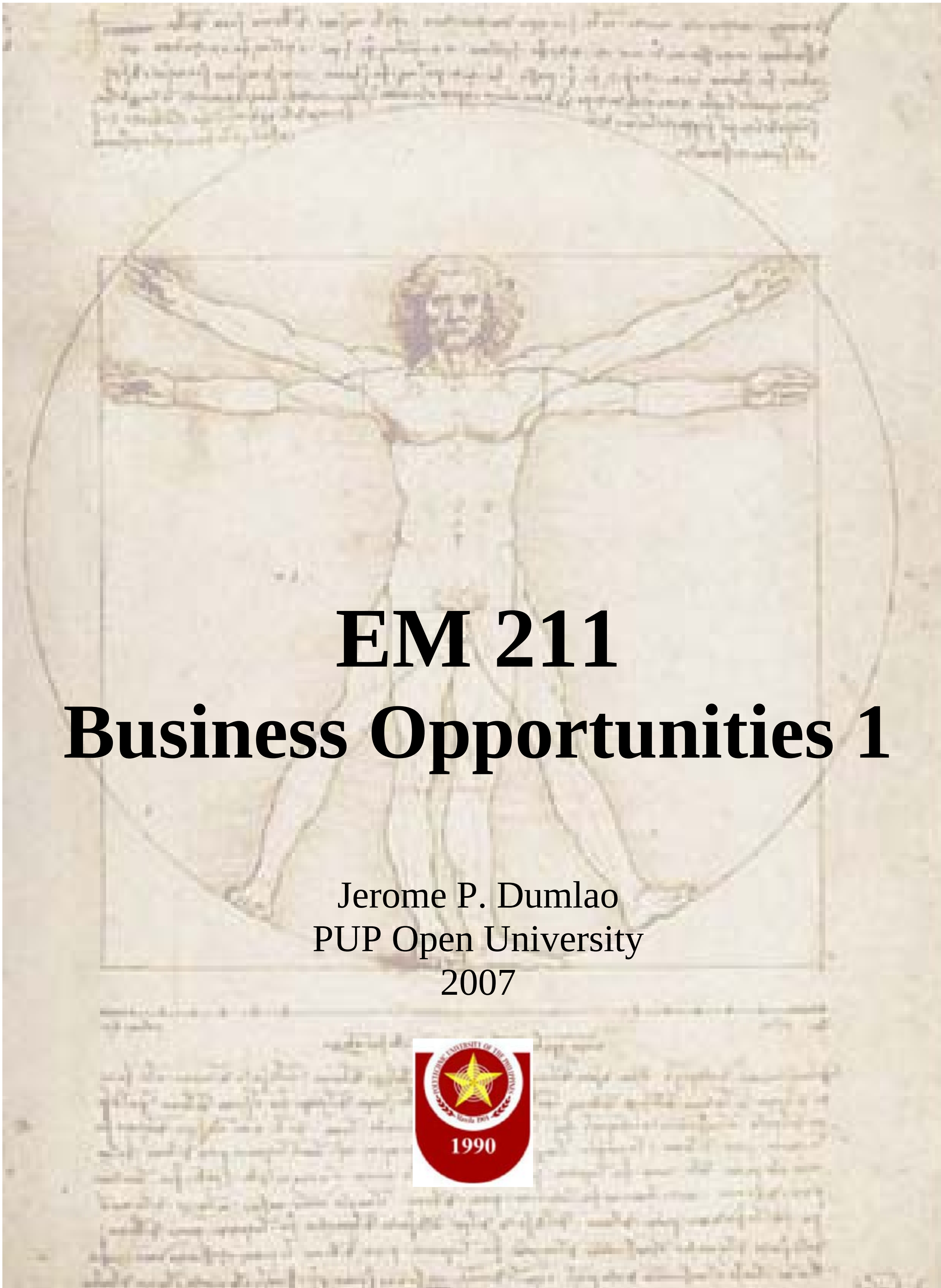

EM 211
Business Opportunities 1

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MODULE 1

THE WORLD OF BUSINESS

The world of business is an exciting one. A person needs only to indulge in it to find out that there indeed are great rewards to be gotten from it. This module will help give you some basics on what business is and what business is like in the Philippines.

