

To identify the best territories to target, you should consider the **market demand** and **consumer profiles**.
This will help you identify the best opportunities that align with your strategy.

Inventory Distribution

When selling a physical product, you have to consider transportation costs and logistics. This becomes more complicated when you sell into multiple territories because you may have to determine how much product inventory to allocate to each territory.

If you allocate too little inventory in a territory, you may miss sales. If you allocate too much inventory, you may increase your costs by having unsold products — and those same products could have helped win sales in another territory. See the example below.

TERRITORY	USA	CANADA
UNITS DISTRIBUTED	110	100
CONSUMER DEMAND	100	120
MISSED SALES	0	20

Complete the table below with additional examples.

TERRITORY	USA	CANADA
UNITS DISTRIBUTED	700	200
CONSUMER DEMAND	750	150
MISSED SALES	________	________

Currency

Many countries have their own monetary **currency**, which adds another complexity to your business as you have to determine the effects of the **currency exchange rates** on your potential costs and profitability.

Review ***§ Currency*** for more details.

Advertising

Advertising is a subset of marketing. Advertisements are messages paid for by those who send them and are intended to inform or influence people who receive them.

For a business, advertising is used to inform consumers about a company and/or its products and services. The objective is to influence consumers to feel good about the company and to buy its products and services.

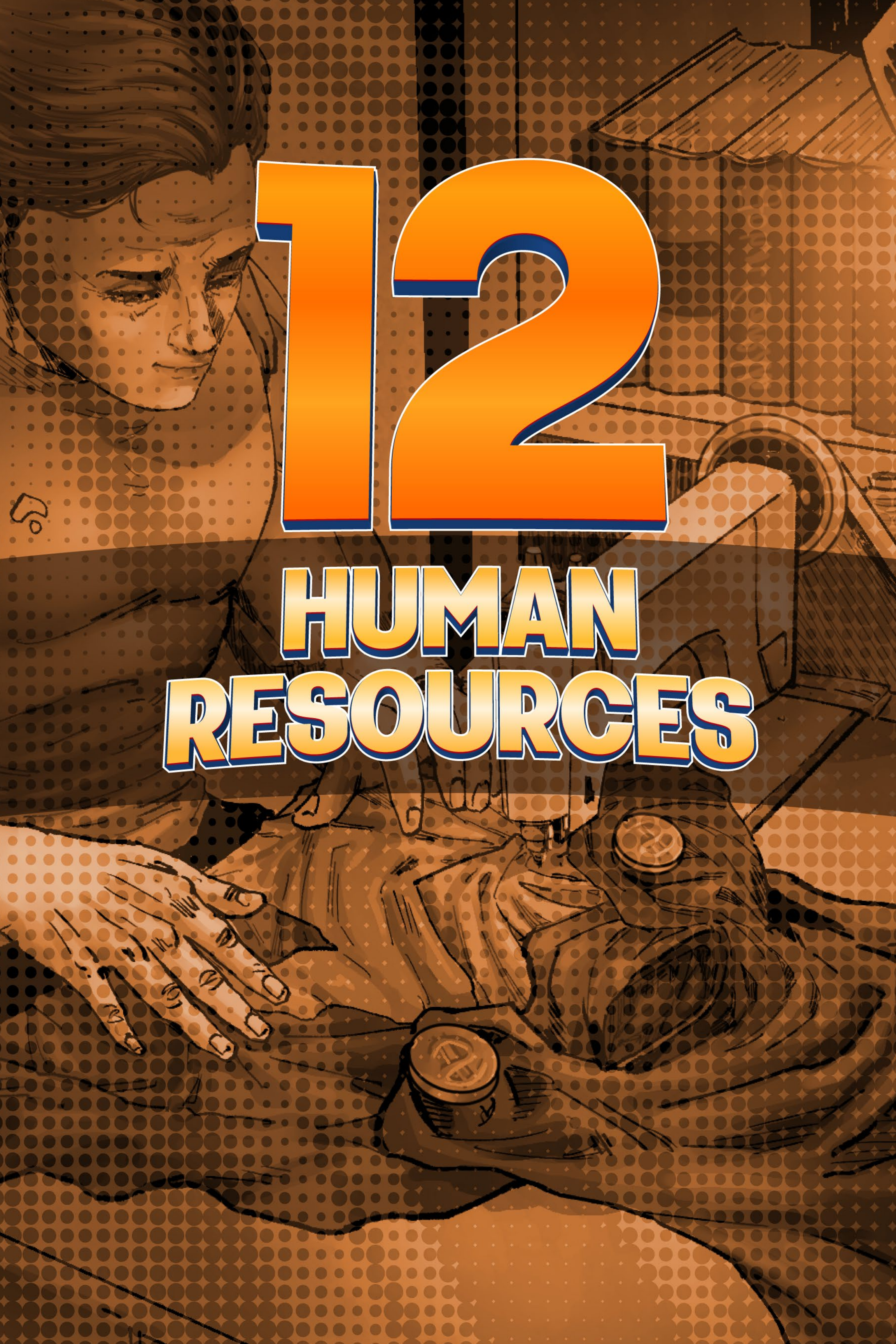
- TV & Video
- Radio, Music, Podcast
- Newspaper
- Magazine
- Direct Mail
- Events
- Sponsorship
- Billboard
- Social Media
- Email

There are many **advertising channels** available to communicate a message. Channels refers to the medium used to communicate the message. Examples are shown below.

Most businesses use one or more channels. How and which channels are used is called the **advertising mix**.

Different channels will reach different consumers, so it is important to understand which advertising channels reach the consumer groups you are targeting. Spending money on advertising that will not directly reach and influence your target consumers is a wasted investment.

12
HUMAN RESOURCES



Employees

Human resources (HR) refers to people hired to work directly for your company. People who work for and in the company are called employees. An employee is someone who does work in exchange for some form of compensation, such as wages. An employer is an individual or organization that provides a job to an employee.

Some people in a company directly manage employees, including their daily work, productivity, morale, and more. Senior executives in larger companies tend to manage business units or business functions, instead of individual employees.

The more customers that a business attracts, the more work that is needed to serve those customers. The maximum number of customers that can be served may depend on the capacity of the business location, the capacity of equipment, and the number of employees working.

Depending on the type of business and product offered, there may be other factors that limit the number of customers that can be served.

Hiring

A business (the employer) can hire employees at any time, as long as it has enough money to compensate the future employees. The first step in the hiring process it to write a job description outlining the details of the job, the skills required to do it, and how to apply for the job.

The job description can then be promoted to encourage people to apply. The wider the job description is promoted, the more likely it is that qualified candidates will be found.

Candidates will submit resumes that the employer can review to identify people that may be most qualified to do the job. The employer can then choose to interview candidates in person or over the telephone or other method. The interview provides an opportunity to find out more about the candidate and for the candidate to find out more about the employer. An employer may also request references that can provide more information about the candidate.

Once a candidate is selected for the job, the employer can submit an employment offer for the candidate to review. If the candidate accepts the employment offer, he or she will become an employee of the business.

It is advisable to document employment relationships in writing to avoid misunderstandings that can lead to financial and legal trouble.

Choosing the right employee for the job is very important for the success of a business and should be done with care. Employers must also be aware of and follow local employment guidelines to assure that candidates for employment and employees are treated properly. Asking a candidate certain questions can even get the employer in trouble.

Managing

Once employees are hired, the employer must be prepared to properly manage them. This means providing appropriate training for the job, scheduling, and ongoing direction.

A business that manages and treats its employees well is more likely to succeed in the long term

Hiring and Severance Costs

Hiring Cost is the cost to hire one new employee, including:

Recruiting
Time and cost to post and promote the job opening, identify candidates, interview candidates, and select someone for the job.

Orientation
Time and cost to introduce the new employee to their job function and the company processes and systems.

Basic job training
Time and cost to train the employee on how to do their job and other tasks related to their role.

Review the example in the table below and complete the final example.

EMPLOYEES HIRED	1	5	8
HIRING COST	$1,000	$5,000	$ ________

Severance Cost is the cost to layoff or fire one employee. Severance Cost varies by company and employee, but could include unpaid vacation pay, unused sick time, compensation for loss of seniority, payment if no advance notice of job loss, and other benefits.

Review the examples in the table below and complete the third item.

EMPLOYEES DISMISSED	1	3	7
SEVERANCE COST	$2,000	$6,000	$ ________

Salary and Benefits

Salary (or wage) is the money paid to an employee for working. Some employees are paid a certain amount of money for each hour they work. Most countries and regions have a minimum wage that must be paid for one hour of work.

Some employees are paid a set salary for consistently working, instead of hourly pay. For example, most full-time employees work 30 to 40 hours each week and may be paid a set salary for the entire year of work — often paid every 2 weeks or once a month.

Part-time employees normally work less than 20 hours each week. The number of hours an employee is expected to work is negotiated between the company and the employee.

Review the example in the table below and complete the final example.

EMPLOYEES	1	3	8
SALARY COST	$30,000	$90,000	$ ________

Benefits and programs are compensation, perks, and incentives that businesses may choose to offer in order to maintain or improve employee morale, loyalty, productivity, recruiting, and turnover.

Review the example in the table below and complete the final examples. The cost of benefits is shown as a percentage of salary.

SALARY COST	$30,000	$40,000	$60,000
BENEFITS COST %	10%	10%	10%
BENEFITS COST $	$3,000	$ ________	$ ________

Employee Morale

Morale represents the emotional well-being and attitude employees have towards their work, work environment, and employer.

Higher employee morale may result in increased job satisfaction, higher productivity, better customer service, reduced absenteeism, lower job turnover, and other benefits.

Employee morale may be influenced by compensation, productivity, work environment, management relations, company reputation, and other factors.

Productivity

Productivity is the labor output, efficiency, or efficient use of an employee, machine, system, materials, etc.

For example, a fast-food restaurant may be able to serve 100 customers an hour with 5 people working in the kitchen. If the restaurant upgrades the kitchen equipment and is able to serve 120 customers an hour, it will have increased productivity by
20% = (120 ÷ 100 – 1) x 100%

Another way to achieve the same productivity increase is for the restaurant to improve its work processes to serve 100 customers an hour with only 4 employees instead of 5. This will result in a productivity increase of **20% = 1 – (4 ÷ 5) x 100%**

Productivity can be more complicated than the simplified examples above demonstrate. Increasing productivity can have negative consequences, such as reducing quality or customer service. Care must be taken to consider all the implications.

Productivity can be influenced by processes, equipment, materials, and many other factors that may have tangible and measurable costs and benefits.

Productivity with employees can be more difficult to manage because of intangible factors. When more employees are needed to accomplish tasks, business costs increase by having to pay more salary and benefits. Sometimes, these additional costs can be justified, while other times there may be inefficiencies that can be improved.

Employee productivity may be affected by **training**, **turnover rate**, and **morale**.

Training
Training an employee can increase their efficiency with completing job tasks and increase confidence and job satisfaction.

Turnover Rate
Reducing and maintaining a low employee turnover rate maintains and increases productivity by not having to continually train new employees. Longer-serving employees can also build their knowledge of the internal workings of the company and their personal expertise in doing their jobs.

Morale
Employees who have higher morale may work faster and smarter to accomplish their tasks.

Turnover

Turnover is when an employee leaves a company, or is laid off or fired.

Employees choose to leave companies for a variety of personal reasons.

Companies choose to lay off employees if they have a shortage of work, financial challenges, a change in strategy, or if the employee is not performing their job as well as required.

Companies may fire employees for misconduct or other reason that justifies dismissing the employee.

Turnover rate is the percentage of employees that leave a business in a year. For example, a business that has 10% turnover means that 10% of all of its employees (such as 10 out of 100) are replaced every year. Companies with high turnover may suggest that employees are not pleased with their compensation, work, or the company.

Review the examples in the table below and complete the final example.

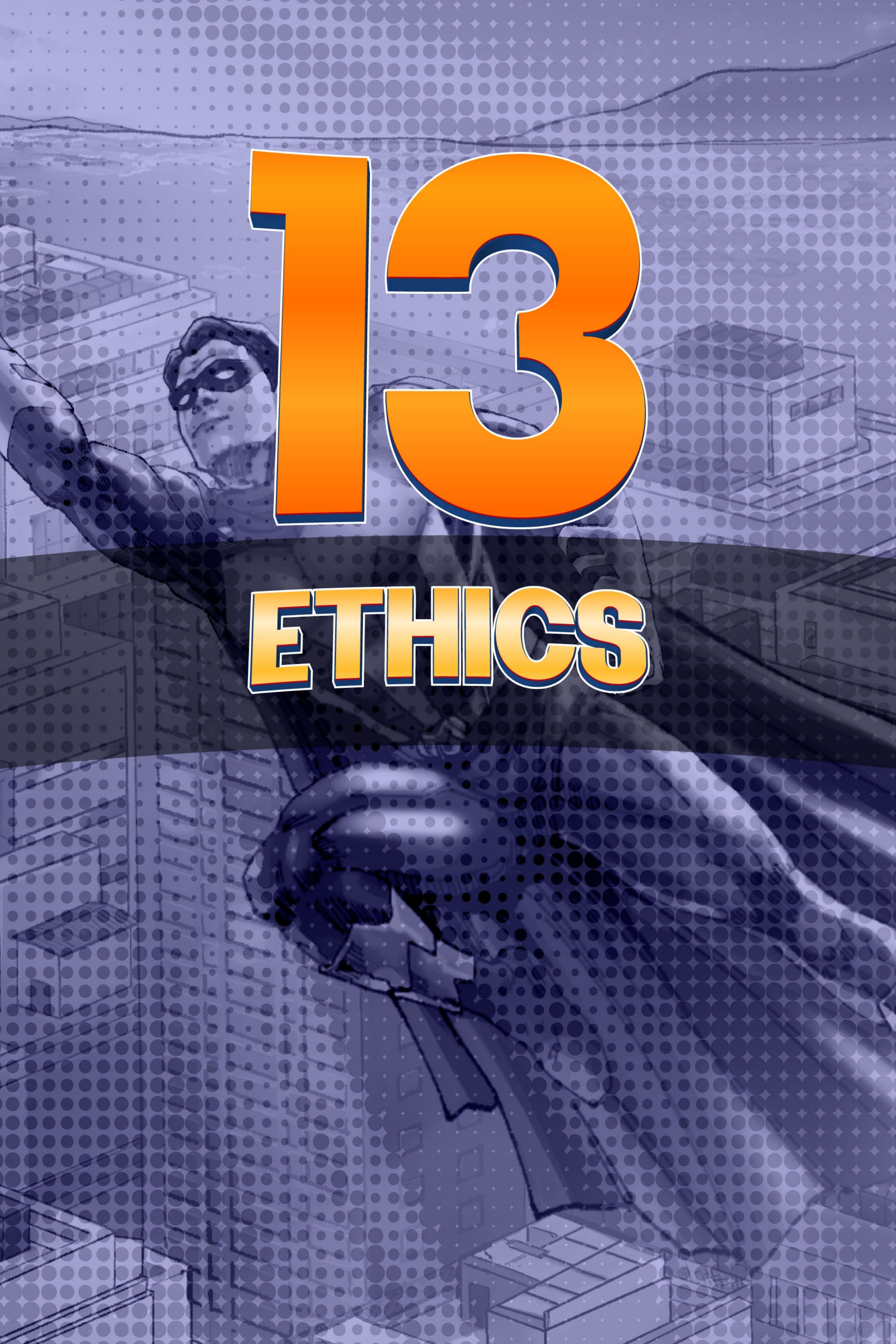
TOTAL EMPLOYEES	100	100	200
TURNOVER RATE	10%	10%	10%
EMPLOYEES REPLACED	10	15	________

Reducing and maintaining a low employee turnover rate saves a company money by not having to incur **hiring costs** each time an employee is replaced, and **severance costs** each time an employee is let go.

