Summer 2023

Accelerated Innovation & Entrepreneurship Bootcamp

Session 15
Startups Financial 1

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Today’s Agenda

- Identify different Revenue Streams for business
- List Cost Structure of your products or services
- Discuss the importance of costing
- Differentiate between variable cost & fixed cost
- Introduce Break-Even Analysis definition

Key Partners

Who are our Key Partners?
Who are our key suppliers?
Which Key Resources are we acquiring from partners?
Which Key Activities do partners perform?

[illegible]
Optimization and economy
Reduction of risk and uncertainty
Acquisition of particular resources and activities

Key Activities

What Key Activities do our Value Propositions require?
Our Distribution Channels?
Customer Relationships?
Revenue streams?

[illegible]
Production
Problem Solving
Platform/Network

Key Resources

What Key Resources do our Value Propositions require?
Our Distribution Channels? Customer Relationships?
Revenue Streams?

[illegible]
Physical
Intellectual (brand patents, copyrights, data)
Human
Financial

Value Propositions

What value do we deliver to the customer?
Which one of our customer's problems are we helping to solve?
What bundles of products and services are we offering to each Customer Segment?
Which customer needs are we satisfying?

[illegible]
Newness
Performance
Customization
"Getting the Job Done"
Design
Brand/Status
Price
Cost Reduction
Risk Reduction
Accessibility
Convenience/Usability

Customer Relationships

What type of relationship does each of our Customer Segments expect us to establish and maintain with them?
Which ones have we established?
How are they integrated with the rest of our business model?
How costly are they?

[illegible]
Personal assistance
Dedicated Personal Assistance
Self-Service
Automated Services
Communities
Co-creation

Channels

Through which Channels do our Customer Segments want to be reached?
How are we reaching them now?
How are our Channels integrated?
Which ones work best?
Which ones are most cost-efficient?
How are we integrating them with customer routines?

[illegible]
1. Awareness
[illegible]
2. Evaluation
[illegible]
3. Purchase
[illegible]
4. Delivery
[illegible]
5. After sales
[illegible]

Customer Segments

For whom are we creating value?
Who are our most important customers?

Mass Market
Niche Market
Segmented
Diversified
Multi-sided Platform

Cost Structure

What are the most important costs inherent in our business model?
Which Key Resources are most expensive?
Which Key Activities are most expensive?

[illegible]
Cost Driven [illegible]
Value Driven [illegible]

[illegible]
Fixed Costs [illegible]
Variable costs
Economies of scale
Economies of scope

Revenue Streams

For what value are our customers really willing to pay?
For what do they currently pay?
How are they currently paying?
How would they prefer to pay?
How much does each Revenue Stream contribute to overall revenues?

[illegible]
Asset sale
Usage fee
Subscription Fees
Lending/Renting/Leasing
Licensing
Brokerage fees
Advertising

[illegible]
List Price
Product feature dependent
Customer segment dependent
Volume dependent

[illegible]
Negotiation (bargaining)
Yield Management
Real-time-Market

Key Partners

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Key Activities

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Our Distribution Channels?
Customer Relationships?
Revenue streams?

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Customer Segments

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Revenue Streams

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How would they prefer to pay?
How much does each Revenue Stream contribute to overall revenues?