OBJECTIVES:

After studying this module, the student should be able to:

1. Discuss the development of business culture.
2. Identify the different kinds of business.
3. Discuss why people go into business.

DEVELOPMENT OF OUR BUSINESS CULTURE

People have engaged in business activities since the earliest beginning of community existence. When early man produced more of a crop or caught more game animals or fish than he could consume and bartered the excess for something produced or caught by a neighbor, he was engaged in business activity.

From its simple beginnings even before recorded history, business grew and proliferated, because increasingly complex and comprehensive, until it came to dominate the overall culture of human society.

Business was already highly developed in the ancient world. Recent discoveries revealed business transactions written on clay tablets that are around 6,000 years old. The Code of Hammurabi, promulgated around 2,000 BC had provisions governing commercial transactions. Devices of business control like accounting and business functions like insurance and banking date back to the Middle Ages.

Business is equally ancient in the Philippines. It also reaches back into prehistoric times.

Historians have shown that the Philippines lies at the crossroads of ancient trade and migration. As early as the ninth century, Arab traders were already visiting the islands. By the twelfth century, Chinese traders took over most of the Philippine trade and even established trading communities in the Philippines.

The Galleon Trade was the trade between manila and Acapulco in Mexico which was carried on mostly during the 18th century. The Spanish community in Manila tried to accumulate fortunes by speculating on the annual trip of the galleon to Acapulco and back.

Business in the Philippines and in other countries of the free world is basically capitalistic in nature. This means that society entrusts the workings of the business process to the guidance of the private businessman. Business is capitalistic if we have:

1. Private ownership of non-personal means of production. Land, industrial plants, equipment, factories, transportation facilities, and other capital goods or at least the larger part of the community's capital goods are owned by individual persons or by private corporations and not the state.

2. Production for private account. This means that private initiative gives rise to production, essential for private profit. The earnings from business go to private individuals or groups.

3. Voluntary savings and institution of bank credit.

In every economy, certain basic functions have to be accomplished—the determination of what, how, how much and for whom to produce, the allocation of the goods and services produced, further growth of the economy, the distribution of economic benefits and maintenance of relations with other countries.

In a capitalist economy, otherwise known as the market economy, prices serve as indicators between the consumers and the producers. The market evolved as a result of the exchange between buyers and sellers which consequently led to the establishment of prices. The forces of supply and demand are allowed to operate with the decisions taken by buyers and sellers coordinated by movement in prices. Hence if buyers wish to purchase more than the sellers wish to sell or can supply, prices will rise. As prices increase, buyers tend to reduce their purchases while sellers increase the quantities they wish to sell. Similarly, if sellers wish to sell more than what buyers are prepared to buy, prices fall causing sellers to decrease quantity sold and buyers to increase the quantity they wish to buy.

The private owner's objective in engaging in business activities is the earning of a handsome profit as a result of the use of his productive assets. The motivation for profit serves as the greatest incentive for economic drive on the part of the owners of resources. Capitalism works along these lines although an ideal market economy could hardly be achieved due to the presence of many market imperfections with result to some problems in resource allocation.

In the Philippines, just like in any other nation, the so-called market economy does not operate in perfect situations since we can still observe the presence of economic inequalities. The resources of production are concentrated in the hands of few and the difference in purchasing power of individuals sometimes lend to distortions in coping with the basic economic functions of what, how, how much, and for whom to produce. The private owner's objective to earn the highest profit which serves as his motivating factors in production can lead to the production to luxury items affordable by few individuals but which can result in the exclusion of the needs of the masses.

Hence, in the Philippines, government regulations and interventions in the operation of the capitalistic economy are necessitated so as to meet the needs of consumers having lower purchasing power, and to promote the welfare of the majority as a whole.

KINDS OF BUSINESS

The extent and nature of business activities are almost as diverse and comprehensive as the totality of the socials and economic interest of man. WR Spreigel classifies business activities into three broad groups: Commerce, Industry and Service.