Having a low turnover rate may also maintain and increase productivity by not having to continually train new employees. Longer-serving employees can also build their knowledge of the internal workings of the company and their personal expertise in doing their jobs.

13

ETHICS



Business Ethics

Business ethics refers to the values and principles that your company maintains in managing business risks and stakeholder relations.

Stakeholders include employees, customers, suppliers, the community, and more.

Ethics is a key decision that will affect every aspect of your business, internally and externally.

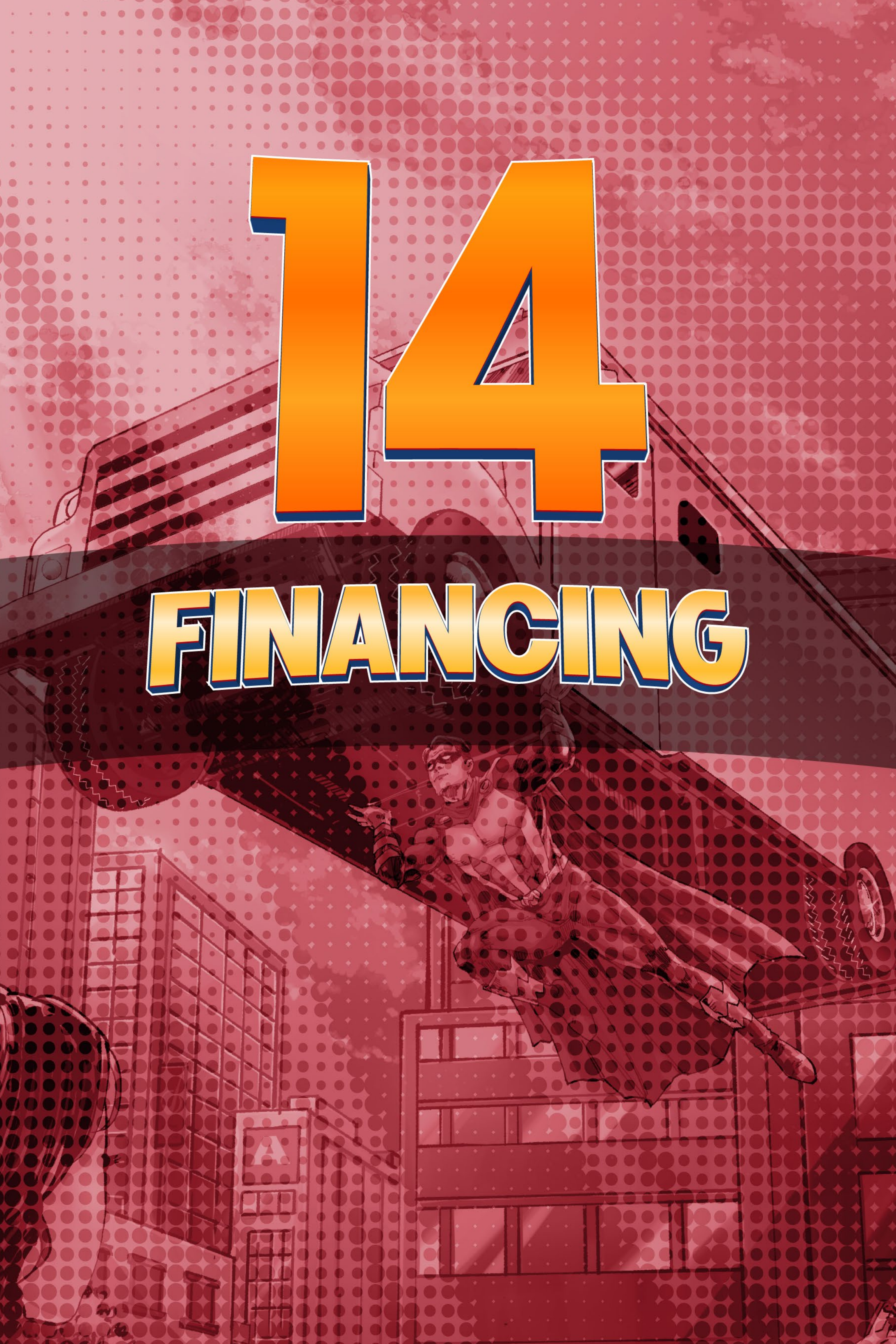
A company that is **ethically weak** is more likely to take advantage of its customers, exploit its workers, and perhaps mislead its shareholders and the public. The result may be short-term financial gain, but with the risk of negative long-term consequences as the weak ethical practices are discovered and exposed.

WEAK ETHICS	BENEFITS	CONSEQUENCES
May take advantage of customers, exploit workers, and mislead shareholders and public.	Short-term financial gain, such as lower costs and maybe more sales from increased brand awareness.	Long-term loss of sales, consumer confidence, brand equity, and exposure to lawsuits.

A company that is **ethically strong** is more likely to be careful and fair in all of its interactions with customers, workers, shareholders, and the public. The result may be increased costs but improved goodwill, customer loyalty, employee retention and commitment, supplier partnerships as well as many other benefits.

STRONG ETHICS	BENEFITS	CONSEQUENCES
More careful and fair in all interactions with customers, workers, shareholders, and public.	Increased brand equity, customer loyalty, employee retention, supplier partnerships, goodwill, and more.	Increased costs required to implement and monitor ethical practices.

14 FINANCING



Business Financing

Financing means money. Businesses often need money to start a business, grow a business, buy new equipment, conduct research and development, expand operations, or achieve other objectives.

Businesses commonly raise money using one or both of these methods:

> **Debt Financing**
> Taking out a loan is debt financing. Debt means borrowing money that must be repaid, often with interest.
>
> **Equity Financing**
> Issuing stock is equity financing. This means selling a share of the business (equity) in return for money. This money is not repaid like a loan. In the real world, a shareholder may be entitled to a share of profits and other benefits. Distribution of profits to shareholders is called issuing **dividends**.

A third method is **grant** financing, but this is less common – more on grant financing below. Entrepreneurs may use their own personal savings to finance a business – this money is usually invested into the company in the form of debt or equity financing.

Debt Financing

Banks and other lenders provide money to businesses in the form of loans. Lenders make their money by charging **interest** on the loan. This means you have to pay back more than you borrow. Normally, a loan is repaid by making monthly payments over a specified period of time (**the term**).

Qualifying for a loan to finance a new business is not easy. Loaning money to new businesses is considered risky because if the business fails, the loan may not be repaid. To reduce the risk, lenders may request that a business loan be personally guaranteed by the owner or be secured with collateral.

A **personal guarantee** is a promise made by the business owner (or an affiliated person) to repay the loan personally, if the business is unable to do so. If the business owner does not have money to repay the loan, the lender could force the sale of personal assets.

Collateral is when a loan is tied to a particular item of value (**asset**). For example, a loan to purchase a home (called a **mortgage**) uses the house as collateral. If the owner cannot pay the mortgage, the lender will take ownership of the house. This is also common with an automobile loan, where the automobile is the collateral.

A loan made to a business may use the business assets as collateral, which may include equipment, inventory, vehicles, trademarks, patents, and other tangible and intellectual property. If the business assets are not of significant value, personal guarantees may be required.

Applying for a Loan

When a business receives a loan, it raises new money that increases cash. Loan terminology:

Loan Principal
The amount of money to be borrowed.

Interest
The extra amount of money to be paid back in addition to the loan principal.

Interest Rate
The interest to be paid, stated as a percentage of the loan principal.

Compounding Period
How often Interest is calculated on the loan.

Payment Period
The frequency in which loan payments will be made.

Amortization Period
The length of time it will take to repay the loan with interest.

Amortization Schedule
The amounts and dates due for each loan payment.

Loan Example

You apply for a loan…

PRINCIPAL	$10,000
INTEREST RATE PER YEAR	10% COMPOUNDED YEARLY
PAYMENT PERIOD	MONTH
AMORTIZATION PERIOD	4 YEARS (48 MONTHS)

When you receive the loan principal, your cash will increase by $10,000. Your loan payments will be withdrawn from cash each month. Each payment includes a portion of principal and interest.

Review the example in the table below that shows how much loan interest is repaid, then complete the other examples.

PRINCIPAL	$10,000	$25,000	$20,000
INTEREST RATE PER YEAR	10% COMPOUNDED YEARLY	10% COMPOUNDED YEARLY	20% COMPOUNDED YEARLY
PAYMENT PERIOD	1 YEAR	1 YEAR	1 YEAR
AMORTIZATION PERIOD	$1,000 $10,000 x 10 ÷ 100%	$ ________	$ ________

Equity Financing

An equity investment is when a person or organization gives money in return for a percentage or share of ownership in a business. The investment does not have to be repaid like a loan, but does have other considerations.

Having investors in a company can be beneficial because it is in their best interest to help the company succeed. But, sometimes investors may try to influence the operations and direction of the company more than the original founders or owners would like.

See ***§ Ownership*** for more details about selling shares or stock in a business.

Equity Example

When raising money by selling shares, a business must determine a share price for the shares. The share price will determine how many shares will be issued to the investors providing the financing or other benefit to the company.

The following formula applies with examples in the table below:

Money Raised = Share Price x Number of Shares

SHARE PRICE	\$1	\$2	\$5
NEW SHARES ISSUED (SOLD)	1,000	1,000	2,000
MONEY RAISED	\$1,000 = \$1 x 1,000	\$2,000 = \$2 x 1,000	\$10,000 = \$5 x 2,000

To raise more money, the number of shares issued has to be increased or the share price has to be increased – or both.

Complete the table below with additional examples.

SHARE PRICE	$3	$5	$10
NEW SHARES ISSUED (SOLD)	1,000	1,000	2,000
MONEY RAISED	$ ________	$ ________	$ ________

Share Price

A business sets its share price based on the total value of the company – called the **company valuation**. Determining the value of a company is a complex topic, but once the value of a company is determined, the share price is easily calculated by dividing the value of the company by the total number of shares issued and outstanding, as follows:

$$\text{Share Price} = \text{Company Valuation} \div \text{Number of Shares Issued and Outstanding}$$

COMPANY VALUATION	$10,000	$50,000	$50,000
SHARES ISSUED AND OUTSTANDING	1,000	1,000	2,000
SHARE PRICE	$10 = $10,000 ÷ 1,000	$50 = $50,000 ÷ 1,000	$25 = $50,000 ÷ 2,000

Complete the table below with additional examples.

COMPANY VALUATION	$60,000	$100,000	$200,000
SHARES ISSUED AND OUTSTANDING	1,000	100,000	2,000
SHARE PRICE	$ ________	$ ________	$ ________

With a public company that is trading on a stock exchange, the price of shares that are already issued and outstanding is set by traders buying and selling the shares on the stock exchange.

However, when raising money, a public company can issue new shares at a price that is different than what is being traded on the stock exchange. Take note that the money used to buy and sell shares on a stock exchange does not go to the company that issued the shares. The money stays with the buyers and sellers, because they are trading shares that were already issued previously by the company (and for which the company has already received money from the person who originally purchased the shares). For a company to raise new money, it must issue new shares from the company.

When a company wants to raise money by issuing new shares, it must find investors who are willing to purchase the new shares at a share price that is agreeable to the investors and the company. This makes determining the value of a company even more complicated and much more than a mathematical exercise.

Earnings Per Share

One of the primary metrics that influences the value of a company is **net profit** – also called **earnings**. When a company makes a profit, it can choose to distribute some or all of the profits to its shareholders – called a **dividend**.

A company that consistently distributes significant profits (dividends) to its shareholders tends to be more desirable to own because shareholders know that they can earn income by owning shares in the business.

Earnings (profit) are distributed to shareholders based on the number of shares owned. For example, a shareholder that owns 10% of the shares issued and outstanding of a company will receive 10% of the earnings that are distributed.

The earnings to be distributed are often described as **earnings per share** — meaning the amount of money to be distributed to each individual share owned. This is calculated as follows:

Earnings Per Share = Total Profit To Be Distributed ÷ Total Shares Issued & Outstanding

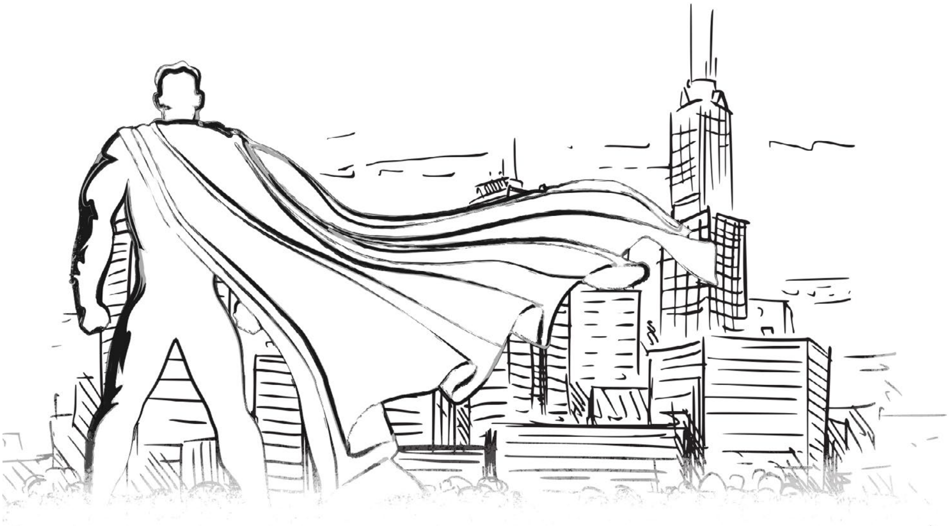
Review the table below and complete the final example.

TOTAL PROFIT TO BE DISTRIBUTED	\$20,000	\$30,000
SHARES ISSUED AND OUTSTANDING	1,000	3,000
EARNINGS PER SHARE	\$20 = \$20,000 ÷ 1,000	\$ ____________

Dilution

Issuing new shares to sell risks negatively impacting **earnings per share** because there will be more shares outstanding. This results in less profit per share, as shown in the table below. Complete the final example.

TOTAL PROFIT TO BE DISTRIBUTED	$20,000	$20,000	$20,000
SHARES ISSUED AND OUTSTANDING	1,000	1,250	2,000
EARNINGS PER SHARE	$20 = $20,000 ÷ 1,000	$16 = $20,000 ÷ 1,250	$ ________



Issuing and selling new shares does not immediately change the current share price because money is provided in return for the shares, as shown in the table below. Complete the second example.