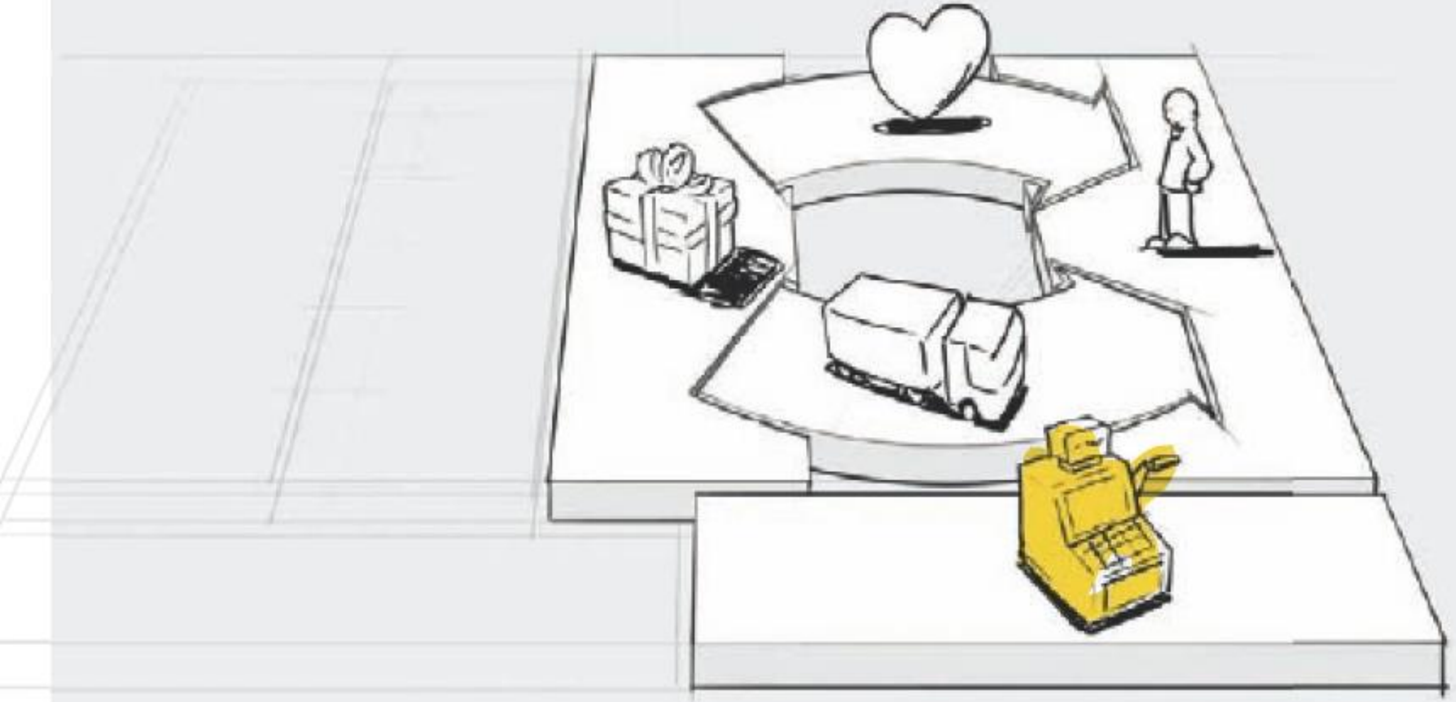
5 Revenue Streams

The Revenue Streams Building Block represents the cash a company generates from each Customer Segment (costs must be subtracted from revenues to create earnings)

If customers comprise the heart of a business model, Revenue Streams are its arteries. A company must ask itself, For what value is each Customer Segment truly willing to pay? Successfully answering that question allows the firm to generate one or more Revenue Streams from each Customer Segment. Each Revenue Stream may have different pricing mechanisms, such as fixed list prices, bargaining, auctioning, market dependent, volume dependent, or yield management.

A business model can involve two different types of Revenue Streams:

1. *Transaction revenues resulting from one-time customer payments*
2. *Recurring revenues resulting from ongoing payments to either deliver a Value Proposition to customers or provide post-purchase customer support*



For what value are our customers really willing to pay? For what do they currently pay? How are they currently paying? How would they prefer to pay? How much does each Revenue Stream contribute to overall revenues?

There are several ways to generate Revenue Streams:

Asset sale
The most widely understood Revenue Stream derives from selling ownership rights to a physical product. Amazon.com sells books, music, consumer electronics, and more online. Fiat sells automobiles, which buyers are free to drive, resell, or even destroy.

Usage fee
This Revenue Stream is generated by the use of a particular service. The more a service is used, the more the customer pays. A telecom operator may charge customers for the number of minutes spent on the phone. A hotel charges customers for the number of nights rooms are used. A package delivery service charges customers for the delivery of a parcel from one location to another.

Subscription fees
This Revenue Stream is generated by selling continuous access to a service. A gym sells its members monthly or yearly subscriptions in exchange for access to its exercise facilities. World of Warcraft Online, a Web-based computer game, allows users to play its online game in exchange for a monthly subscription fee. Nokia's Comes with Music service gives users access to a music library for a subscription fee.

Lending/Renting/Leasing
This Revenue Stream is created by temporarily granting someone the exclusive right to use a particular asset for a fixed period in return for a fee. For the lender this provides the advantage of recurring revenues. Renters or lessees, on the other hand, enjoy the benefits of incurring expenses for only a limited time rather than bearing the full costs of ownership. Zipcar.com provides a good illustration. The company allows customers to rent cars by the hour in North American cities. Zipcar.com's service has led many people to decide to rent rather than purchase automobiles.

Licensing
This Revenue Stream is generated by giving customers permission to use protected intellectual property in exchange for licensing fees. Licensing allows rights-holders to generate revenues from their property without having to manufacture a product or commercialize a service. Licensing is common in the media industry, where content owners retain copyright while selling usage licenses to third parties. Similarly, in technology sectors, patentholders grant other companies the right to use a patented technology in return for a license fee.

Brokerage fees

This Revenue Stream derives from intermediation services performed on behalf of two or more parties. Credit card providers, for example, earn revenues by taking a percentage of the value of each sales transaction executed between credit card merchants and customers. Brokers and real estate agents earn a commission each time they successfully match a buyer and seller.

Advertising

This Revenue Stream results from fees for advertising a particular product, service, or brand. Traditionally, the media industry and event organizers relied heavily on revenues from advertising. In recent years other sectors, including software and services, have started relying more heavily on advertising revenues.