Commerce

Commerce refers to the transfer or exchange of goods and services with the movement of goods from pint of production to point of consumption. It covers buying, selling, and marketing and merchandising, which are directly involved in the transfer of goods. Under commerce are also other activities which indirectly concern the transfer of goods like collecting of goods, grading, warehousing, transportation, insurance and the financing of transfers.

Sometimes, trading business are set apart as a class but in a broad sense, trade is part of commerce. Trade may be either **retail** or **wholesale, domestic** or **foreign.**

The retail business is represented by a sari-sari store, a grocery department store. Wholesalers buy and maintain stocks of merchandise for distribution to retailers or to institutional, commercial, or industrial users, but not in significant amounts to ultimate consumers.

Under commerce, we also include a host of activities that have grown around the actual transfer of goods. The collecting of goods, their grading, warehousing, transportation, insurance and the financing of the transfer are subjects of business in themselves.

Industry

Industry is primarily concerned with the creation of form utility or the production of goods that are used either by the consumer and are, therefore, called **consumer's goods** or by other industries in the further production of other goods and, therefore, called **producer's goods.**

The broad grouping of industry is further subdivided into genetic, extractive, manufacturing, and construction industries.

Genetic industries derived from the word "genesis" or beginning, include agriculture, forestry and fish culture.

Extractive industries include mining, lumbering, hunting and fishing. They are characterized by the extraction of goods from natural resources.

Manufacturing industries are involved in the changing of raw materials of secondary products into more useful forms. The change from a basic to a more advanced form may be physical or it may be chemical.

Manufacturing industries include food, beverage, tobacco, textiles, footwear and wearing apparel, paper and paper products, printing, leather, rubber, chemical, machinery, electrical appliances, transportation equipment, and hundreds of other industries manufacturing other goods or products.

Construction industries may range from the building of multi-million peso highways, airports, and multi-story buildings to the more humble dwellings and residences were we live.

Services

Services are the third broad classification of business. These enterprises cater to personal needs of people, or with the rendering of a personal service. Businesses engaged in service are not involved in the buying and selling of goods or the manufacture of products.

Recreation services include motion picture production and distribution, theaters for drama and stage presentations, television and the like.

Personal services include such businesses as restaurants, hotels, lodging houses, laundry shops, beauty parlors, barber shops, portrait and photographic studies, and refreshment parlors.

These broad classifications, though, are not mutually exclusive. Certain businesses do not fall clearly into one classification or another but may overlap into two or three groups. Thus transportation and communication may be classified as commerce if the yare essentially intended to transfer goods. But a passenger bus or a home telephone system would be performing service. Similarly, banks, financial institutions, and insurance companies may deal in both commerce and industry or even services.

WHY PEOPLE GO INTO BUSINESS

People go into business for a variety of reasons. They may go into business as owners and employers or as an employee. The decision to go into business and not into some other activity as the priesthood or medicine or law, may be the result of conscious thought and deliberate preparation over a period of years. Or it may be due to the fact that a person finds no easier or more satisfactory way or earning a living.

Whether a person goes into business as employer or an employee, he faces the hazards of loss and other problems inherent in the conduct of business. Both owner and the employee need essentially the same personal characteristics that are required to succeed. Both also enjoy certain values which are derived when people go into business. These values are:

Social Approval

The businessman has a high social standing in the community. It used to be that society looked with greater favor upon the soldier, the landlord, the priest or the doctor. Early businessmen were looked upon as second class citizens who belonged to a lower social stratum.

Profit

The major factor of motivation for going into business is profit. Individuals enter into these activities because of the anticipation of a reward for their toiling in the form of monetary benefits. Aside from this, returns must be realized by their productive assets so as to maintain a satisfactory level of productive operations.

Service to the Community and to Employees

While profit is an important value, it is not an overriding one. There is a maxim in business which states that “he profits most who serves best.” Many businessmen render service to the community in donating money, sponsoring civic activities, setting up facilities for community needs, or providing opportunities for employment.

Service is likewise given not only to the community but to the employees as well. Industrial relations as a function of business has expanded into various activities intended for the wellbeing of employees.

Personal Satisfaction

This personal satisfaction comes about from the social status conferred on those engaged in business. It also arises from the many opportunities given the businessmen to satisfy his creative urge, his desire to witness the concrete fruits of his endeavors, and his search for self-fulfillment in what he feels is useful activity. Business is not only a means to provide livelihood but a way of life and a pattern of existence as well.