SHARE PRICE	$10	$15
TOTAL SHARES ISSUED AND OUTSTANDING	100	100
COMPANY VALUATION	$1,000 = $10 x 100	$ ________
NEW SHARES ISSUED (SOLD)	20	20
PRICE PER SHARE SOLD	$10	$15
NEW MONEY RAISED	$200 = 20 x $10	$ ________
TOTAL SHARES ISSUED & OUTSTANDING	120 = 100 + 20	________
COMPANY VALUATION	$1,200 = $10 x 120	$ ________

As shown above, even though company value has increased with the new money, the share price has stayed the same because now there are more shares outstanding.

Profit

Raising money by issuing stock or taking out a loan does not increase profit. A business can only generate profit by selling products or services or through grants or investment gains.

Raising money gives a business more money to invest in areas such as sales, marketing, production, and other business functions.

By having more money to invest, a business may be able to generate more revenue and profit. But, if a business does not invest the new money wisely, it could end up losing the money.

Having more money to spend means there is a risk of losing even more money, as shown in the table below. Complete the final example.

BUDGET SPENT	$30,000	$50,000	$60,000
REVENUE	$20,000	$20,000	$25,000
LOSS	–$10,000	–$30,000	–$ ________

Sources of Financing

Sources of financing are the people and organizations that provide money to businesses, as listed below.

Love Money

Money from family and friends is called **love money** and is one of the most common sources of financing for small businesses. Accepting money from family and friends is risky because if the business fails or the money is not repaid, personal relationships can become strained.

Government

Various government departments and agencies want to encourage entrepreneurship and have set up programs to help finance business startup and expansion. Money is usually provided as grants or loans.

Unlike a loan, a **grant** is money that does not have to be repaid. Loans usually have to be repaid, but sometimes they are provided as provisionally repayable. This means the loan only has to be repaid if the business achieves certain milestones or financial success.

Angel Investors

Angel investors are wealthy individuals who invest in private businesses. Angels may provide loans or equity financing. Angels are focused on generating a return on investment. Some angels may also want to help support budding entrepreneurs, and so may be willing to accept an investment that may be higher risk or lower return.

Venture Capital

Venture capital refers to professionally-organized funds that are raised specifically for the purpose of investing in businesses that can generate a high return on investment.

People operate these funds as a business and they are often referred to as **VCs**. VCs generally only buy equity in high-growth businesses – this excludes the majority of businesses. VCs normally invest larger amounts of money, usually in the hundreds of thousands of dollars in a business, but more often in the millions of dollars.

Banks and Other Lenders

Banks and other lenders provide money to businesses in the form of loans. Qualifying for a loan to finance a new business is not easy. Loaning money to new businesses is considered risky because if the business fails, the loan may not be repaid. To reduce the risk, lenders may request that a business loan be personally guaranteed or be secured with collateral.

A number of online services are available that make it easier for new businesses to seek debt financing from people around the world.

Customers and Strategic Partners

A business with a unique product may be able to pre-sell the product to a customer and generate revenue, or other type of financial investment, even before the product is completed. This is not a common method of financing, but it is possible.

A business may also be able to convince another business to finance the new business. The investing business may have a strategic interest in seeing the new business succeed. This can result in the new business acting as a subsidiary of the investing business, or as an independent business of its own.

Crowdfunding

A newer and popular method of raising money to launch a new product or business is through crowdfunding. This involves creating a website or registering with an online service that enables individuals from around the world to pre-purchase a new product that is not yet available for sale, or to invest money in a new business in return for product or equity.

Public Markets

Raising money from public markets normally refers to being listed on a stock exchange or similar service. A new business cannot access the public markets as it must be in business for a period of time and follow specific government and other regulations. Doing so can be quite expensive and does not fit the profile for most businesses. Newer crowdfunding methods may also be considered a type of public financing, but are quite different than stock exchanges.

15

CURRENCY

Global Currencies

Different regions of the world use different monetary **currency**. Currency refers to the system of money used in a country. A **currency symbol** is a sign that represents the Currency. Examples are shown below.

COUNTRY	CURRENCY	SYMBOL
USA	US Dollar	$
CANADA	Canadian Dollar	$
AUSTRALIA	Australian Dollar	$
UNITED KINGDOM	British Pound	£
JAPAN	Japanese Yen	¥
MEXICO	Mexican Peso	$
CHINA	Chinese Yuan or Renminbi	¥

Complete the table below with additional examples. Search the Internet for the answers.

COUNTRY	CURRENCY
FRANCE	
GERMANY	
ITALY	
INDIA	
SOUTH AFRICA	
SAUDI ARABIA	
EGYPT	
PHILIPPINES	
BRAZIL	
ALGERIA	
RUSSIA	

Exchange Rate

Exchange rate is the value of one currency compared to another currency. Not all currencies carry the same value, and the value changes over time.

In the example below, currency A has 20% more value than currency B. If you had 1.00 of currency A, you could exchange it for 1.20 in currency B.

CURRENCY A	1.00
CURRENCY B	1.20

Another example:

US DOLLAR	1.00
CANADIAN DOLLAR	1.20

In the example above, the US Dollar is 20% stronger than the Canadian Dollar.

If you had $1.00 US Dollar, exchanging it to Canadian Dollars would provide you with $1.20 Canadian Dollars (**$1.00 + 20% = $1.20**).

If you had $1.00 Canadian Dollar, exchanging it to US Dollars would provide you with $0.83 US Dollars (**$0.83 + 20% = $1.00**).

Buying or Selling

When doing an exchange rate calculation, you have to know which currency you are selling and which you are buying.

If you have US Dollars and want to convert them to Canadian Dollars, you are *buying* Canadian and *selling* US dollars.

Complete the table below by adding the current exchange rates in comparison to the US Dollar when *selling* US Dollars. Search the Internet for the answers.

COUNTRY	CURRENCY	EXCHANGE RATE SELLING US DOLLARS
USA	US Dollar	1.00
CANADA	Canadian Dollar	________
AUSTRALIA	Australian Dollar	________
UNITED KINGDOM	British Pound	________
JAPAN	Japanese Yen	________
MEXICO	Mexican Peso	________
CHINA	Chinese Yuan or Renminbi	________

Currency can be exchanged at banks and other financial institutions. This can be done in person with cash or online using electronic money transfer and brokerage accounts.

Currency exchange also carries a fee that you must pay for the service, which is normally a few percentage points of the value of the transaction.

Impact of Exchange Rates

The currency where your business is located is often called the **domestic currency**. All other currencies are then considered **foreign currencies**.

15. Currency

When selling into territories that have a different currency than where your business is located, you have to consider the impact that the exchange rates will have on your costs and potential profit. This applies if you are accepting payment from customers in different currencies.

Review the example below.

Your business is located in the US.

The cost to make and sell your product in the US is $5.

You sell your product in the US at a price of $7. This provides you with $2 in profit ($7 - $5).

You sell the same product in Japan and price it at ¥700 in Japanese Yen. You set this price because the current exchange rate is ¥100 for $1 and it will provide you the same profit per product sale as in the US. ¥700 = $7 price.

Exchange rates change all the time and now the Japanese Yen has increased in value to ¥140 for $1.

Your price in Japan still remains at ¥700. But when you make a sale and exchange the ¥700 for US Dollars, the new rate means you will only receive $5 (¥700 ÷ ¥140), instead of the $7 you had received previously. This means you now have $0 profit on this sale.

Your profit is now gone because of the change in exchange rate.

The example above shows what can happen if the foreign exchange rate increases in value in comparison to your domestic exchange rate. The result is that you lose money.

But what happens if the foreign exchange rate reduces in value in comparison to your domestic exchange rate? The result is that you will make more money, as shown in the example below.

Using the same example above but with the Japanese Yen decreasing in value to ¥78 for $1.

Your price in Japan still remains at ¥700. When you make a sale and exchange the ¥700 for US Dollars, the new rate means you will receive $9 (¥700 ÷ ¥78), instead of the $7 you had received previously. This means you now have an additional $2 profit on this sale for a total profit of $4.

Your profit has increased because of the change in exchange rate.

Reducing Risk

What can a business do about fluctuating exchange rates?

From the example above where profit fell, you could consider raising your price in Japan. But, what if raising the price might deter customers from buying? What if there are competing products that are better priced? What happens when the exchange rate changes again? There are no simple answers.

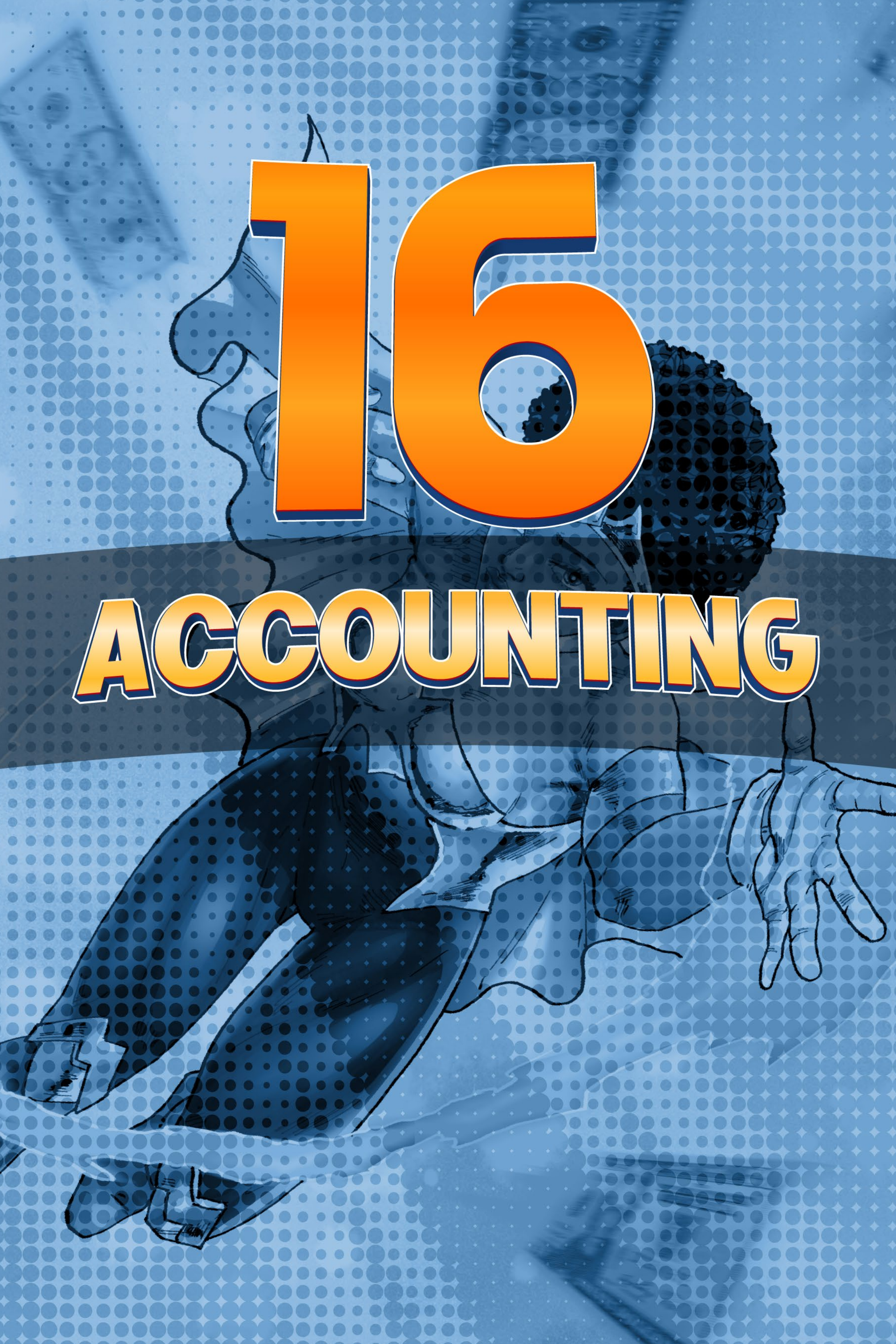
Some businesses choose to sell their product in only one currency. This forces all customers to only pay in that currency. This can work for some online businesses, but does not work for sales that are made in store because people in a particular country normally only carry money in their domestic currency.

15. Currency

Imagine if at a Wal-Mart in the US the prices were all in Japanese Yen — how would consumers react?

Some businesses will set their price on only one currency, but allow customers to purchase in their own domestic currency. You often see this with online businesses where the price may be set using US Dollars but you can choose to pay in a different currency. The online payment system will automatically do the currency exchange rate conversion so the customer can see the price in their own domestic currency before completing the purchase.

16 ACCOUNTING



Business Accounting

Accounting is the process of tracking financial transactions and reporting the results of the transactions.

A financial transaction occurs every time that money or something of value moves in or out of a business. Examples of financial transactions include:

- Making a sale
- Delivering a product to a customer
- Converting raw materials into a finished product
- Buying advertising
- Paying employees
- Receiving loan money
- Making a payment on a loan
- Paying rent
- Buying office supplies
- Collecting taxes
- and more.

Tracking financial transactions is called **bookkeeping**.

Once financial transactions are recorded, financial reports can be generated to display the results of those transactions.

Double-Entry Bookkeeping

Businesses use a system called double-entry bookkeeping to record their financial transactions. This system is believed to have been developed over 600 years ago.

A personal checkbook is an example of a single-entry bookkeeping system. Each time you record a payment or deposit, you write it down once and add or subtract the amount from your bank balance. Each entry will either increase cash or decrease cash.

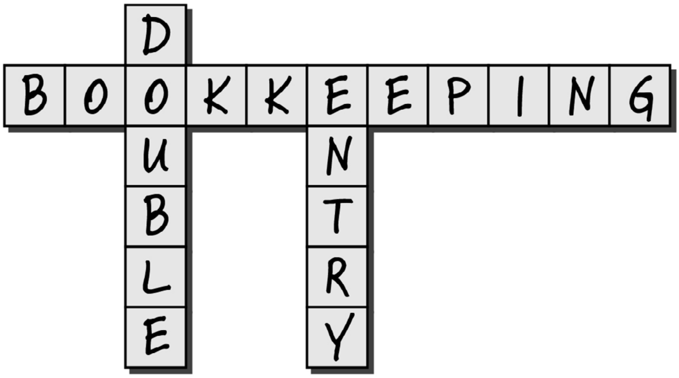
DESCRIPTION	AMOUNT	CASH BALANCE	
		700	
Rent	-500	200	Easy to make a math mistake
Utilities	-125	75	
Paycheck	+1,000	1,075	

It is easy to make a mistake using single-entry bookkeeping. This could result in the balance of money available to be incorrect.

A business needs a system which will not have this potential for error. And, a business has to categorize all its transactions very carefully. Double-entry bookkeeping solves these challenges.

Double-entry means each item gets entered twice – once to record the impact on cash and once to record the category of the transaction.

By recording the amounts twice (in different subtotals), the system tracks finances more carefully and crosschecks the totals to make sure they are the same. This is similar to how a crossword puzzle requires letters to fit both down and across the puzzle.



Below are three transactions recorded using double-entry bookkeeping. Notice how each transaction has two entries – one to show the effect on Cash and the other to show the effect on a related account.