Each Revenue Stream might have different pricing mechanisms. The type of pricing mechanism chosen can make a big difference in terms of revenues generated. There are two main types of pricing mechanism: fixed and dynamic pricing.

Activity 1

- Aumet
- Wajeez
- Cargenie
- POS Rocket

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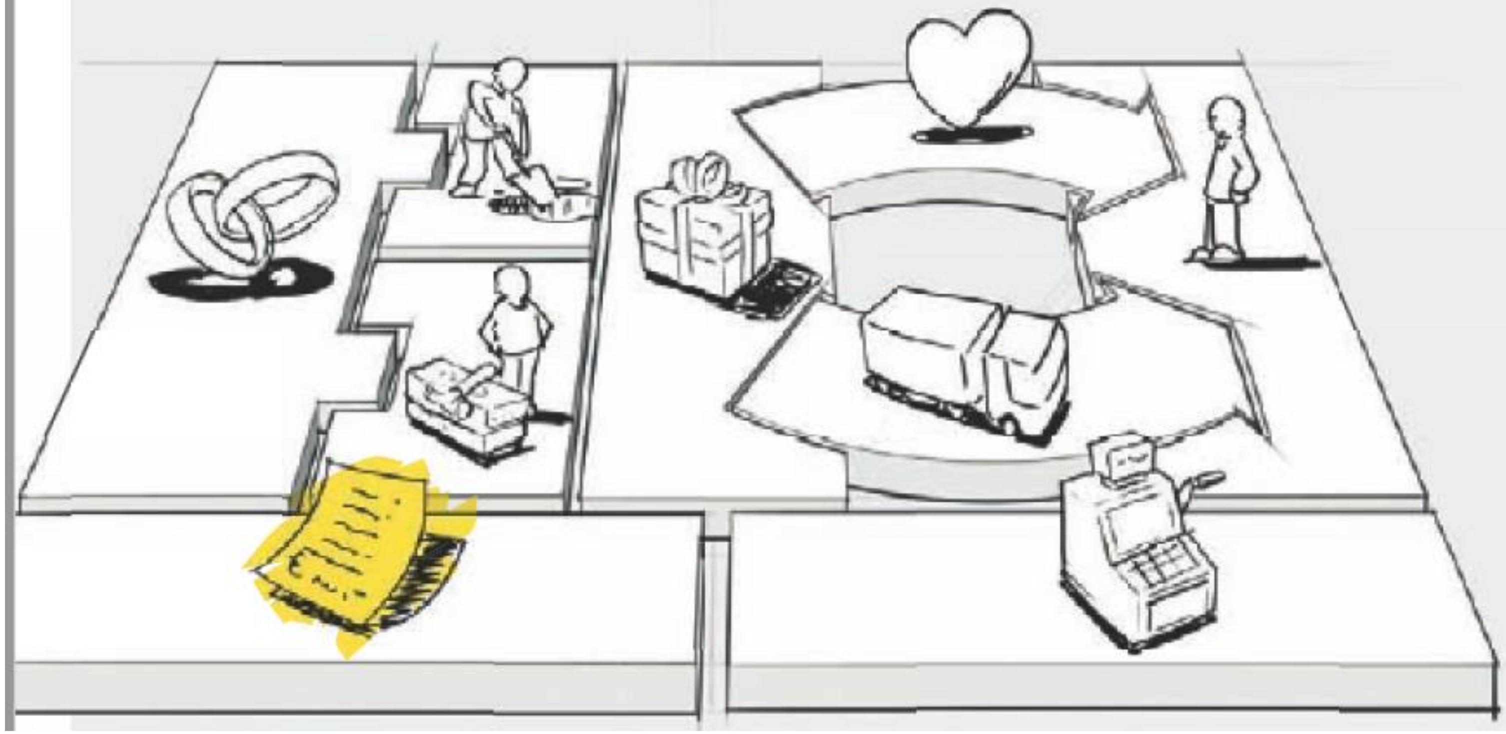
Cost Structure

The Cost Structure describes all costs incurred to operate a business model

This building block describes the most important costs incurred while operating under a particular business model. Creating and delivering value, maintaining Customer Relationships, and generating revenue all incur costs. Such costs can be calculated relatively easily after defining Key Resources, Key Activities, and Key Partnerships. Some business models, though, are more cost-driven than others. So-called "no frills" airlines, for instance, have built business models entirely around low Cost Structures.



What are the most important costs inherent in our business model? Which Key Resources are most expensive? Which Key Activities are most expensive?

Naturally enough, costs should be minimized in every business model. But low Cost Structures are more important to some business models than to others. Therefore it can be useful to distinguish between two broad classes of business model Cost Structures: cost-driven and value-driven (many business models fall in between these two extremes):

Cost-driven
Cost-driven business models focus on minimizing costs wherever possible. This approach aims at creating and maintaining the leanest possible Cost Structure, using low price Value Propositions, maximum automation, and extensive outsourcing. No frills airlines, such as Southwest, easyJet, and Ryanair typify cost-driven business models.