Livelihood

People go into business to earn a living. The pervasive influence of business in human activity is such that very often the only avenue where one could enter in the hopes of earning a living is to work for commercial, industrial, or service establishment.

Power

Some people enter business because they expect to rise up to positions of prestige, power and leadership. The successful businessman whether employer or manager-employee wields power in the community, exercise influence with the money or productive facilities under his control, and commands authority over the subordinates working under him. The desire for power is a craving that is human enough and is often fulfilled in a successful business.

Questions to Answer:

Kindly answer the following questions:

1. Recent discoveries revealed business transactions written on clay tablets that are around _______ years old.
2. Business in the Philippines and in other countries of the free world is basically capitalistic in nature. Explain.
3. What three characteristics must be present in order for business to be classified as capitalistic?
4. The capitalist economy is otherwise known as the ___________ _______________.
5. What are the three kinds of business? Explain each.
6. What values are derived by people when they go into business? Enumerate and explain each.

MODULE 2

ENTREPRENEURSHIP

Entrepreneurs organize, manage, and assume responsibility for new business or enterprise ventures. Their goal is to earn a profit by providing products and services everyone needs. If entrepreneurs are successful in carrying out this task, they can build rewarding careers for themselves.

Many opportunities exist to start new enterprise ventures. But before you decide to become an entrepreneur, you should find out what is involved. This module examines entrepreneurship as a career. You will see if, and how, entrepreneurship fits into your future.

OBJECTIVES:

After studying this module, the student should be able to:

1. Discuss the advantages and disadvantages of working for oneself.
2. Describe eight types of entrepreneurs.
3. Identify the characteristics common to successful entrepreneurs.
4. Estimate your personal financial needs.

WORKING FOR ONE'S SELF COMPARED TO WORKING FOR OTHERS

Thousands of Filipinos are interested in starting their own business. However, many think only of the rewards and give little thought to the risks. In this section, you will look at both the advantages and the disadvantages of being an entrepreneur.

Advantages of Working for Yourself

Those who choose entrepreneurship as a career usually do so for five appealing reasons: (1) personal satisfaction, (2) independence, (3) profit, (4) job security, and (5) status.

Personal Satisfaction. To some persons, the chief reward of working for yourself is personal satisfaction. **Personal satisfaction** means doing what you want with you life. As an entrepreneur, you will be able to spend each workday in a job you enjoy. For example, if you like photography, you may start your own studio. Each time a customer is pleased with a portrait, you will receive personal satisfaction.

You may have personal satisfaction from aiding the community in which you live. Entrepreneurs supply goods and services and create jobs for residents. They also buy goods and services from other local enterprises, borrow money from local banks, and pay taxes.

Independence. Another advantage of entrepreneurship is independence. **Independence** is freedom from the control of others. As an entrepreneur, you decide how you will use your knowledge, skills, and abilities. Compared to those who work for others, entrepreneurs have more freedom of action. They are in charge and can make decision without first getting the approval of someone else.

If you choose to become an entrepreneur, you can develop any creative ideas you have—assuming, of course, that the business is legal and that you have money to invest.

Profit. One of the major rewards expected when starting a new business is profit. **Profit** is the amount of sales income left after all expenses have been paid. Profits go to the owner of a business. Being self-employed, you would receive all the profits. Very often, increased time and effort put into the enterprise result in increased income. This is not often the case when you work for someone else.

Job Security. Many enterprises are created by persons who are seeking job security not available elsewhere. **Job security** is the assurance of continuing employment and income. Entrepreneurs cannot be laid off, fired, or transferred to another city, nor can they be forced to retire at a certain age because of company policy.

Status. Self-employed people often enjoy personal benefits, such as status. **Status** is a person's social rank or position. Entrepreneurs receive attention and recognition through customer contact and public exposure. As a result, they may enjoy status above that of many blue-collar and white-collar workers.

Closely related to socials status is pride in ownership. Most people enjoy, at least for a while, seeing their names on buildings, on stationery and business cards, and in advertisements.