For example, when a business buys an office chair for $50, Cash is reduced by the $50 used to pay for the chair, and Assets are increased by $50 because the business now owns a chair valued at $50. The business did not lose $50. It converted $50 of value from Cash to an Asset.

DESCRIPTION	CASH ACCOUNT	OTHER ACCOUNT
Buy office chair	-50	+50 Assets
Sell product	+100	+100 Revenue
Buy Product to resell	-75	+75 Assets

Double-entry bookkeeping reduces the possibility of error because if an amount is entered incorrectly, it might cause the accounting to unbalance, which can immediately be seen and corrected.

Traditionally, bookkeeping was done using paper books and pen, but most businesses now use accounting software to save time and provide better reporting.

Accounts

A proper accounting system does more than just track cash in and out of a business – it also tracks how cash is used and how any item of value is moved in an out of the business, or changes value within the business.

The example above used three types of accounts – Cash, Revenue, and Assets. Accounts are a way of categorizing financial transactions in accounting.

There are five major categories (or classes) of accounts commonly used in business accounting:

Assets – *Items of value, like cash and product inventory.*

Liabilities – *Debts that the business owes.*

Equity – *Money from selling shares (ownership) in the business and holds retained profit.*

Revenue – *Money received from customers and others.*

Expenses – *Goods and services purchased by the business.*

Each category may have subcategories. For example, Assets could have Cash, Furniture, Equipment, Property, and Product Inventory as subcategories.

Debits and Credits

Every time a financial transaction is recorded in accounting, at least two of the categories above must be modified.

Repeating the earlier example, buying an office chair for $50, Cash is reduced by the $50 used to pay for the chair, and Assets are increased by $50 because the business now owns a chair valued at $50.

DESCRIPTION	CASH ACCOUNT	OTHER ACCOUNT
Buy office chair	-50	+50 Assets

Another way to show the above transaction is to use the accounting terms **debits** and **credits**, as shown here.

ACCOUNT	DEBIT	CREDIT	DESCRIPTION
Cash		50	Buy office chair
Assets	50		Buy office chair

Debit means to *increase* Assets or Expenses and decrease Liabilities or Equity or Revenue.

Credit means to *decrease* Assets or Expenses and increase Liabilities or Equity or Revenue.

In the example above, the Cash account is credited (decreased) by $50 and the Assets account is debited (increased) by $50. The description is the same for both because they form part of the same transaction.

Accounting prefers the terms debits and credits, which are sometimes abbreviated DR and CR. These terms are used to avoid the confusion that could arise with the use of plus, minus, increase, decrease.

	DEBIT	CREDIT
Assets	↑	↓
Liabilities	↓	↑
Equity	↓	↑
Revenue	↓	↑
Expenses	↑	↓

Cash Versus Accrual Accounting

When creating accounting systems for a business, one of the decisions that needs to be made first is whether to use **cash** or **accrual** basis accounting.

The difference between the two methods is the timing of when transactions are recorded in accounting.

With **cash** basis accounting, revenue is recorded when cash is received from customers, and expenses are recorded when cash is paid out.

With **accrual** basis accounting, revenue is recorded when the sale is made, whether or not the cash money is received from customers. Expenses are recorded when they are incurred, whether or not the cash money has been paid out. See examples below.

TRANSACTION	CASH	ACCRUAL
Product sale $100 on January 1. Customer pays on February 1.	Post $100 sale on February 1.	Post $100 sale on January 1. Post again on February 1 when cash is received.
Purchase office chair $50 on January 1. Pay for chair on February 1.	Post $50 expense on February 1.	Post $50 expense on January 1. Post again on February 1 when cash is paid.

Cash basis accounting is simpler but may not give an accurate picture of the company's current financial condition. This is because revenue may be earned on a particular date, but this will not be reflected in the accounting until the cash is received. Similarly, a company may owe a debt that may not appear in the accounting until it is paid.

Accrual basis accounting is the standard practice for most businesses, except for some very small businesses.

Accounts Payable & Receivable

With accrual basis accounting, a business normally uses two accounts to track the purchase and sale of goods when payment is not immediately made:

> **Accounts Payable** is used to record purchases of goods and services made by the business for which the business has not yet paid, but expects to pay within one year. It is a liability that is abbreviated as **A/P**.

> **Accounts Receivable** is used to record sales made of goods or services by the business for which the business has not yet received payment, but expects to within one year. It is an asset that is abbreviated as **A/R**.

With accrual basis accounting, a product may be sold today but payment may not be received for some time in the future. This means the business is owed money and this debt to the business should appear in accounting as an asset until payment is received, at which point it appears as cash.

For example, when a furniture business sells an office chair for $50, this is recorded as Revenue at the time the sale is made. But, if the payment is not yet received, it is posted in Accounts Receivable as money that is due to the company and expected to be received in a few days, weeks, or longer – up to one year (based on whatever payment terms are negotiated).

ACCOUNT	DEBIT	CREDIT	DESCRIPTION
Revenue		50	Sold office chair
A/R	50		Sold office chair

Once the customer pays $50 for the office chair, the furniture company records the payment by moving the $50 from Accounts Receivable to Cash, as shown below.

ACCOUNT	DEBIT	CREDIT	DESCRIPTION
A/R		50	Sold office chair
Cash	50		Sold office chair

The net result is Revenue +50, Cash +50, A/R 0.

The date on which the office chair was sold is different than the date on which payment was received. This time difference is properly tracked with accrual basis accounting and assures that the $50 owed to the furniture business is recorded in accounting from the moment the office chair was sold to the moment payment was received.

With cash basis accounting, Accounts Payable and Accounts Receivable are not used because all financial transactions are posted in accounting when cash is exchanged. So, the time between when a product is purchased or sold and when payment is made or received is not recorded.

Now, consider the above transaction from the customer's point of view, instead of the furniture company. Assuming the Ford company purchases the office chair for use in one of its buildings, the transaction records the purchase of the office chair as an Asset and the money owed for the chair as an Accounts Payable.

ACCOUNT	DEBIT	CREDIT	DESCRIPTION
Asset	50		Buy office chair
A/P		50	Buy office chair

Ford has a new asset in its possession worth $50, but Ford owes the furniture company $50, which is shown as an Accounts Payable liability. Everything balances with $50 in value minus $50 owed for a difference of $0.

When Ford pays for the office chair, Ford moves $50 out of Cash for the payment and reduces Accounts Payable by the same amount because it no longer owes the money and therefore has no liability.

ACCOUNT	DEBIT	CREDIT	DESCRIPTION
Cash		50	Buy office chair
A/P	50		Buy office chair

The net result is Assets +50, Cash -50, A/P 0.

Buying and Selling Products

The examples above describe how a product can be purchased and paid for at a later date. The purchase and payment of a product is normally documented using **order forms**, **purchase orders**, and **invoices**.

Order Form

An order form is a document, online form, or online shopping cart provided by a seller to be used by customers to place orders for products.

An order form includes product names, prices, tax information, and payment options. A buyer submits a completed order form to the seller. Payment may be required at the time the order is submitted, or at some designated time in the future.

Examples:

- In a quick-serve restaurant, a customer places their order at a cash register or self-serve kiosk as soon as they enter the business and pays immediately upon ordering. The food is then prepared and delivered to the customer.

- In a full-service restaurant, a customer will first be seated and then a server will take their order and send it to the kitchen. The food is then delivered to the customer. After the customer has finished their meal, payment will be made.
- When purchasing from an online store, a customer will add products to an electronic shopping cart and then checkout by making a payment. The order is transmitted to the seller to fulfill.

Some businesses allow customers to order and receive a product before they have to pay. This happens in the full-service restaurant above. But in that example, the customer is physically inside the business, so there is a high assurance that the customer will pay the amount owing.

What if the customer is not physically present? How does the seller assure that payment will be made after a product is delivered to the customer?

This is accomplished using a **purchase order**.

Purchase Order

A purchase order (PO) is a document used to place an order for goods or services. The buyer prepares and sends a PO to the seller, indicating the product to be purchased, the price, and payment method. If the seller agrees with the offer in the PO, the seller will provide the product to the buyer.

A PO usually has payment terms where the buyer will receive the product and then have a few days or longer before making payment for the product.

To properly document the delivery of the product and the required payment, the seller will issue an **invoice** to the buyer – more on this below.

A PO is a legally-binding agreement that helps assure that the product requested by the buyer will be delivered by the seller, and that payment will be made by the buyer. While there are no guarantees that everything will go smoothly, this is a common business practice to build trust between parties.

A PO is also a way for a buyer to control who in the organization is authorized to make purchases on behalf of the company. For example, if a company has many employees, normally, only a select few will have the authority to make purchases in the name of the company. By using a valid PO to place an order, an employee is providing the seller with the assurance that they have the authority to act on behalf of the company that is placing the order.

Bill and Invoice

When a customer eats at a full-service restaurant, they place an order for their food. Sometime later, the customer is given a **bill** – a document that lists the goods and services consumed with a total cost that they are expected to pay. The goods and services were delivered and payment is due immediately.

Similarly, a telephone company provides communications services and then issues a bill to the customer for payment.

A bill is also called an **invoice**. The terms are often used to mean the same thing, but for accounting purposes a business that provides a product and expects to be paid will issue an invoice to a customer. The customer that receives the invoice records the invoice as a bill.

Accounts Receivable (seller) records invoices
Accounts Payable (buyer) records bills

Another example to demonstrate the distinction between a bill and an invoice is with a restaurant. The customers who buy from the restaurant are issued bills by the restaurant. The suppliers who provide food and drinks to the restaurant will issue invoices to the restaurant – and the restaurant considers these as bills.

When a business sells a product for which it is not immediately paid, it is common for the business to issue an **invoice** to the customer.

An invoice is a document that includes the following information:

- The word INVOICE prominently displayed.
- Invoice number – unique for every invoice.
- Name, address, and telephone number of the business issuing the invoice.
- Name and address of the customer.
- Date of invoice, which is usually when the product was given or delivered to the customer.
- Name or description of the product sold.
- Quantity of product sold.
- Price of the product, including discounts, taxes, and fees.
- Payments made by the customer, if any.
- Terms describing when the remaining payment is due.

INVOICE

BILL TO

CUSTOMER NAME
345 King Street
Springfield, ON, 92181

COMPANY LOGO

COMPANY NAME
123 Main Street
Springfield, ON 92173
555.902.4567

INVOICE # 1001
TERMS: NET 30
INVOICE DATE: OCT 1, 2020
DUE DATE: OCT 31, 2020

ITEM	QUANTITY	PRICE	AMOUNT
PRODUCT NAME OR DESCRIPTION	2	$10.00	$20.00

TAX $3.00
TOTAL DUE $23.00

Payment terms are often described as Net 30, Net 60, or other timeframe. *Net* means the remaining balance owing. 30, 60 or other number means the number of the calendar days by which the full payment is due.

Receipt

A receipt is a document that confirms that something of value has been transferred from one person or organization to another.

Most often, receipts are issued by businesses to customers when a payment is made by the customer. A receipt normally includes the amount paid, the name or description of the product or item of value purchased by the customer (transferred), the date of the transaction, and how payment was made.

RECEIPT

RECEIPT # 1001
DATE: OCT 31, 2020

COMPANY LOGO

COMPANY NAME
123 Main Street
Springfield, ON 92173
555.902.4567

ITEM	QUANTITY	PRICE	AMOUNT
PRODUCT NAME OR DESCRIPTION	2	$10.00	$20.00

TAX $3.00
TOTAL $23.00

PAID CASH

Financial Statements

Financial statements report the current and past financial state of the business. Proper accounting makes it easy to generate accurate reports for many aspects of a business.

There are three primary financial statements for a business:

Balance Sheet, **Income Statement** (sometimes called a Profit and Loss or P&L), and **Cash Flow** statement.

Cash Flow Statement
Shows the timing of money flowing in and out of the business. This report is particularly important in helping make sure the business does not run out of money, unexpectedly.

Income Statement
Shows all of the money flowing in and out of the business to determine if the business is profitable or not.

Balance Sheet
Shows the value of the business by adding up everything the business owns and subtracting everything that the business owes. The actual value of a business is often more complex than the Balance Sheet shows, but the Balance Sheet provides an accurate view of its financial position.

The reports above are described in detail, further in this book.

General Ledger

The **General Ledger (GL)** provides a record of each financial transaction that takes place during the life of an operating company.

Accounting accounts appear in the General Ledger, with each account showing the debits and credits made on the account and the running balance.

A **trial balance** can be generated from the General Ledger that shows the balance of each account. The balance of debits and credits can then be compared to assure they are identical and that the accounting is mathematically correct.

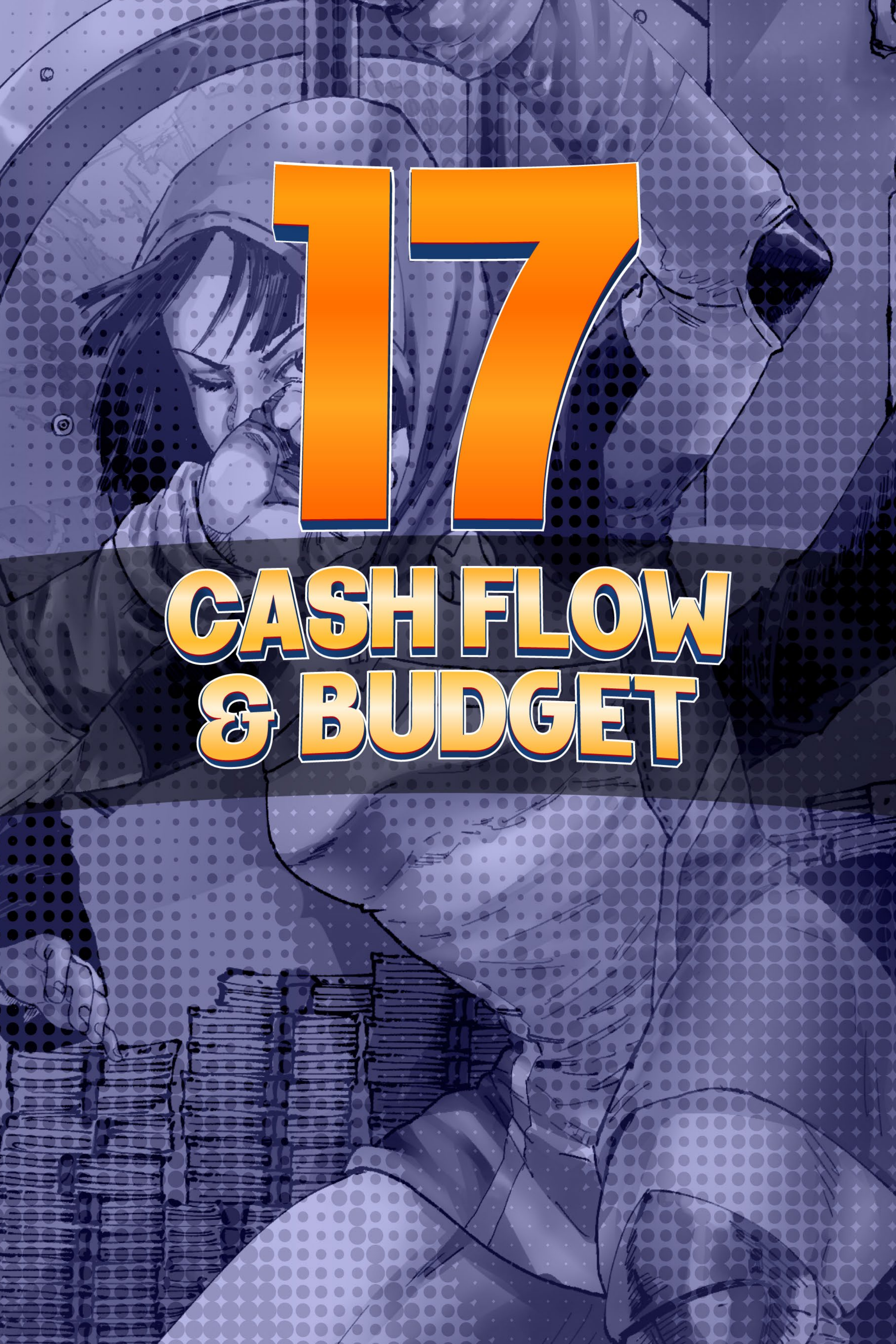
Accounting Standards

Accounting rules may vary based on the different standards used around the world.