Value-driven
Some companies are less concerned with the cost implications of a particular business model design, and instead focus on value creation. Premium Value Propositions and a high degree of personalized service usually characterize value-driven business models. Luxury hotels, with their lavish facilities and exclusive services, fall into this category.

Cost Structures can have the following characteristics:

Fixed costs
Costs that remain the same despite the volume of goods or services produced. Examples include salaries, rents, and physical manufacturing facilities. Some businesses, such as manufacturing companies, are characterized by a high proportion of fixed costs.

Variable costs
Costs that vary proportionally with the volume of goods or services produced. Some businesses, such as music festivals, are characterized by a high proportion of variable costs.

Economies of scale
Cost advantages that a business enjoys as its output expands. Larger companies, for instance, benefit from lower bulk purchase rates. This and other factors cause average cost per unit to fall as output rises.

Economies of scope
Cost advantages that a business enjoys due to a larger scope of operations. In a large enterprise, for example, the same marketing activities or Distribution Channels may support multiple products.

- Costing is the process of establishing the exact amount paid to produce or provide a product or a service.

- **Importance of costing :**

1- To determine what price, you should sell your product/ service

2- To evaluate how much profit/loss your business is making

3- To know which items cost too much so that you can develop alternative ideas.

4- To find out how much each product/service costs

- **Costing helps your business to:**

1- Set competitive prices for your goods and services.

2- Reduce and control costs

3- Make better decisions about business.

4- Plan for future needs of the business.

Companies incur two types of production costs: variable costs and fixed costs.

Variable Costs

- Variable costs are a company's costs that are associated with the number of goods or services it produces. A company's variable costs increase and decrease with its production volume. When production volume goes up, the variable costs will increase. On the other hand, if the volume goes down, so too will the variable costs.

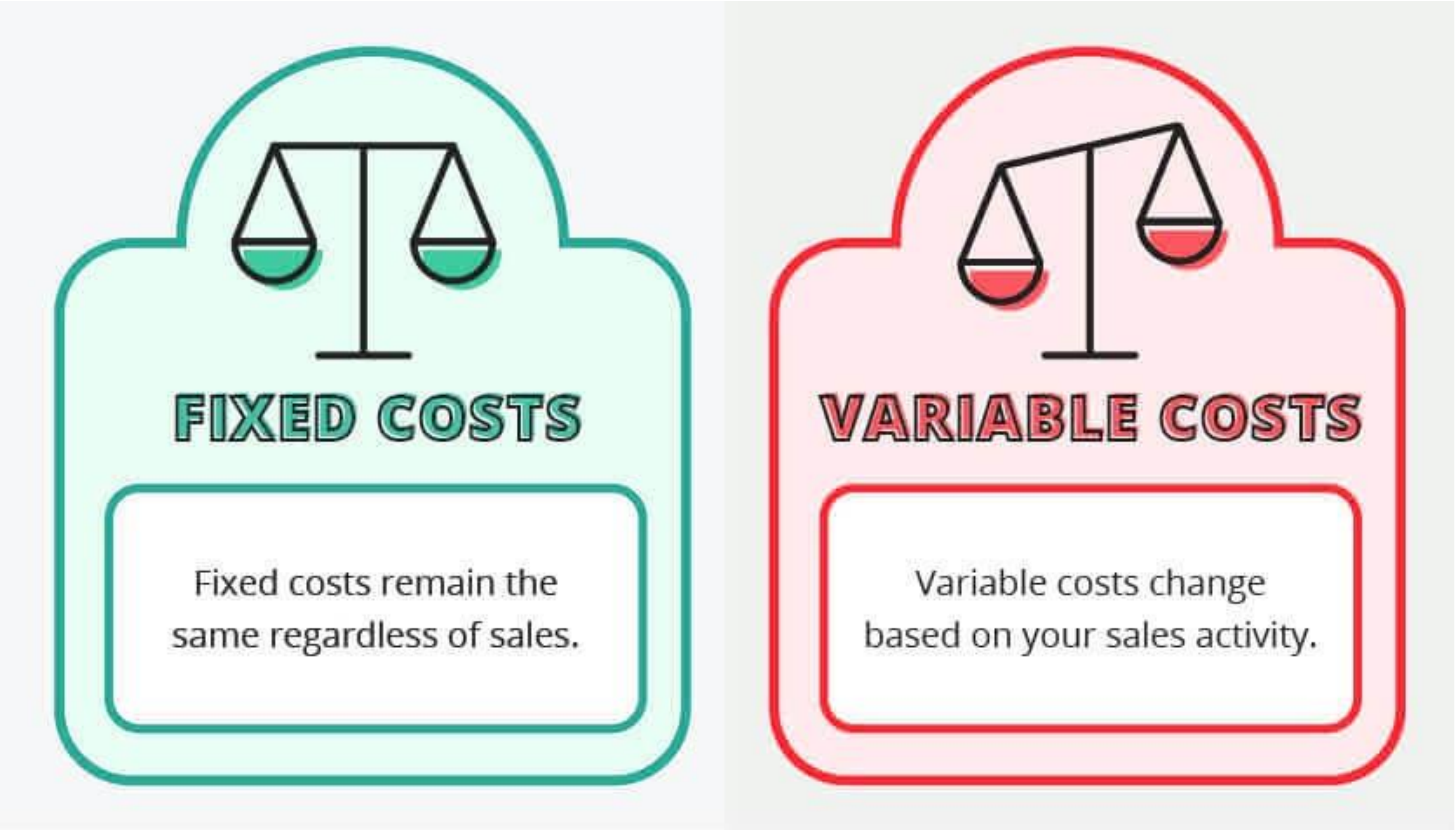
- calculate variable costs by multiplying the quantity of output by the variable cost per unit of output. This calculation is simple and does not take into account any other costs such as labor or raw materials.

