Module 4 - Financial Profile

Module 4 Financial Profile (Hours 10)

- Financial estimates like amount of funds needed for infrastructure facilities – land, building, plant, machinery, equipment, working capital requirement and other financial estimates - Estimates of financial costs and benefits of the business outcomes - Means of finance, i.e. how the business is to be financed - Projected financial statement for three to five years as per requirement.

Course Outcome

After finishing the course, the students will be able to:

1. Understand the nuts and bolts of preparing a business plan.
2. Remember and implement the business/management skills.
3. Understand and evaluate the content of business plan in detail.
4. Identify the tools and techniques involved in Business plan process.
5. Analyse the competitive structure and strategy development.
6. Launch a new venture company or start one an established organization

Topics covered

- Financial estimates like amount of funds needed for infrastructure facilities – land, building, plant, machinery, equipment, working capital requirement and other financial estimates
- Estimates of financial costs and benefits of the business outcomes
- Means of finance, i.e. how the business is to be financed
- Projected financial statement for three to five years as per requirement


Funding sources
Short-term loans
Sale and leaseback
Retained Profits
Grants & funding
PFI
Issuing shares
Share Capital
Debentures
Business Angels
Venture Capital
Overdrafts

Short Term Loans and Advances

- The short term loans and advance is generally provided for a shorter duration of time, for instance, a year.
- The bank will sanction this as a short-term loan, an overdraft, cash credit or a bill purchase.
- The advance will be facilitated only if the borrower meets specific conditions as outlined by the Reserve Bank of India.

Sale & Leaseback

- A leaseback is an arrangement in which the company that sells an asset can lease back that same asset from the purchaser.
- With a leaseback—also called a sale-leaseback—the details of the arrangement, such as the lease payments and lease duration, are made immediately after the sale of the asset.
- In a sale-leaseback transaction, the seller of the asset becomes the lessee and the purchaser becomes the lessor.

Retained Earnings

- The term refers to the historical profits earned by a company, minus any dividends it paid in the past.
- The word "retained" captures the fact that because those earnings were not paid out to shareholders as dividends they were instead retained by the company.
- For this reason, retained earnings decrease when a company either loses money or pays dividends, and increase when new profits are created.

Grant and Funding

- A government grant is a financial award given by a federal, state, or local government authority for a beneficial project. It is effectively a transfer payment.
- A grant does not include technical assistance or other financial assistance, such as a loan or loan guarantee, an interest rate subsidy, direct appropriation, or revenue sharing.
- The grantee is not expected to repay the money but is expected to use the funds from the grant for their stated purpose, which typically serves some larger good.

A Private Finance Initiative (PFI)

- A private finance initiative (PFI) is a way of financing public sector projects through the private sector. PFIs alleviate the government and taxpayers of the immediate burden of coming up with the capital for these projects.
- Under a private finance initiative, the private company handles the up-front costs instead of the government.
- The project is then leased to the public and the government authority makes annual payments to the private company.
- These contracts are typically given to construction firms and can last as long as 30 years or more.

Issuing Shares

- Issued shares are the subset of authorized shares that have been sold to and held by the shareholders of a company, regardless of whether they are insiders, institutional investors, or the general public (as shown in the company's annual report).
- Issued shares include the stock a company sells publicly to generate capital and the stock given to insiders as part of their compensation packages.

Share Capital

- Share capital is the money a company raises by issuing common or preferred stock. The amount of share capital or equity financing a company has can change over time with additional public offerings.

Debenture

- A debenture is a type of bond or other debt instrument that is unsecured by collateral.
- Since debentures have no collateral backing, they must rely on the creditworthiness and reputation of the issuer for support.
- Both corporations and governments frequently issue debentures to raise capital or funds.

Business Angel

- A business angel is a private individual, often with a high net-worth, and usually with business experience, who directly invests part of their assets in new and growing private businesses.
- Business angels can invest individually or as part of a syndicate where one angel typically takes the lead role.

Venture Capital

- Venture capital (VC) is a form of private equity and a type of financing that investors provide to startup companies and small businesses that are believed to have long-term growth potential.
- Venture capital generally comes from well-off investors, investment banks, and any other financial institutions.
- However, it does not always take a monetary form; it can also be provided in the form of technical or managerial expertise.
- Venture capital is typically allocated to small companies with exceptional growth potential, or to companies that have grown quickly and appear poised to continue to expand.