Businesses in the USA, Canada, and some other countries use **Generally Accepted Accounting Principles** – **GAAP**.

The **International Financial Reporting Standards** – **IFRS** – is another common standard used in many countries.

There are several other less-popular standards.



17

CASH FLOW & BUDGET

Importance of Cash

Running out of money (**cash**) is the most severe problem a business can face. Without money, employees cannot be paid, products cannot be made or shipped, customers cannot be served, and everything eventually comes to a full stop.

Managing cash is of critical importance. Proper planning is needed because the timing of when cash is received by a business and when it has to be paid out is constantly changing. This is particularly challenging when a business is not profitable and has more cash going out than coming in.

Cash Flow

Money flowing in and out of a business is described as **cash flow**:

Cash Flow = Money IN – Money OUT

Money IN
All sources of incoming cash, such as **revenue** and other **income**.

Money OUT
Everything that requires money to be paid.

MONEY IN	
REVENUE	$15,000
OTHER INCOME	$1,000
TOTAL	**$16,000**

MONEY OUT	
MANUFACTURING	$5,000
SALES & MARKETING	$4,000
WAGES	$3,000
OPERATIONS	$2,000
OTHER	$1,000
TOTAL	**$15,000**

CASH FLOW	
MONEY IN	$16,000
MONEY OUT	$15,000
MONEY IN – MONEY OUT	**$1,000**

Knowing how much money is coming in and going out is important, but equally important is knowing the timing of when money is coming in and going out.

Timing can be difficult to predict because it is not always known exactly when customers will pay bills, or other payments will be made.

Even very successful businesses can run into cash flow problems.

Cash Flow Statement

A **Cash Flow** statement is a report that projects the timing of money in and money out in the immediate future. The report includes a time **period** and **duration**. The period is the segments of time in which the report shows money IN and money OUT – such as weekly, monthly, quarterly, or other time period. The duration is the length of time in the future being projected.

Most often, Cash Flow statements use monthly periods projected 12 months into the future. Review the example in the table below that projects three months forward.

CASH FLOW	JAN	FEB	MAR
MONEY IN	$16,000	$14,000	$15,000
MONEY OUT	$15,000	$16,000	$15,000
MONEY IN – MONEY OUT	$1,000	- $2,000	$0

Complete the table below with additional examples.

CASH FLOW	APR	MAY	JUN
MONEY IN	$13,000	$14,000	$15,000
MONEY OUT	$12,000	$12,000	$17,000
MONEY IN – MONEY OUT	$ ________	$ ________	$ ________

Cash Flow statements include one more important item – a running balance of the cash surplus or deficiency. Review the example in the table below where the Balance for the current month is added to the total Balance of all the previous months.

CASH FLOW	JAN	FEB	MAR
MONEY IN	$16,000	$14,000	$15,000
MONEY OUT	$15,000	$16,000	$15,000
MONEY IN – MONEY OUT	$1,000	- $2,000	$0
BALANCE Starting Balance = $0	$1,000 = $0 + $1,000	- $1,000 = $1,000 – $2,000	- $1,000 = – $1,000 – $0

In the example above:

- January Balance equals the Starting Balance of $0 plus the result of January $1,000 for an ending Balance of $1,000.
- February Balance equals the Balance of January $1,000 plus the result of February – $2,000 for an ending Balance of – $1,000.
- March Balance equals the Balance of February – $1,000 plus the result of March $0 for an ending Balance of – $1,000.

17. Cash Flow and Budget

Complete the table below.

CASH FLOW	JAN	FEB	MAR
MONEY IN	$22,000	$21,000	$18,000
MONEY OUT	$20,000	$20,000	$20,000
MONEY IN – MONEY OUT	$2,000	$1,000	- $2,000
BALANCE Starting Balance = $0	$ ________	$ ________	$ ________

In the examples above, the Starting Balance was $0. This makes it easier to see if future projections will result in a surplus or deficit. Sometimes, a business will use its actual cash balance in the Cash Flow statement as this makes it easier to see if the business risks running low on cash.

Repeat the example above using a Starting Balance of $2,000.

CASH FLOW	JUL	AUG	SEP
MONEY IN	$22,000	$21,000	$18,000
MONEY OUT	$20,000	$20,000	$20,000
MONEY IN – MONEY OUT	$2,000	$1,000	- $2,000
BALANCE Starting Balance = $2,000	$ ________	$ ________	$ ________

Budget and Cash

Budget is an amount of money a business has reserved to invest in a project or business function in a given period of time – week, month, quarter, year.

Budget is not money already spent – it is money set aside to be spent. Examples:

- Budget $10,000 to spend on an advertising campaign in the month of February.
- Budget $5,000 to conduct a market research survey.
- Budget $100,000 to develop a mobile app.
- Budget $20,000 to spend on the purchase of new furniture during the calendar year.

Using budgets serves three purposes:

1. Knowing how much money could be spent on individual activities within the company helps the business manage cash flow and the overall cash available in the business. In basic terms, it helps the company avoid running out of money, or spending more money than desired.
2. Budgets help guide the people who will be spending the money on the project or business function for which they are responsible. By having a specific budget, the scope of the effort can be scaled so that the desired goal is achievable with the money available.
3. Helps the business measure and compare results, which helps with future decision making.

Budget should not be confused with cash. Cash is the amount of money a business has available, often in bank accounts and short-term liquid investments.

Budget is taken from cash, but is usually only a small portion of the cash available in the business. Cash is needed to operate a business and a good amount of cash needs to always be available to provide working capital for the business. This is why the budget is only a small portion of cash.

CASH	$100,000
BUDGET	$20,000
BUDGET AS % OF CASH	20%

The board of directors and management of a company determine how much cash is allocated to individual budgets. A company may have many budgets for different activities that the business must undertake.

Over and Under Spending

Once a budget amount is set aside for a specific activity, should the entire budget be spent on that activity? The best answer is that as much of the budget should be spent as is necessary to achieve the desired goals.

Achieving a specific goal may require the full budget or only a portion of it.

Spending more money in certain business functions can increase the opportunity to make more profit, but it can also risk losing the business more money.

For example, investing more money to produce more products provides a business with more products to sell and thereby the opportunity to generate more revenue. But, if the business does not sell all of the extra products produced, the business may end up losing money.

Similarly, spending more money on sales and marketing could help generate more sales. But, if the business strategy does not work, then all of that extra money spent on sales and marketing will be lost.

MONEY INVESTED	\$20,000	\$20,000	\$20,000
SALES REVENUE	\$25,000	\$18,000	\$8,000
PROFIT (LOSS)	\$5,000	- \$2,000	- \$12,000

Complete the table below with additional examples.

MONEY INVESTED	\$50,000	\$30,000	\$18,000
SALES REVENUE	\$52,000	\$45,000	\$8,000
PROFIT (LOSS)	\$ ________	\$ ________	\$ ________

In business, spending money always offers you both opportunity and risk.

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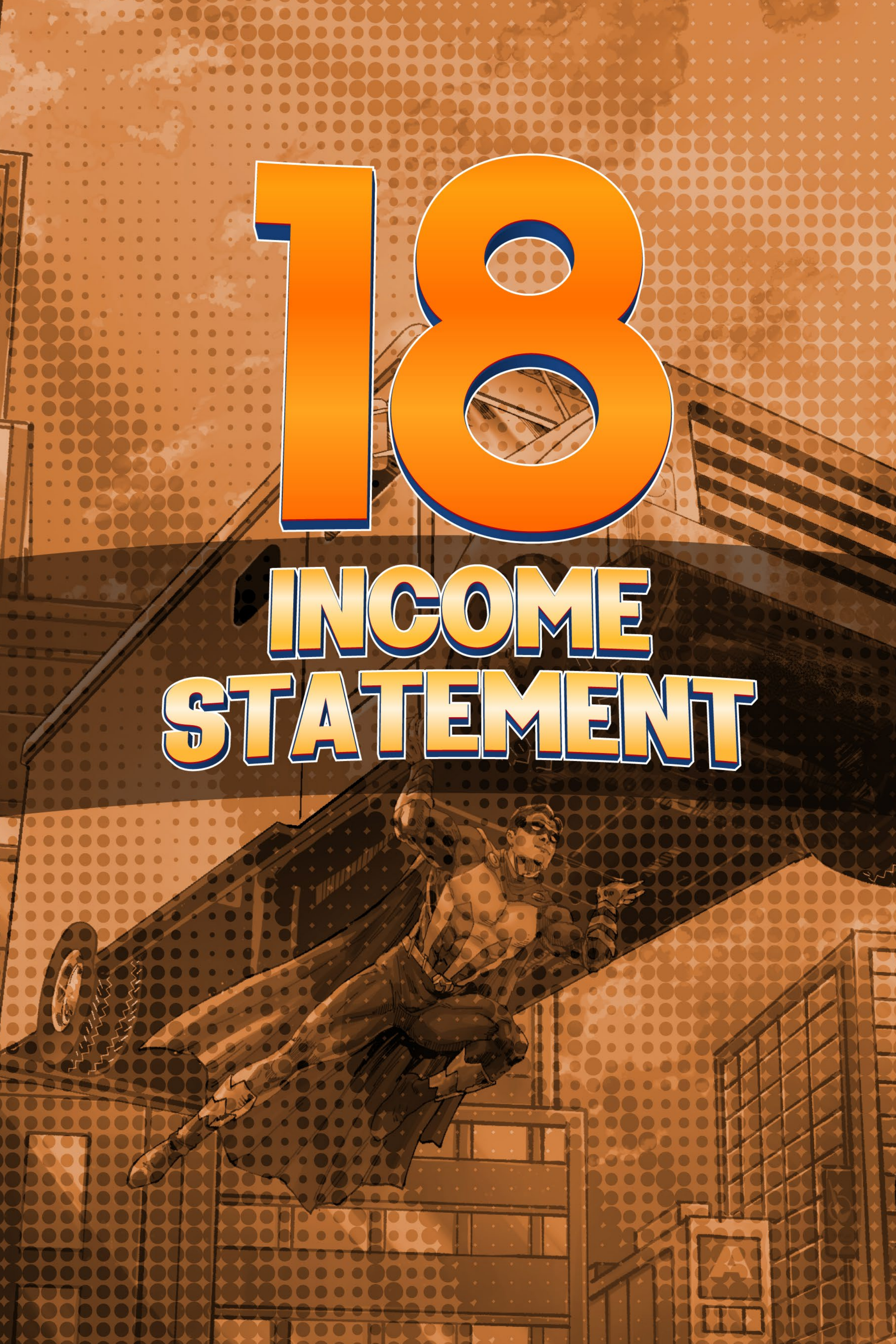
INCOME STATEMENT



Financial Statements

There are two primary financial statements for a business:

Balance Sheet and the **Income Statement** (sometimes called a Profit and Loss or P&L).

The **Income Statement** shows all of the money flowing in and out of the business to determine if the business is profitable or not.

The **Balance Sheet** shows the value of the business by adding up everything the business owns and subtracting everything that the business owes. The actual value of a business is often more complex than the Balance Sheet shows, but the Balance Sheet provides an accurate view of its financial position.

Revenue and Expenses

To understand the **Income Statement**, you must first understand some key definitions.

Revenue or Income
This is money earned by selling a product or service. You receive this money directly from end consumers, resellers, or distributors.

Cost of Goods Sold (COGS)
The cost to produce the products you have sold are recorded as COGS. For clarity, COGS is only for products that have been sold, not for products that are in inventory and not yet sold.

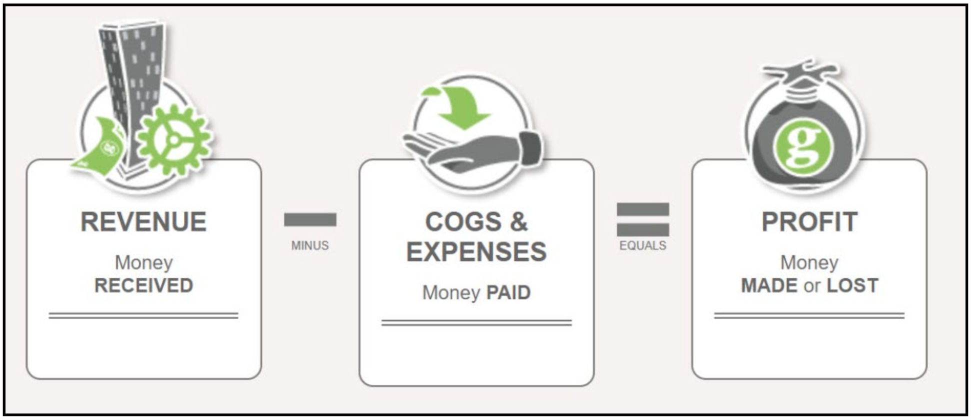
Expenses
This is money paid out to sell your products and operate the business. It can include employee wages, sales and marketing expenses, interest on loans, and more.

Profit
This is the money generated from your business activity that exceeds the costs of the business. If revenue minus COGS minus expenses is positive, it means you have generated a profit. If it is negative, you have losses. Profit is also called earnings.

The Income Statement adds up all the revenue, COGS, and expenses and applies this formula:

Revenue – COGS – Expenses = Profit

If the formula above results in a positive number, then the business has generated a profit. If the number is negative, then the business has suffered losses. Here is the Income Statement formula visually:



Here is an example that applies the Income Statement formula:

Revenue – COGS – Expenses = Profit

REVENUE $5,000	Product Sales $5,000
COGS & EXPENSES $3,000	COGS $1,000 Expenses $2,000
PROFIT $2,000	$2,000

The business above has generated a profit of $2,000.

Complete the table below with additional examples.

REVENUE	Product Sales $8,000	Product Sales $6,000 Sale of Services $2,000
COGS & EXPENSES	COGS $2,500 Expenses $1,000	COGS $3,000 Expenses $6,000
PROFIT	$ ____________	$ ____________

If profit is negative, the company has suffered a loss. Losses in accounting are sometimes shown with negative numbers or numbers in parenthesis, like this:

– $100 or ($100)

Both of the above mean negative $100 or a loss of $100.