Fixed Costs

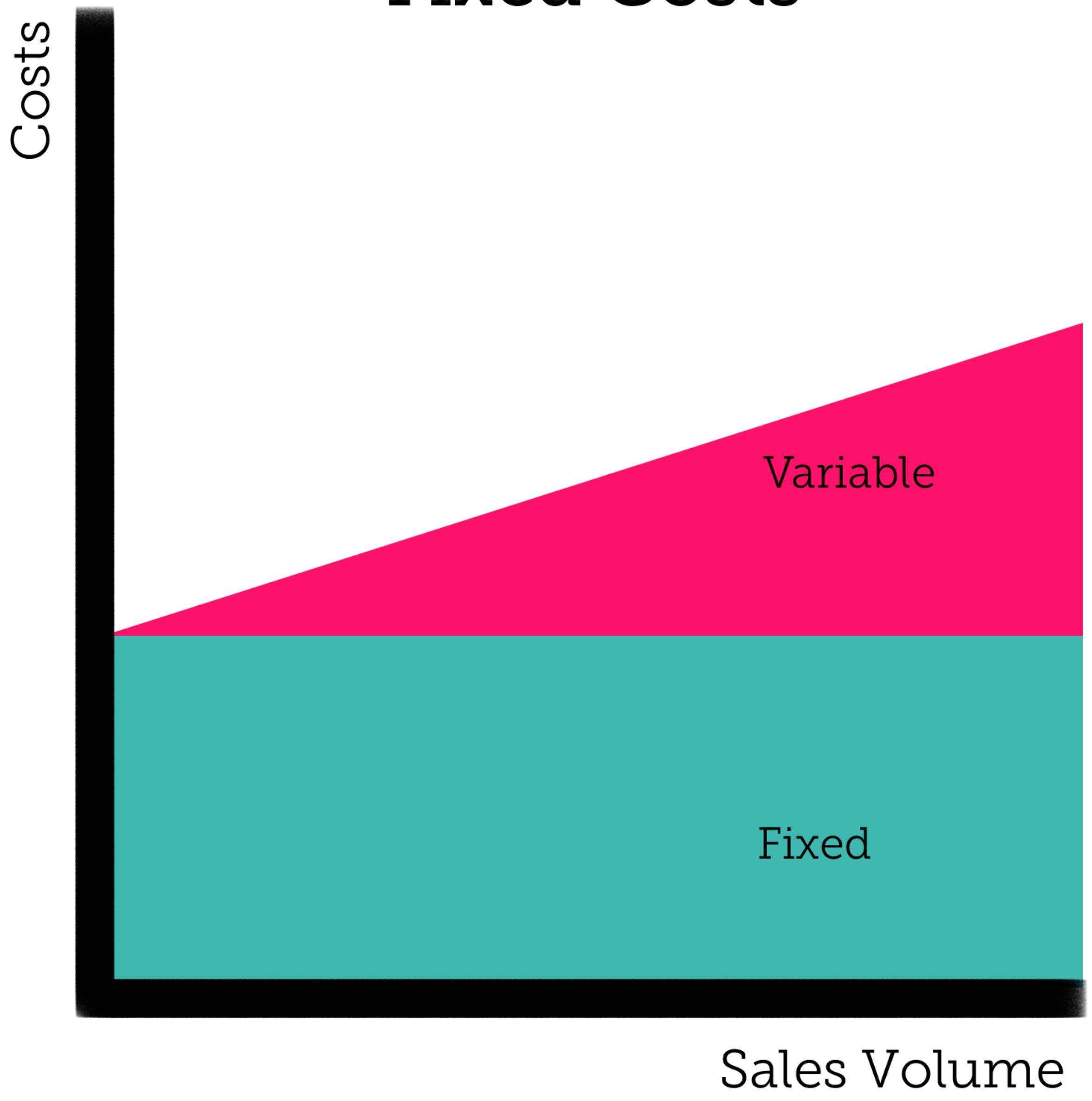
- Unlike variable costs, a company's fixed costs do not vary with the volume of production. Fixed costs remain the same regardless of whether goods or services are produced or not. Thus, a company cannot avoid fixed costs.