Disadvantages of Working for Yourself

In addition to knowing the advantages of working for yourself, you should also be familiar with the disadvantages: (1) possible loss of invested capital, (2) uncertain or low income, (3) long hours, and (4) routing chores.

Possible Loss of Invested Capital. A risk of entrepreneurship is the possibility of losing invested capital. **Invested capital** refers to the entrepreneur's money used in starting the enterprise. As a general rule, the riskier the business, the greater the profit potential. If the enterprise succeeds, profits may be high; if not, invested capital may be lost. The entrepreneur risks losing personal and family savings. It may take years to repay banks, suppliers, or individuals who made loans to get the business started.

Uncertain or Low Income. Another disadvantage of owning your own business is the possibility of uncertain or low income. Unlike paychecks of salaried workers, profits usually vary from month to month. This is true even in well-established enterprises. When income is available, there may not be enough to meet personal and family needs. This is often the case during the first six to twelve months of operation. The level of sales and income tends to be low in these early months when the business is not known to many people.

Long Hours. Entrepreneurs are not 8-5 persons; they do not punch time cards. Many entrepreneurs work fourteen and fifteen hours a day, six or seven days a week. The owner is often the first to arrive in the morning and the last to leave at night. Business hours are set at the convenience of customers, not the desire of the owner. For example, many mall stores are open from 10 am to 9 pm. Likewise, many restaurants open before noon and do not close until after midnight. Not only are the hours long, but also the time between vacations. Some entrepreneurs feel than cannot leave their businesses for more than one or two days at a time.

Routine Chores. Running your own business may involve chores you d on not like. For example, new business owners expect to do some paperwork. However, many do not realize how much is required until the business is started. By that time, some feel they are buried under a mound of paper. One of the surprises is the extent of record keeping for items such as billing, payroll, and taxes. Maintenance and cleaning are other chores that must be performed each day. While it is possible to hire employees to perform these routine duties, a shortage of cash may prevent owners from doing so.

IDENTIFYING TYPES AND CHARACTERISTICS OF ENTREPRENEURS

An entrepreneur is a person who attempts to earn a profit by taking the risk of operating a business enterprise. While all entrepreneurs may have certain characteristics in common, no two entrepreneurs are exactly alike.

Types of Entrepreneurs

Entrepreneurial characteristics combined in different people result in different types of entrepreneurs. Entrepreneurs are classified into the following types: (1) solo self-employed individuals, (2) team builders, (3) independent innovators, (4) pattern multipliers, (5) economy-of-large-scale exploiters, (6) capital aggregators, (7) acquirers, and (8) buy-sell artists.

Solo Self-Employed Individuals. Entrepreneurs who work alone or with only a few employees are known as **solo self-employed individuals**. They generally perform the work themselves rather than assigning it to other people. Solo self-employed individuals are perhaps the most numerous of all entrepreneurs. Their ranks include small store and repair shop owners, independent sales representatives, attorneys, and physicians.

Team Builders. Entrepreneurs who expand small, usually one-person businesses into larger companies are **team builders**. An example is a self-employed electrician who gradually hires additional employees until a full-scale electrical contracting firm is established.

Independent Innovators. Individuals who create companies to manufacture and sell products they have invented are **independent innovators.**

Franchisers. Entrepreneurs who build several units of an effective business are known as franchisers. The entrepreneurs may have designed and built the original business, or they may have purchased a business started by someone else. Once this type of entrepreneur is successful with a business, the entrepreneur establishes for profit similar units elsewhere. Perhaps the best example of this type of entrepreneur is one who perfects a method of doing business and sells it to others.

Economy-of-Large-Scale Exploiters. When a firm has lower average costs due to its large sales volume, economies of large scale are involved. Entrepreneurs who can sell a large volume of goods at reduced prices are **economy-of-large-scale exploiters**. Discount store operators are one example of this type of entrepreneur. Because of the larger scale of their establishments, the may be able to afford advanced and specialized equipment such as the scanners built into the checkout counters at some larger supermarkets. This equipment enables one cashier to handle more customers in less time, thus lowering the store's payroll expense because fewer cashiers are needed. Economy-of-large-scale exploiters often obtain merchandise at a price discount because they buy in such large quantities.