Net Profit and Gross Profit

The Income Statement often shows two different profit numbers: Gross profit and net profit.

Net Profit is as described above, using the P&L formula:

Revenue – COGS – Expenses = **Net** Profit

Gross Profit uses this formula:

Revenue – COGS = **Gross** Profit

Gross profit is the revenue generated from product sales minus the cost of good sold (COGS). Unlike net profit, gross profit does not account for other expenses, like sales and marketing, operations costs, interest paid, and more.

See the example below.

Revenue	\$5,000	
COGS	\$1,000	
	\$4,000	= Gross Profit
Expenses	\$3,000	
	\$1,000	= Net Profit

Net profit generally means the final, bottom line, profit. This is also called earnings.

Complete the table below with additional examples.

REVENUE	$8,000	$6,000
COGS	$2,500	$3,000
GROSS PROFIT	$ ______________	$ ______________
EXPENSES	$2,000	$4,000
NET PROFIT	$ ______________	$ ______________

COGS and COS

Cost of goods sold (COGS) is normally used to refer to physical products (goods).

When selling services, the term **cost of sales** (COS) is often used instead.

Cost of revenue is also a common term, and could apply to both goods and services.

COGS normally includes all costs associated with producing a product. This includes raw materials, parts, assembly, and the transportation costs to bring everything together. Human labor costs needed to make the product are also included in COGS.

Costs that are not *directly* associated with making a product are not included in COGS. This includes sales and marketing, financing costs, employee wages that are not involved in the making of the product, and more. These are all considered Expenses not COGS. And, COGS only includes the costs of products that are already sold, not the cost of products that remain in inventory.

The concepts above also apply to services and cost of services.

Other Income

Sometimes, a business will generate money (revenue or income) in ways that are not part of its primary business. This money is normally classified as **other income**.

For example, a company that makes and sells widgets as its primary business may also earn income from interest on the money it has in the bank. The company may also receive a government grant (a grant is a financial incentive that does not have to be repaid).

This new money that is not derived from the primary business is classified as Other Income, and appears on the Income Statement as shown below.

Revenue – COGS – Expenses + Other Income = **Net** Profit

REVENUE $5,000	Widget Sales $5,000
COGS & EXPENSES $3,000	COGS $1,000 Expenses $2,000
OTHER INCOME $1,500	Bank Interest $1,000 Grant $500
NET PROFIT $3,500	$3,500

Complete the table below with additional examples.

REVENUE	Widget Sales $7,000	Widget Sales $6,000
COGS & EXPENSES	COGS $3,000 Expenses $2,000	COGS $5,000 Expenses $3,000
OTHER INCOME	Bank Interest $750 Grant $750	Bank Interest $1,000 Grant $1,000
NET PROFIT	$ ________________	$ ________________

Period

When generating an Income Statement, you have to choose two dates: The starting (From) date and the ending (To) date. The data that will be displayed will include all transactions between and including the dates you select.

Retained Earnings

An important term that appears in financial statements is **retained earnings**.

Earnings is another word for net profit.

“Retained” means held or kept.

Retained earnings is net profit that remains in the company — as opposed to profit or earnings that are paid out to company shareholders.

Some companies will pay out a portion of net profits to the company owners (the shareholders). This payout is called a **dividend**.

When a dividend is paid, the net profits held (retained) in the company are reduced. This means the retained earnings are reduced.

Retained earnings are a running total of all the profits accumulated and held in a business. The Income Statement may show both the net profit of the current time period, and the cumulative net profit from the entire history of the company.

The table below shows how retained earnings is a running total of the profits from past years and the current year.

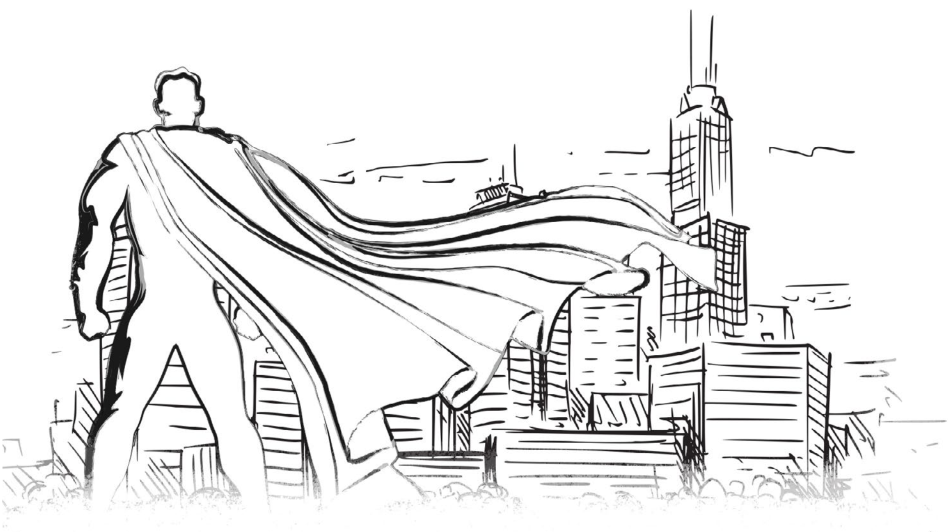
	YEAR 1	YEAR 2	YEAR 3
NET PROFIT	\$1,000	\$2,000	\$1,500
RETAINED EARNINGS	\$1,000	\$3,000 = \$1000 + \$2,000	\$4,500 = \$3,000 + \$1,500

The table below shows how dividends paid out will reduce retained earnings.

	YEAR 1	YEAR 2	YEAR 3
NET PROFIT	\$1,000	\$2,000	\$1,500
DIVIDENDS	\$0	\$500	\$1,000
RETAINED EARNINGS	\$1,000	\$2,500 = \$1000 + \$2,000 - \$500	\$3,000 = \$2,500 + \$1,500 - \$1,000

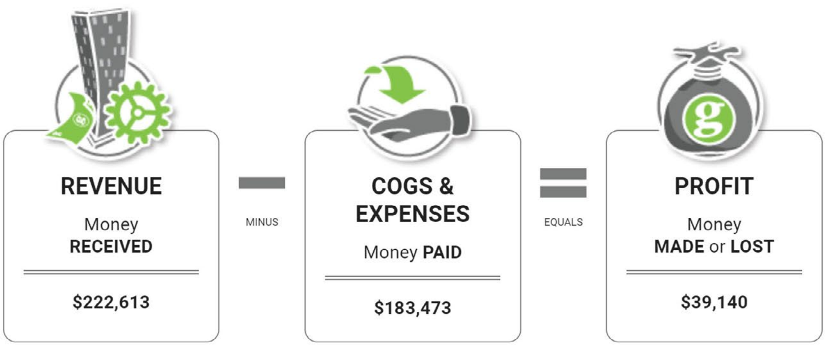
Complete the table below with additional examples.

	YEAR 1	YEAR 2	YEAR 3
NET PROFIT	$2,000	$4,000	$3,000
DIVIDENDS	$0	$1,000	$2,000
RETAINED EARNINGS	$ ________	$ ________	$ ________



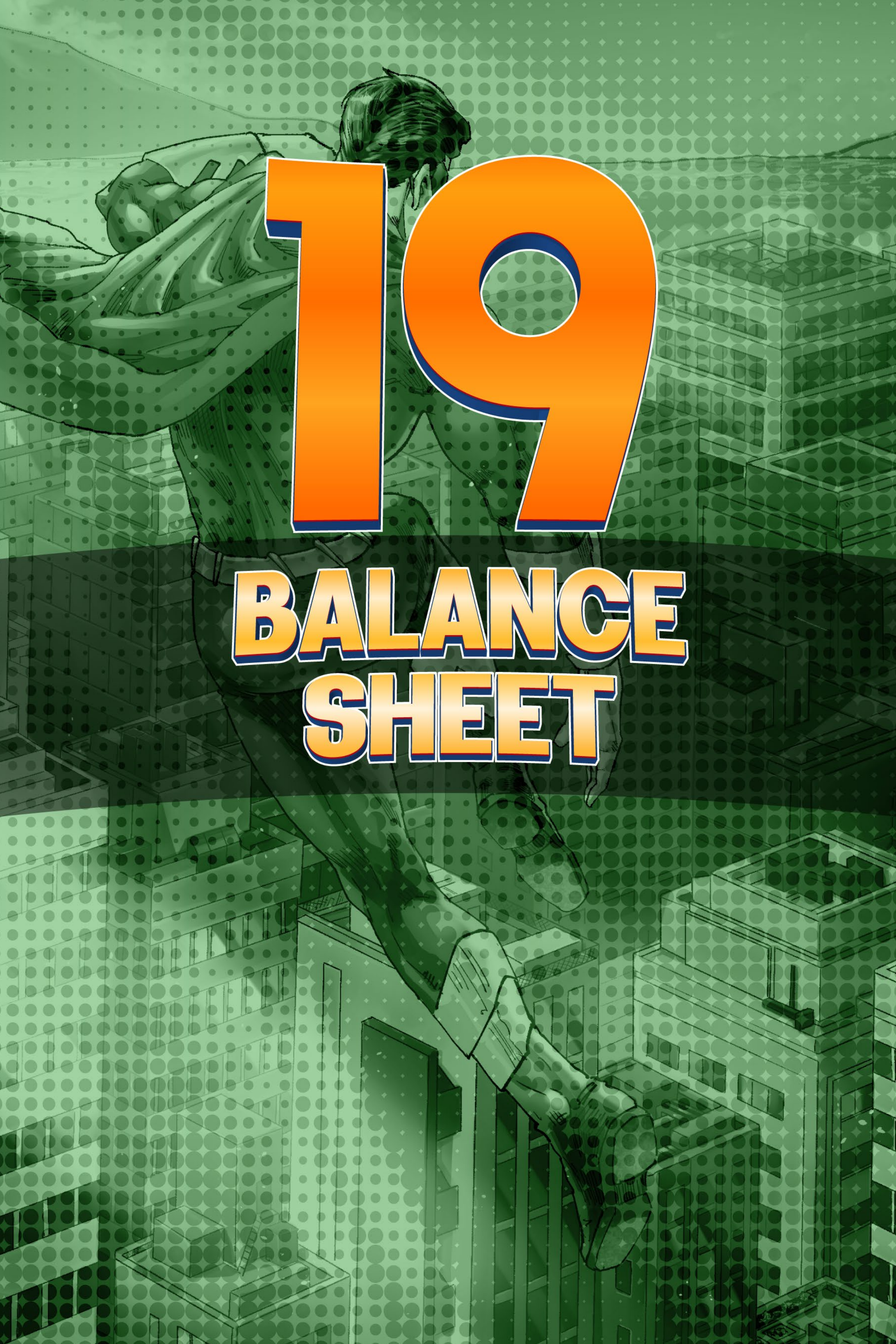
Sample Income Statement

Income Statement



Revenue	
Sales Products	$212,613.03
Sales Services	$10,000.00
Other Income	$0.00
Total Revenue	**$222,613.03**
Cost of Goods Sold (COGS)	
Production & Inventory	$57,482.49
Research & Development	$0.00
Transportation, Commission, Cost of Sales	$9,597.36
Total COGS	**$67,079.85**
Gross Profit	**$155,533.18**
Expenses	
Rent, General, and Administrative	$14,150.00
HR Salaries & Wages	$29,963.74
HR Benefits & Programs	$11,662.88
Sales & Marketing	$39,550.00
Professional Services	$5,000.00
Maintenance and Insurance	$5,000.00
Inventory Spoiled or Damaged	$11,066.48
Tax Paid	$0.00
Interest Paid	$0.00
Bad Debt	$0.00
Income Tax	$0.00
Total Expenses	**$116,393.10**
Net Profit (Loss)	**$39,140.08**

19 BALANCE SHEET



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The **Balance Sheet** shows the value of the business by adding up everything the business owns and subtracting everything that the business owes. The actual value of a business is often more complex than the Balance Sheet shows, but the Balance Sheet provides an accurate view of its financial position.

Assets and Liabilities

To understand a Balance Sheet, you must first understand some key definitions.

Asset
This is something that a business owns. This could be cash, furniture, property, buildings, computer software, and more.

Liability
This is something that a business owes. This could be money owed to employees, vendors, the government, or loans owed to banks and others.

The Balance Sheet adds up all the assets and the liabilities and then applies this simple formula:

Assets – Liabilities

If the business owns more value in assets than it owes in liabilities, then it has positive equity. **Equity** is the value held in the business and is the third component of the Balance Sheet formula, as shown here:

Here is an example that applies the Balance Sheet formula:

Assets – Liabilities = Equity

ASSETS $5,000	Cash $4,000 Furniture $600 Computer $400
LIABILITIES $3,000	Bank Loan $2,000 Credit Card $1,000
EQUITY $2,000	

One way to read the above is to say that if the business is shut down and everything in it sold (liquidated) and the liabilities paid off to $0, there would be $2,000 left over. This is how much value currently exists in the business.

Complete the table below with additional examples.

ASSETS	Cash $8,000 Furniture $700 Computer $400	Cash $12,000 Unpaid Sales $1,000 Land $10,000
LIABILITIES	Bank Loan $2,500 Credit Card $900	Bank Loan $9,500 Owed to Suppliers $6,000
EQUITY	$ ________________	$ ________________

Business Value

Intangible Assets

The concept of business value is somewhat simplified in the examples above, as a business may also have intangible assets which contribute to its value.

Intangible assets may include patents, trademarks, customer contracts, goodwill, and more. Intangible means something that is not physical and cannot be touched. Furniture and computers are tangible assets — they have physical form.

Assigning value to intangible assets can be subjective, but generally equates to the value of what the intangible asset could be sold for if it had to be sold. This means that there has to be a reasonable expectation that a buyer can be found that is willing and able to purchase the intangible asset at the price set. However, sometimes intangible assets are valued differently based on generally-accepted accounting principles.

This is an advanced topic beyond the scope of this document, but is noted here to help frame the Balance Sheet.

See the table below and complete the second example. Notice that intangible assets (patents and customer contracts) have been added to the Balance Sheet.

BALANCE SHEET		
ASSETS	Cash $8,000 Furniture $1,000 **Patents $2,000**	Cash $12,000 Land $10,000 **Customer Contracts $2,000**
LIABILITIES	Bank Loan $7,000	Bank Loan $12,000
EQUITY	$4,000	$ ____________________

Tangible Assets

Another element that affects business value is the value of the tangible assets on the Balance Sheet. The value shown for assets is not the original purchase price, but the depreciated value of the asset. Depreciation is also an advanced topic, but it generally means that most assets will lose value over time, and so the Balance Sheet should properly reflect this change in value.

For example, a computer may cost $900 brand new today, but if you tried to sell that computer in one year, you may only get a few hundred dollars for it. The Balance Sheet should show the computer at this reduced value.

See the table below and complete the additional example. Notice that the value of the computer has changed from Year 1 to Year 2 on the Balance Sheet because it has depreciated.