Example

- Suppose company ABC produces ceramic mugs for a cost of $2 a mug. If the company produces 500 units, its variable cost will be $1,000. However, if the company does not produce any units, it will not have any variable costs for producing the mugs. Similarly, if the company produces 1000 units, the cost will rise to $2,000.
- suppose company ABC has a fixed cost of $10,000 per month to rent the machine it uses to produce mugs. If the company does not produce any mugs for the month, it would still need to pay $10,000 for the cost of renting the machine. On the other hand, if it produces one million mugs, its fixed cost remains the same. The variable costs change from zero to $2 million in this example.


FIXED COSTS
Fixed costs remain the same regardless of sales.
VARIABLE COSTS
Variable costs change based on your sales activity.

Variable vs Fixed Costs

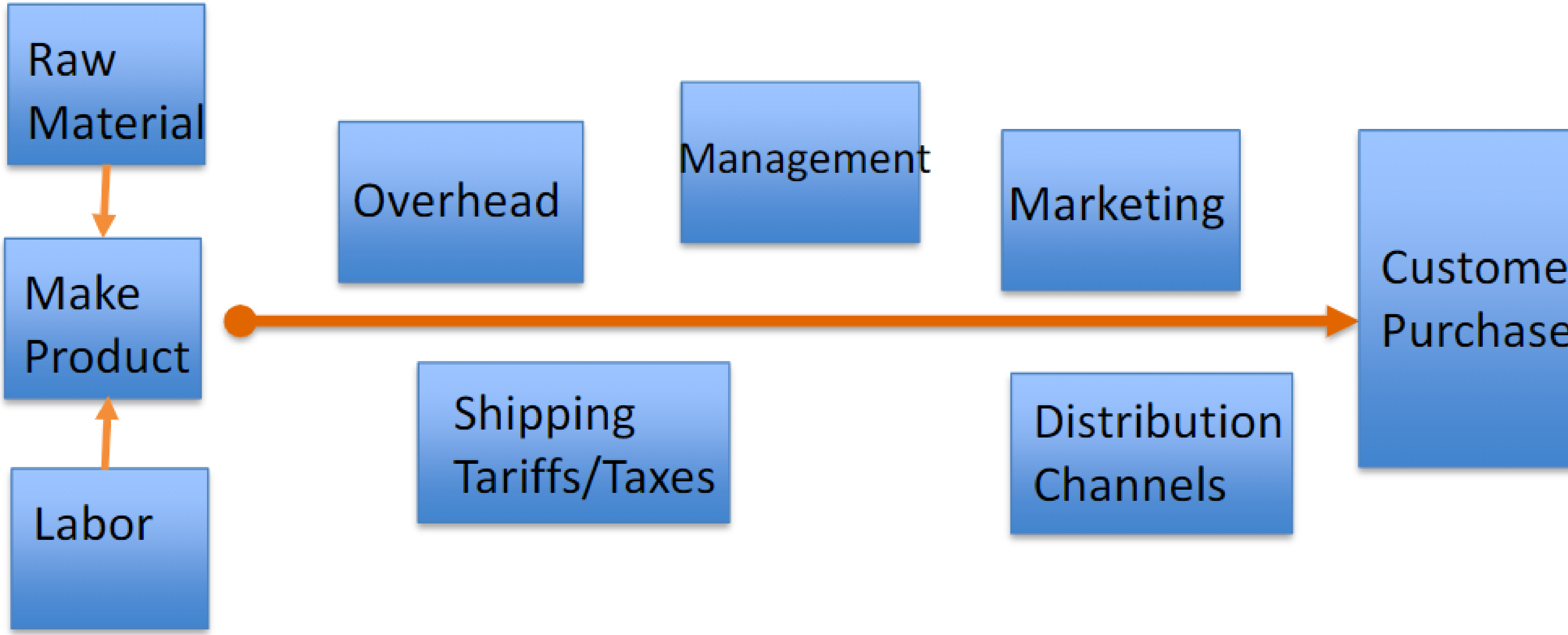


- While variable costs tend to remain flat, the impact of fixed costs on a company's bottom line can change based on the number of products it produces. So, when production increases, the fixed costs drop. The price of a greater amount of goods can be spread over the same amount of a fixed cost. In this way, a company may achieve economies of scale by increasing production and lowering costs.
- For example, ABC has a lease of $10,000 a month on its production facility and it produces 1,000 mugs per month. As such, it may spread the fixed cost of the lease at $10 per mug. If it produces 10,000 mugs a month, the fixed cost of the lease goes down, to the tune of $1 per mug.

	Variable Cost	Fixed Cost
Definition	Costs that vary/change depending on the company's production volume	Costs that do not change in relation to production volume
When Production Increases	Total variable costs increase	Total fixed cost stays the same
When Production Decreases	Total variable costs decrease	Total fixed cost stays the same
Examples	Direct Materials (i.e. kilograms of wood, tons of cement)	Rent
	Direct Labor (i.e. labor hours)	Advertising
		Insurance
		Depreciation

How much does it cost to produce your product?