Capital Aggregators. Entrepreneurs who take the lead in establishing financial institutions that require a large amount of start-up capital are **capital aggregators**. Those who start banks and insurance companies are examples of this type of entrepreneur.

Acquirers. People who become entrepreneurs by buying an existing business are **acquirers.** Finding a business that someone is ready to sell is not usually difficult. Check the classified section of your local newspaper. You may be surprised at the number and variety of businesses for sale in your community.

Buy-Sell Artists. Rather than making their money from the day-to-day operations of a business, **buy-sell artists** turn profit by buying a business and then selling it at a higher price. Buy-sell artists usually buy companies with problems that they solve before they sell the company. Typical actions include reducing costs and payrolls and eliminating unprofitable products. IN most cases, buy-sell artists do not wish to own a particular company for more than a few years.

Characteristics of Successful Entrepreneurs

Whatever type of entrepreneur, successful entrepreneurs are often described as being persons who (1) take moderate risks, (2) have self-confidence, (3) work hard, (4) set goals, (5) are responsible, (6) are innovative, (7) have technical knowledge, and (8) have business knowledge.

Moderate In Taking Risks. Persons who quit secure jobs and invest money in a new enterprise have much at stake. They are taking a risk. Their businesses may succeed and provide profits for years to come. On the other hand, the business may fail and cause financial ruin. Entrepreneurs are willing to take middle-of-the-road or moderate risks. **Moderate risks** means the chances of winning are neither too small nor too great. That is, results are not left purely to chance, nor are they sure to happen. Instead, they depend on a person's abilities and actions.

Entrepreneurs like challenges suited to their skills. They want to make things happen rather than let them happen by chance.

Self-Confident. Successful entrepreneurs have self-confidence. **Self-confidence** means believing you can achieve what you set out to do. You are not afraid to take chances. You know you can get the job done. This strong inner feeling about oneself is important for the owner of a small business. It can often spell the difference between success and failure. Self-confidence sustains the owner during the difficult times in the growth of the new business.

Having self-confidence also means you are realistic and you know the limits of your abilities. You know what you can and cannot do. Entrepreneurs are not afraid to ask for help with difficult tasks.

Hardworking. Creating a new enterprise is hard work. Helping customers, keeping accounting records, and cleaning are just a few duties you may have to perform on a given day. You may also have to make deliveries, order supplies, and repair equipment. Much work must be done with few, if any, employees to help. Therefore, good health and physical stamina are important.

Only when their businesses are firmly established do entrepreneurs feel the freedom to put in fewer hours. Even then, however, they are ready to work when a job must be done.

Goal-Oriented. Do you know what you want to achieve in life? Successful entrepreneurs know where they are going by setting goals. A **goal** is an objective, something you plane to achieve. Your chances of becoming a business owner are slim unless you first decide you want to own your own business.

An example of a goal could be to get a summer job in a fast-food restaurant. Another example could be to have your own fast-food restaurant within five years.

You should learn to focus on one goal at a time. Direct all your energy toward this goal. When you have attained it, go to the next goal. If you try to pursue several goals at once, you can become confused and lose sight of your target.

Responsible. When you are **responsible**, you answer or account for what happens. You accept blame for failure, and you accept credit for success. An as entrepreneur, you will be responsible for the success or failure of your business. You will set goals and hold only yourself responsible if they are not met.

Entrepreneurs have many responsibilities. They must pay debts and wages. They must keep promises to employees or customers. They must also be willing to make personal sacrifices. For example, during busy seasons, the owner may not be able to take vacations with the family.

Innovative. Successful entrepreneurs are **innovative** because they introduce new ideas or methods. They try to improve existing products and services or create new products and services. Entrepreneurs invented fiberglass snow skis, video games, ballpoint pens, zippers, and automatic transmissions. They also introduced fast-food restaurants, quick oil change shops and computer shops.

Perhaps you have a new idea for a gift shop, a landscaping service, or a day-care center. Of course, not all ideas can be turned into profitable businesses. If you find one that can, you may build a satisfying career for yourself.