	YEAR 1	YEAR 2
ASSETS	Cash $8,000 Computer $900	Cash $8,000 Computer $400
LIABILITIES	Bank Loan $7,000	Bank Loan $7,000
EQUITY	$1,900	$ ______________

Equity

How does a business create value, or equity? Reviewing the Balance Sheet formula:

Assets – Liabilities = Equity

This may suggest to increase assets. But, how does a business increase the value of an asset? Most assets lose value over time, like furniture and computers. Real estate may or may not increase in value over time.

Buying a new asset will not increase equity. This is because if a business buys a new asset, then cash may be reduced to pay for the new asset. In this case, the equity has not changed, as shown in the table below.

ASSETS	Cash $8,000	Cash $6,000 **Computer $2,000**
LIABILITIES	Bank Loan $7,000	Bank Loan $7,000
EQUITY	$1,000	$1,000

What if the business buys the computer using a credit card? In this case, the credit card balance will appear as a liability, and again the equity does not change, as shown in the table below.

ASSETS	Cash $8,000	Cash $8,000 **Computer $2,000**
LIABILITIES	Bank Loan $7,000	Bank Loan $7,000 **Credit Card $2,000**
EQUITY	$1,000	$1,000

Buying, renting, or leasing assets does not increase the value or equity of a business. It's what the business does with those assets that may contribute to increasing equity.

For example, buying a new computer may allow you to serve more customers to sell more product and generate more revenue and profit. This additional profit increases equity. Buying the computer did not directly increase equity, but how it was used did.

Again, reviewing the Balance Sheet formula:

Assets – Liabilities = Equity

This may suggest that decreasing Liabilities will increase equity. But, decreasing a liability normally means using an asset, like cash.

For example, you can pay off a $7,000 bank loan to eliminate the liability, but if you use cash to pay the loan, then your asset will also decrease, as shown in the table below.

ASSETS	Cash $8,000	Cash **$1,000**
LIABILITIES	Bank Loan $7,000	
EQUITY	$1,000	$1,000

Increasing Equity

Equity is most often increased in two ways:

Profit
As a business generates profits over its history, the total cumulative profits (and losses) over its entire time in business are added to its equity.

Selling Shares
When a business sells stock or shares in the business, which means ownership in the business, those who buy the shares give the money to the business and this money is recorded as equity.

Equity is reduced if the business suffers losses (negative profit) or if the business issues dividends to its shareholders (owners). A dividend is simply a share of the profits (which are shown as equity).

Profit (Retained Earnings)

Profit increases equity. For example, if you make or buy 100 widgets for $5 each and sell them for $7, you will make a profit of $2 per widget, as shown in the table below. This assumes there were no other expenses incurred with buying and selling the widgets.

BUY $500	100 Widgets $5 Each
SELL $700	100 Widgets $7 Each
PROFIT $200	$700 - $500

The $200 profit shown above gets added to the equity on the Balance Sheet, as shown in the table below. Notice that before the widgets are purchased, you have $1,000 cash. Then $500 is used to purchase the widgets, so cash is reduced by $500 and widgets are added as an asset that you own. Then, the widgets are sold for $700 that is added to cash, and the widgets no longer appear as assets.

	BEFORE	DURING	AFTER
ASSETS	Cash $1,000	Cash $500 Widgets $500	Cash $1,200
LIABILITIES			
EQUITY	$1,000	$1,000	$1,200

Profit is the most common way that businesses increase Equity. Profit is tracked on the **Income Statement** (or Profit and Loss or P&L). The profit (more specifically, the net profit) at the bottom of the Income Statement is added to the equity on the Balance Sheet.

Profit is added under equity as what is called **retained earnings** — more on this below.

Selling Shares

When a business sells stock (shares) in the business, which means ownership in the business, those who buy the shares give the money to the business and this money is recorded as equity.

For example, let's say you sell a certain number of shares for a total of $500. The new shareholder gives your company $500 cash and you record this transaction on the Balance Sheet by increasing cash by $500 and increasing equity by $500, as shown in the table below. Money gained through the sales of shares is not considered profit and does not appear on the Income Statement.

Notice that the Balance Sheet equation still remains in balance:
Assets – Liabilities = Equity

	BEFORE	AFTER
ASSETS	Cash $1,000	Cash $1,500
LIABILITIES	$0	$0
EQUITY	$1,000	$1,500

Balance

The Balance Sheet has the word "balance" in the name to indicate that it must always remain in balance. This means that the formula always remains true:

Assets – Liabilities = Equity

The formula can also be rearranged as follows:

Assets – Equity = Liabilities

Liabilities + Equity = Assets

Whichever format the formula takes, it must always balance, otherwise it indicates that there has been an accounting error made that needs to be corrected. See the example below.

	IN BALANCE	OUT OF BALANCE
ASSETS	Cash $3,000	Cash $2,500
LIABILITIES	Bank Loan $1,000	Bank Loan $1,000
EQUITY	$2,000	$2,000

In the table below, identify if each Balance Sheet example is in or out of balance and by how much. Enter $0 if in balance.

ASSETS	Cash $5,500	Cash $2,500 Computer $300	Cash $3,500 Furniture $500
LIABILITIES	Bank Loan $1,500	Bank Loan $2,000	Bank Loan $2,000 Credit Card $500
EQUITY	$4,000	$900	$1,000
IN OR OUT OF BALANCE?	$ ________	$ ________	$ ________

Dividends and Retained Earnings

Profit is added under equity as what is called **retained earnings**. "Earnings" means profit. "Retained" means held or kept — as opposed to profit or earnings that are paid out to company shareholders.

When profit is paid out to the company shareholders, it is called a **dividend**. When profit is paid out of a company, the equity in the company is reduced, as shown in the table below. Notice also that cash has been reduced by the amount of the dividend paid.

	BEFORE $1,000 DIVIDEND	AFTER $1,000 DIVIDEND
ASSETS	Cash $9,000	Cash $8,000
LIABILITIES	Bank Loan $1,000	Bank Loan $1,000
EQUITY	$8,000	$7,000

Complete the table below with additional examples.

	BEFORE $2,000 DIVIDEND	AFTER $2,000 DIVIDEND
ASSETS	Cash $7,000	Cash $ ___________
LIABILITIES	Bank Loan $2,000	Bank Loan $2,000
EQUITY	$5,000	$ ______________

Period

When generating a Balance Sheet, you have to choose a date. The data that will be displayed will include all past history up to and including the date you select.

Connecting the Balance Sheet and Income Statement

The Income Statement and the Balance Sheet are connected through one number: Retained Earnings.

The Balance Sheet shows the current value of the business. Value includes the total net profit accumulated by the business, minus dividends paid out to shareholders — what is known as retained earnings. This appears under Equity, along with money invested in the business by shareholders.

INCOME STATEMENT
REVENUE
COGS & EXPENSES
NET PROFIT

BALANCE SHEET
ASSETS
LIABILITIES
EQUITY + RETAINED EARNINGS

In the table above, net profit from the Income Statement is added to Equity on the Balance Sheet.

Sample Balance Sheet

Balance Sheet

Andreas Neger • Burgercenter • Casual Restaurant • Full Business

Assets

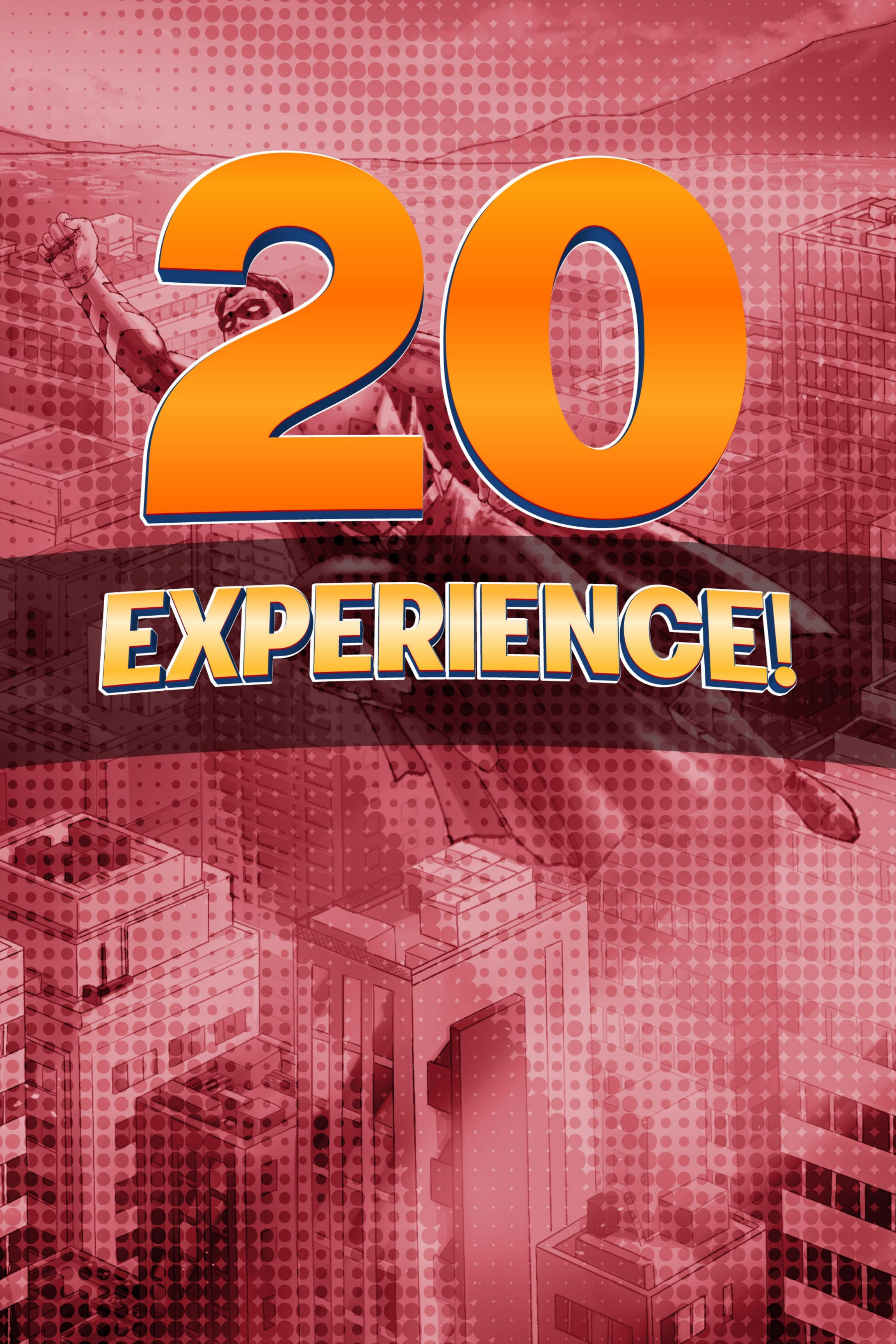
Cash	$61,288.16
Accounts Receivable	$0.00
Inventory	$1,661.34
Transportation	$1,885.37
Property, Equipment, Startup	$43,250.00
Total Assets	**$108,084.87**

Liabilities

Accounts Payable	$8,944.79
Tax Collected	$0.00
Credit	$0.00
Loans	$0.00
Total Liabilities	**$8,944.79**

Equity

Startup Capital	$60,000.00
Capital from Shares Sold	$0.00
Retained Earnings	$39,140.08
Total Equity	**$99,140.08**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EXPERIENCE!

Experience!

Now that you have learned the fundamental concepts of business and entrepreneurship, you are ready to put your knowledge to practice.

Gain experience by doing business-related activities or starting your own business.

YOUR BUSINESS SUPERHERO ORIGIN STORY BEGINS NOW!

Discover books, games, courses, and answers to the activities in this book at **Georghiou.com**

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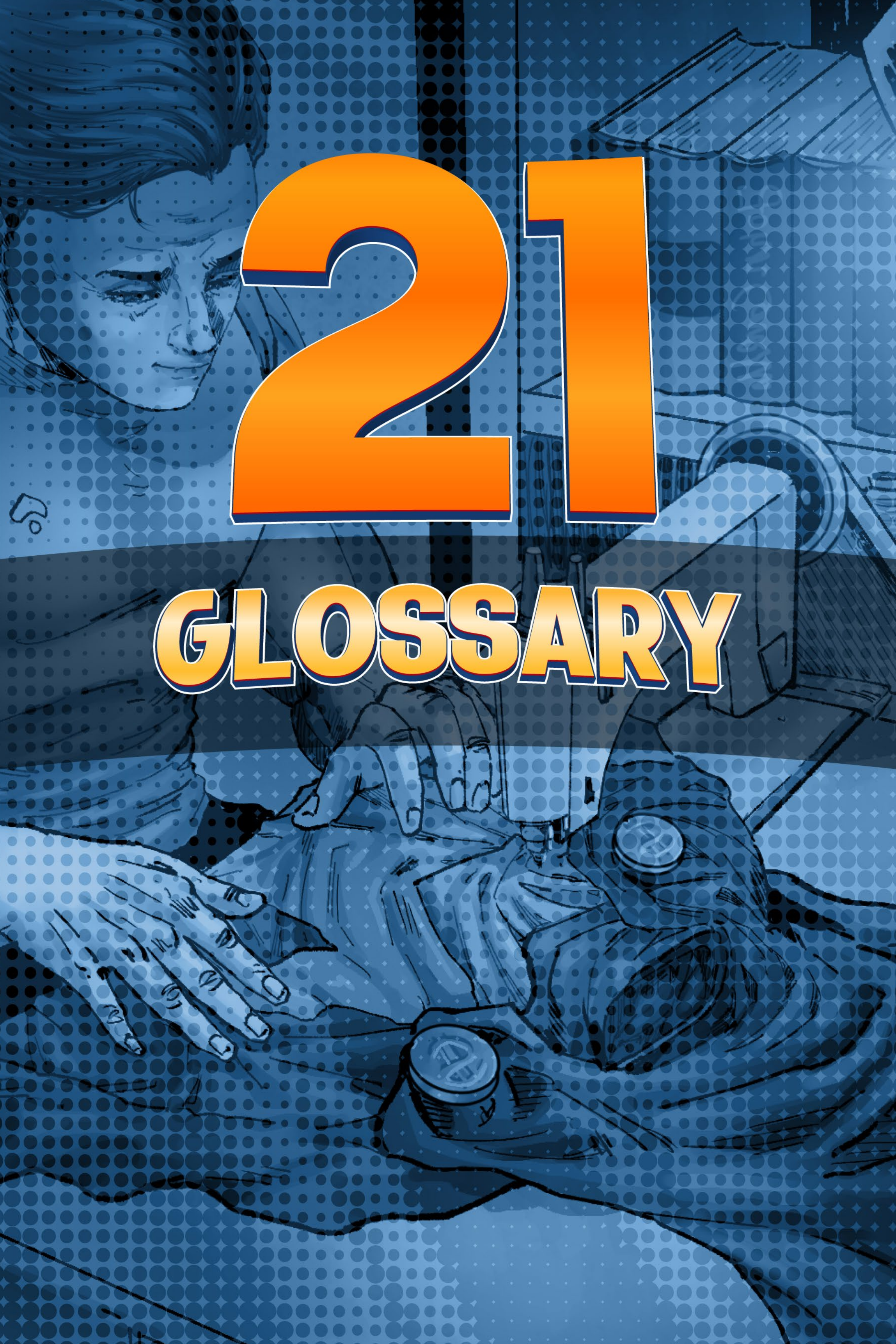
GLOSSARY



INDEX

Accounting

The process of tracking financial transactions and reporting the results of the transactions. A financial transaction occurs every time that money or something of value moves in or out of a business.