Costing


Raw Material
Make Product
Labor
Overhead
Shipping Tariffs/Taxes
Management
Marketing
Distribution Channels
Custome
Purchas

Costing

- How much does it cost **to make (build)** your product?
  - Raw Materials
  - Labor
  - Software Design (UX/UI)

- How much does it cost **to run** your business?
  - Management Salaries
  - Rent
  - Marketing
  - Depreciation of equipment

- How much does it cost **to start** your business?
  - Equipment
  - Factory
  - Company Registration

Costing

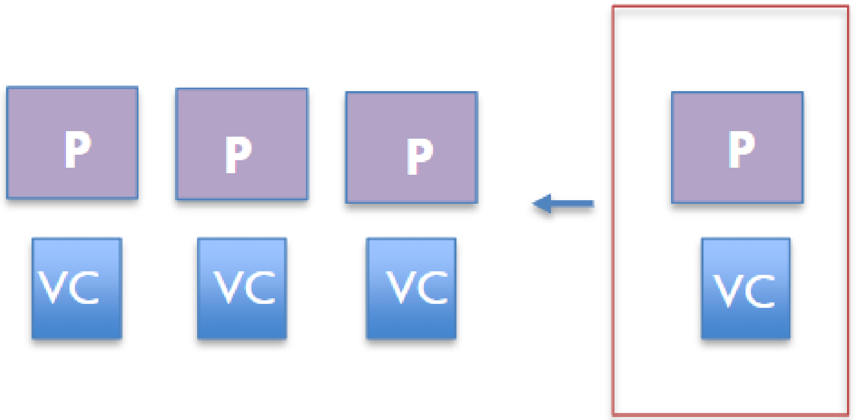
- **Variable Cost**

  Materials

  Direct Labor

  Utilities and Production Supplies

  Shipping and Freight



- **Fixed Cost**

  Rent

  Salaries

  Depreciation

  Insurance

  Interest

  Utilities

General Discussion

Company **HTU Burgers** manufactures frozen burgers to sell to supermarkets

- Materials: 200grams of meat for one burger cost $.15
- Labor: Factory worker salary is $15/hour. He can produce 100 burgers for one hour
- Cost of factory rent is $2,000 per month
- Cost of Advertising is $12,000 per year
- Cost of shipping to super markets per burger is $.25
- Cost of shipping raw materials to factory is $.20

How much does it cost to manufacture one burger (variable cost)?

What are the fixed costs per month?

Activity 2

Variable cost, fixed cost, cost/bag

Company **HTU Fashion**

Item	$	Description
Cost of Materials	1,000	per 1000 bags
Cost of accessories	1,500	per 500 bags
Factory Labor	250	per month (produces 2500 bags per month)
Factory Manager	700	per month
Electricity	500	per month (75% is factory consumption)
Shipping of materials	2,000	per container (10000 Bag)
Manager Salary	1,500	per month
Online support staff	900	per month
Advertising	24,000	per year
Machine for production	25,000	life expectancy 5 years
factory rent	12,000	per year
Office rent	400	per month
Webiste hosting fees	250	per month
Customs on raw materials	10% of value	

Product Pricing

- **Prices of products and/or services:**
- Pricing is the monetary value of a product or services that you charge to cover your total costs (direct and indirect costs) and profit that you desire on each unit of product or service.

1- Competition

2- Value-Brand

Product Pricing

3- Mark Up

- When you add a certain percentage of profit desired on the sale of a product or service, it is called a mark up. For example: If you desire to mark up the cost of a wooden cupboard by 20% and it cost you 13,000 to make, the following is the calculation;

Your Cost	= 13,00
Mark up – 20%	= 2,600
Selling Price	**15,600**
Your Selling Price	**15,600**
Cost	**13,00**
Profit	**2,600**

- Price is important in all business ventures. This is because it determines the profits that the entrepreneur will make. In setting the price, one has to make marketing mix decisions, estimate the demand curve, calculate the cost, understand the environmental factors, set pricing objectives and determine the selling price. A formula that articulates how to estimate the selling price is:

Selling price = cost of goods sold/unit + Operating costs/Unit + Desired profit/ Unit

Factors that Influence Pricing

1. Nature of the market: open market with little competition - abundant supply and low demand normally means low prices, and vice versa

2. Consumer demand for a product; customers generally buy more of a product when prices are low.

3. Costs in the distribution channel; If a product is sold through a middle-person the price charged will be affected by how that middleperson treats the product.