Overdraft

- An overdraft occurs when there isn't enough money in an account to cover a transaction or withdrawal, but the bank allows the transaction anyway.
- Essentially, it's an extension of credit from the financial institution that is granted when an account reaches zero.
- The overdraft allows the account holder to continue withdrawing money even when the account has no funds in it or has insufficient funds to cover the amount of the withdrawal.
- It could be suitable for short term requirement

XYZ Company Balance Sheet As at 30 June 2010		
Current Assets		
Cash at bank	30,000	
Inventory	250,000	
Debtors	75,000	
Total current assets		355,000
Non - Current Assets		
Buildings	550,000	
Plant & equipment	250,000	
Vehicles	120,000	
Total non-current assets		920,000
Total Assets		**1,275,000**
Current Liabilities		
Credit cards	15,000	
Creditors	110,000	
Tax Payable	25,000	
Total current liabilities		150,000
Non-current Liabilities		
Long term loans		700,000
Total Liabilities		**850,000**
Owners Equity		
Capital	100,000	
Retained earnings	250,000	
Current earnings	75,000	
Total Owners Equity		**425,000**

An example of Company Balance Sheet to explain the sources of funds, long term funds short term funds, retained earnings, and etc

Video on long term funds for Entrepreneurship

- https://www.youtube.com/watch?v=c8hIwQ5xFY8

Working Capital

- Proper management of working capital is essential to a company's fundamental financial health and operational success as a business.
- A hallmark of good business management is the ability to utilize working capital management to maintain a solid balance between growth, profitability and liquidity.

Working Capital (Cont…)

- A business uses working capital in its daily operations; working capital is the difference between a business's current assets and current liabilities or debts.
- Working capital serves as a metric for how efficiently a company is operating and how financially stable it is in the short-term.
- The working capital ratio, which divides current assets by current liabilities, indicates whether a company has adequate cash flow to cover short-term debts and expenses.

Key Points of Working Capital

- The goal of working capital management is to maximize operational efficiency.
- Efficient working capital management helps maintain smooth operations and can also help to improve the company's earnings and profitability.
- Management of working capital includes inventory management and management of accounts receivables and accounts payables.

Video link on Working Capital

- Basics of Working Capital (essential)
- https://www.youtube.com/watch?v=hV2f6Ujv9zY

- Types of Working Capital (optional)
- https://www.youtube.com/watch?v=_4lcuLJfbzQ

Financial costs and benefits of the business outcomes - What Is a Cost-Benefit Analysis (CBA)?

- A cost-benefit analysis is a systematic process that businesses use to analyze which decisions to make and which to forgo.
- The cost-benefit analyst sums the potential rewards expected from a situation or action and then subtracts the total costs associated with taking that action.
- Some consultants also build models to assign a dollar value on intangible items, such as the benefits and costs associated with living in a certain town.

KEY POINTS – COST-BENEFIT ANALYSIS

- A cost-benefit analysis (CBA) is the process used to measure the benefits of a decision or taking action minus the costs associated with taking that action.
- A CBA involves measurable financial metrics such as revenue earned or costs saved as a result of the decision to pursue a project.
- A CBA can also include intangible benefits and costs or effects from a decision such as employees morale and customer satisfaction.

Cost Benefit Analysis for Computerised Customer Service System				
Costs				
Category	Item	Qty	Price	Total
Equipment	Workstations c/w software	10	£2,500	£25,000
	Server	1	£3,500	£3,500
	Printers	3	£1,500	£4,500
	Network cable installation	1	£4,500	£4,500
	Specialised software (site licence)	1	£16,000	£16,000
Training	Basic computer skills	8	£400	£3,200
	Office software	8	£400	£3,200
	Customer service system	12	£750	£9,000
Other	Man hours lost	320	£25	£8,000
	Sales lost during initial phase (est)		£40,000	£40,000
			Total Cost:	**£116,900**
Benefits (estimated per annum)				
Postal campaigns and telesales				£60,000
Lead conversion				£45,000
Customer retention				£35,000
Accuracy of client information				£15,000
Improvements in management efficiency				£30,000
			Total Benefit:	**£185,000**

How the business is to be financed?

- Long term own fund
  - Share Capital
  - Retained Earnings
  - Sale & Buyback Lease
  - Business Angel
- Long term debt fund
  - Bank long term loan
  - Debenture (a fixed interest)
  - Bonds
  - Venture Capital
- Short term fund
  - Overdraft
  - Working capital Loan
  - Gaining credit period from suppliers
  - Money Market Instruments

Activity: Projected financial statement for five years as per requirement

- From the following details prepare the financial projection for 5 years (with the template).
- Indian Oil Corporation is issuing license to operate fuel station being its agent with the following requirements (Assume you are one among the applicant):
- A land with minimum of 15 cents either owned or leased
- Construction and Installation charges would be Rs. 20 lakhs
- Assume that you are having part of the land required and remaining your are acquiring against cash.
- Loan arranged Rs. 30 lakhs with the interest of 7.4% per annum for 15 years. The EMI (Equated Monthly Installment) would be Rs. 27640
- The staff to operate 7 and 1 cashier cum manager. Each staff will be paid a salary of Rs. 9000 p.m. and cashier cum manager Rs. 15000 p.m. The salary will be revised by 5% once in two years
- The source of revenue for the fuel station is commission on Petrol and Diesel sold per liter. Rs. 3.00 commission on Petrol per liter and Rs. 2.20 commission on Diesel per liter paid by Indian Oil Corporation.
- Assume 185 liters of petrol and 220 liters of diesel are sold per day and expected to increase by 5% in each year sales.
- The average sale of oil and lubricant per month would by Rs. 120 liters that would effetely results in Rs. 15000 of profit
- There is a offer by SBI to open a ATM counter in the vicinity of the fuel station with the rent of Rs. 2000 per month.