Accounts Payable

An accounting account used to record purchases of goods and services made by a business for which the business has not yet paid, but expects to pay within one year.

Accounts Receivable

An accounting account used to record sales made of goods or services by a business for which the business has not yet received payment, but expects to within one year.

Accrual Basis Accounting

An accounting method where revenue and expenses are recorded when the transaction occurs rather than when payment is received or made.

Amortization Period

The length of time over which a loan is scheduled to be fully repaid.

Amortization Schedule

A list of the dates and payment amounts due to be made on a loan.

Angel Investor

A wealthy individual who invests in a private business by providing debt or equity financing.

Assets

Something of value that a business owns.
This could be cash, furniture, property, buildings, computer software, and more.

Balance Sheet

A financial report that shows the value of a business by adding up everything the business owns and subtracting everything that the business owes. The Balance Sheet formula is Assets minus Liabilities equals Equity.

Benefits

Compensation, perks, and incentives that a business may choose to offer employees in order to maintain or improve employee morale, loyalty, productivity, recruiting, and turnover.

Bookkeeping

A system for tracking financial transactions.

Brand

How people feel about a business, good, or service. This feeling may be influenced by a brand promise, brand personality, visual identity, and tone of voice.

Brand Personality

The human personality characteristics that are associated with a brand.

Brand Promise

The promise made for the kind of experience people will have with a business, good, or service.

Budget

An amount of money a business reserves to invest in a project or business function, sometimes within a given period of time.

Business

An organization that sells goods or services.

Business Ethics

The values and principles that a company follows to sustain its brand, manage business risks, and maintain good stakeholder relations.

Business Founder

The person or people who start a business and usually own the business in the early stages of startup.

Business Plan

A document that describes, with some detail, how the business founders, owners, and managers plan to achieve success.

Carrying Costs

Costs associated with storing inventory, making sure it is secure and undamaged. Carrying costs may also include insurance costs, potential depreciation in value of the goods, and more.

Cash Basis Accounting

An accounting method where revenue and expenses are recorded when payments are received or made.

Cash Flow

Money moving in and out of a business.

Cash Flow Statement

A report that projects the timing of money moving in and out of a business.

Collateral

Something of value in a loan agreement that is pledged by the borrower as security for repayment of a loan. The collateral may be forfeited to the lender if the loan is not repaid.

Company

An organization that is created and structured to do business.

Company Valuation

The value of a company if it were to be sold.

Compound Period

The span of time between when interest on a loan was last compounded and when it will be compounded again.

Consumer Groups

A collection of consumer profiles that indicate similar psychographics.

Consumer Profiles

The demographics and psychographics that define the needs and desires of a consumer.

Consumers

Individuals or organizations that purchase and use a good or service.

Copyright

A type of intellectual property protection that applies to original literary, dramatic, musical, and artistic works.

Corporation

A legal term used to describe a specific form of business registration. A corporation is an entity that has been created to conduct business – for profit or nonprofit – and is effectively recognized as a person under law.

Cost of Goods Sold (COGS)

The cost to buy or make a good that has been sold.

Cost-Plus Pricing

A pricing method that sets the selling price of a good or service at a set amount higher than the cost to make and sell the good or service.

Credit

Used in accounting to record a decrease in Assets or Expenses or an increase in Liabilities, Equity, or Revenue.

Used in finance to borrow money or access goods or services with the understanding that payment will be made at a future date.

Used in personal finance to measure the reliability of a borrower to repay a lender.

Crowdfunding

A website or an online service that enables individuals from around the world to pre-purchase a new product that is not yet available for sale, or to invest money in a new business in return for goods or equity.

Currency

The system of money used in a country, such as dollar, euro, or yen.

Currency Symbol

A text character that identifies a specific monetary currency, such as $ for dollar, € for euro, and ¥ for yen.

Customer

An individual or an organization that purchases a good or service.

Dealer

An organization that resells goods made by other businesses.

Debit

Used in accounting to record an increase in Assets or Expenses or a decrease in Liabilities, Equity, or Revenue.

Debt Financing

Borrowed money that must be repaid, often with interest.

Demographics

A person's gender, age, income, location, and other statistical data.

Direct Sales

Selling goods or services directly to the consumer, without an intermediary.

Distribution Channel

An intermediary through which a good or service passes until it reaches the final consumer.

Dividend

Distribution of business profit paid to shareholders.

Domestic Currency

Monetary currency used in the country in which a business is located.

Double-Entry Bookkeeping

An accounting system whereby each transaction gets entered twice, so that every entry to any one account requires a corresponding and opposite entry to a different account.

Elevator Pitch

A short text script or verbal presentation that summarizes a business in a few sentences.

End Consumer

A person or organization that uses a good or service.

Entrepreneur

A person who starts and operates a business, while assuming its risks and rewards.

Equity

The value of a business as calculated on a Balance Sheet using the formula: Equity equals Assets minus Liabilities.

Equity Financing

Money given to a business by a person or organization in return for a percentage or share of ownership in the business.

Exchange Rate

The value of one monetary currency compared to another monetary currency.

Executive Summary

A brief summary of a business plan.

Expenses

The financial costs to operate a business, including employee wages, sales and marketing costs, interest on loans, and more.

Financials

Financial reports that show the current and projected future state of a business. Most commonly refers to the Balance Sheet, Income Statement (Profit & Loss), and Cash Flow Statement.

Financial Transaction

A record of money, or something of value, moving in or out of a business.

For-Profit Organization

A business that is intended to create profit for its owners to use as they choose.

Good

A tangible item that can be used once or multiple times.

Income Statement

A financial report that shows all of the money flowing in and out of a business to determine if the business is profitable or not.

Industrial Design

A type of intellectual property protection for the shape, pattern, or ornamentation applied to a manufactured article.

Integrated Circuit Topography

A type of intellectual property protection for three-dimensional configurations of electronic circuits embodied in integrated circuit products or layout designs.

Interest Rate

The percentage of interest to be paid on the principal of a loan.

Inventory

The goods and materials that a business holds and expects to sell.

Liabilities

The debts that a business owes. Plural of liability.

Liability

Something of value that a business owes.

Loan Principal

The amount of money to be borrowed in a loan agreement.

Logo

A unique visual identifier that distinguishes a business.

Love Money

The money invested in a business by family and friends of the business founders and owners.

Loyal Customer

A customer that repeatedly buys from the same business and is reluctant to change.

Market

In sales and marketing, market is the profile and number of people who might buy a particular type of good or service and the amount of money those people may collectively spend on such purchases.

Market Data

In sales and marketing, quantitative and qualitative information about a market.

Market Demand

In sales and marketing, the amount of money that is spent by consumers to purchase a type of good or service.

Market Pricing

A pricing method that sets the price of a good or service to what consumers are estimated to be willing to pay.

Market Share

The percentage of customers or sales a business wins in comparison to other businesses in the same type of business.

Marketing

Activities that generate leads or prospects for the purchase of a good or service.

Marketing and Sales Strategy

A plan for how to reach consumers and sell them a specific good or service.

Mission Statement

A description of how a business will achieve its vision.

Nonprofit or Not-For-Profit Organization

A business or other type of organization that is intended to support a social cause without distributing profits external to the organization. This may include a charity, medical research, local community, industry association, or other initiative.

Order Form

A document, online form, or online shopping cart provided by a seller to be used by customers to place orders for goods or services.

Organizational Customer

A customer that is a company, government, school, hospital, or other organization that is not an individual person.

Partnership

A legal term used to describe a specific form of business registration, similar to a sole proprietorship, but created by two or more people who are personally responsible for all business obligations.

Patent

A type of intellectual property protection for new inventions or processes that offer innovative and useful functions.

Payment Period

The frequency in which loan payments will be made.

Personal Guarantee

A promise made by a business owner, or an affiliated person, to repay a loan using personally-owned assets, if the business is unable to do so.

Pitch Deck

A slide presentation of a business plan summary.

Price

The money a customer gives to a business to buy goods or services.

Price Anchoring

The price a consumer expects to pay for a good or service, based on a previous purchase of the same or similar good or service, or based on some other influence.

Price Discount Advertising

The promotion of a sale or other price reduction of goods or services.

Private Organization

An organization that is not obligated to disclose its financials or operations to the public, and which places limits on how its stock can be traded.

Product

A tangible item or service that is made available for sale by a business.

Product Line and Brand Advertising

A promotion to build awareness and generate sales of an overall product line and brand, as opposed to the promotion of a specific good or service.

Productivity

The labor output, efficiency, or efficient use of an employee, machine, system, or material.

Profit

A financial gain or an earned surplus (often referring to money).

Psychographics

In sales and marketing, how a consumer thinks, including attitudes, aspirations, and other psychological criteria.

Public Company

A business that is required to disclose its financial information to the public, and which has greater flexibility in how its stock can be traded.

Purchase Order

A document used to place an order for goods or services.

Receipt

A document that confirms that something of value has been transferred from one person or organization to another.

Reseller

An organization or person that resells goods or services made or provided by another organization or person.

Retained Earnings

Cumulative net profit generated by a business and which remains in a business (not paid out as dividends).

Revenue

The money given to a business by customers purchasing its goods and services.

Salary

The money paid to an employee for working.

Sales

The activities needed to directly persuade a lead or prospect to actually buy a good or service.

Sales Promotion

In-store displays, contests, and other sales tactics to directly reach a consumer to build awareness and generate sales of a specific good or service.

Satisfied Customer

A customer that is pleased with the results of using a specific good or service.

Seed Financing

The money used to cover business startup costs, such as business registration, equipment, permits, insurance, building renovations, and more.

Selling Price

The money a reseller, distributor, or customer pays a business for a good or service.

Service

An action that someone does, usually in return for compensation. Unlike a good, a service is intangible, such as car repair, haircut, teaching, legal advice, medical procedures, and more.

Severance Cost

The direct financial cost to dismiss an employee.

Shareholder

An owner of a business – specifically, a corporation.

Sole Proprietorship

A legal term used to describe a specific form of business registration where a business is owned by one person with no share structure and the owner is personally responsible for all business obligations.

Spoilage

Expiration of or damage to a nondurable consumer good.

Stock Certificate

A paper document issued to a shareholder that demonstrates ownership in a business.

Stock Exchange or Stock Market

A physical or online marketplace where shares of companies can be bought and sold (traded) by the public.

Store

A place where consumers can view and purchase goods and services. Usually refers to a physical location but may also be an online store, website, or software app.

Strategy

A plan for how a business will achieve its goals.

Supplier

An organization that supplies parts or services used by another organization to produce its own goods or services.

Trademark

A type of intellectual property protection for combinations of letters, words, sounds, or designs that distinguish the goods or services offered by one organization from those of others in the marketplace.

Turnover

The rate at which employees leave a workforce and are replaced. May also refer to business revenue.

Values

The core principles and standards that guide the way the people in a business operate. May include beliefs and attitudes about how people should behave towards each other, suppliers, and customers, and the ethical standards by which a business strives to abide.

Venture Capital

A professionally-managed fund that is raised specifically for the purpose of investing in businesses that can generate a high return on investment.

Vision Statement

A phrase that describes the future state of a business, if it is successful.

Wordmark

Stylized text used as a logo.

Word-of-mouth

In sales and marketing, when a person, usually a satisfied customer, informs other people about a business, good, or service.

Working Capital

The money used to buy product inventory and pay the operating expenses for a business.

BUSINESS SUPERHERO

A powerfully clear and concise guide to the basics of business and entrepreneurship

by Mathew Georghiou

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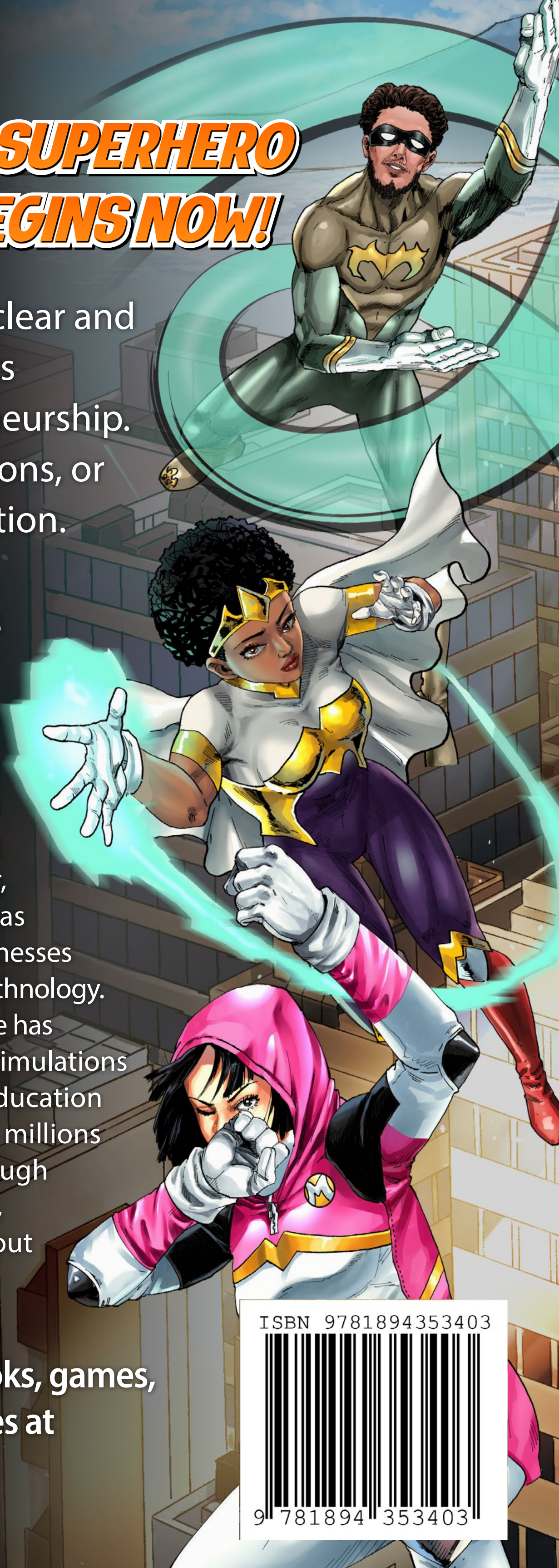

This book is a powerfully clear and concise guide to the basics of business and entrepreneurship. There are no stories, opinions, or other extraneous information. Just the fundamentals — presented in a style that is quick to read and easy to understand.

About the Author

Mathew Georghiou is an engineer, inventor, and entrepreneur who has founded and operated several businesses in education, entertainment, and technology. An expert in experiential learning, he has designed educational games and simulations that have transformed business education and entrepreneurship training for millions of learners around the world, through thousands of schools, universities, nonprofits, and businesses. Find out more at Georghiou.com

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