Definitions

- **Profit:** is net income: total earnings after expenses are considered. Profit is the money a business makes after accounting for all expenses. Making profit is the goal of every for-profit company.
- **Revenue:** the total amount of sales during a specific period, including discounts and returned merchandise.
- **Price:** the sum or amount of money or its equivalent for which anything is bought, sold, or offered for sale.
- **Sales Volume:** quantity or number of goods sold or services rendered in the normal
- operations of a firm in a specified period.
- **Expenditure:** actual payment of cash or cash-equivalent for goods or services

simple formulas

- **Profit =** Revenue **-** Expenditures
- **Revenue =** Price **x** sales volume
- **Expenditure =** Material **+** Labour **+** Transportation...
- **Price =** Cost + Profit

What you should know?

- Bank Balance
- Money coming in
- Money going out

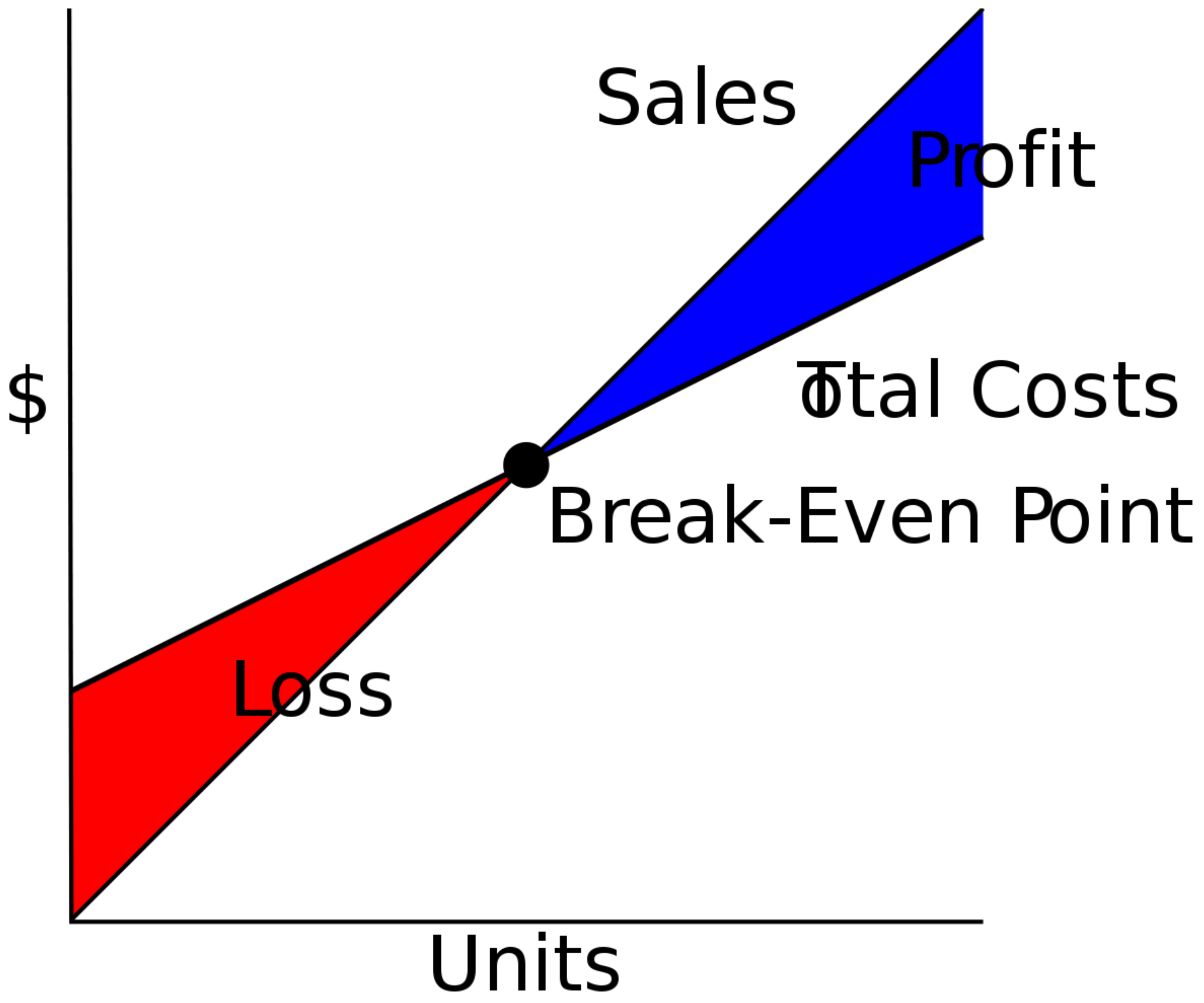
When to look at your numbers?

- Every quarter
- Every month
- Every week

Break Even Analysis

- A **breakeven analysis** is used to determine the volume of sales your business needs to start making a profit. The breakeven analysis is especially useful when you're developing a pricing strategy, either as part of a marketing plan or a business plan.

$$\text{Break Even} = \frac{\text{Fixed Costs}}{\text{Revenue per unit} - \text{Variable cost per unit}}$$


Sales
Profit
$
Total Costs
Break-Even Point
Loss
Units