Knowledgeable About Technical Factors. You must have technical knowledge to succeed as an entrepreneur. **Technical knowledge** is what you know about a product or service. For example, a photographer must know how cameras operate. A pet shop owner must learn about the care of animals. A printer must have knowledge of different printing presses, inks, and papers.

One way to gain technical knowledge is by taking classes in school. You may also gain technical knowledge from a hobby or from a job in your area of interest. Make sure you have technical knowledge before you start a new enterprise.

Knowledgeable About Business Factors. You will also need business knowledge. **Business knowledge** is knowing how to operate the enterprise. Entrepreneurs must see that all tasks are performed appropriately. Examples are helping customers, setting prices for products and services, paying bills, planning advertising, and keeping accounting records.

ESTIMATING YOUR PERSONAL FINANCIAL NEEDS

It may be months or even years before the enterprise can provide you with enough money for living expenses. Every year, promising new enterprises are closed before they really get a chance to prove themselves. The owners simply run out of money and must obtain salaried jobs to support themselves and their families.

It is important, therefore, to estimate your personal financial needs. Do this for a period of three to six months. Then make sure your will have the money to cover that time period. If the money will not be available, you would be wise to delay the starting of the enterprise.

Questions to Answer:

Part I.

Kindly answer the following questions.

1. What are the advantages and disadvantages of working for yourself?
2. Enumerate the eight types of entrepreneurs. Explain each.
3. List the characteristics of successful entrepreneurs. Explain each.
4. What are the five factors you should study before getting into franchising? Elaborate.
5. Compare the three ways of going into business by writing the advantages and disadvantages of each.

Part II.

Analyze the following case and answer the questions.

OLD STATION RESTAURANT

Twenty years ago, when the bus company decided to close the station near the edge of town, Carolyn and Jeffrey Milano leased the property. They remodeled the building and opened the new business, the Old Station Restaurant. The menu consisted of lunch, dinner and an assortment of desserts.

Carolyn and Jeffrey's ideas about the type of restaurant that would be successful in town must have been correct. The Old Station Restaurant has been both popular in town and profitable to the Milano family.

Within the last few years, the dessert items on Old Station's menu have gained a reputation of their own. Many people buy a whole cake or pastries to take home with them. Even those who have eaten dinner at home or in another restaurant will have their dessert at the Old Station.

Katherine Milano, Carolyn and Jeffrey's daughter, is now managing the restaurant. In studying the various items on the menu, she found that desserts are the highest profit items. Following a discussion with her parents, she has decided to package dessert items, particularly cakes and pastries, and distribute them for sale through supermarkets in the area. The brand name that has been chosen is "Old Station Dessert Goodies."

The business, which will be reorganized and called Milano Foods Company, will consist of two divisions: Old Station Restaurant Division and Old Station Dessert Goodies Division. Katherine will be president of Milano Foods and will continue to manage the restaurant. She is in the process of hiring a manager for the dessert division. Several people applied for the job by sending their personal data sheets to Katherine. She has narrowed the choice to two people: Ralph Adamos and Michelle Sison. However, Katherine is having rouble making the final selection. Both Ralph and Michelle appear to be qualified for the job, and they each made good impressions in their interviews. When she asked them to describe briefly how they would operat the dessert division, Ralph answered, "As the manager, I would oversee the day-to-day operations of the business." Michelle said, "I would run the dessert division just as an entrepreneur would."

Questions:

1. Which of the two people should Katherine hire? Why?

2. Would a person who has the characteristics of and entrepreneur be happy working for someone else? Give details.
3. Assume that Katherine wants to hire Michelle, but Michelle will accept the job only if she is allowed, in most cases, to run the business as an entrepreneur. Is there anything Katherine could do that would satisfy Michelle's request? Explain.

MODULE 3

FINDING IDEAS FOR BUSINESS VENTURES

New business ventures appear in the marketplace everyday. Indeed, relatively new companies provide many of the products and services we use daily. Many of these ventures were started by entrepreneurs or businessmen. This module discusses sources of new ideas for business ventures and methods of generating new venture ideas.

OBJECTIVES:

After studying this module, the student should be able to:

1. Describe sources of ideas for business ventures.
2. Explain formal and informal surveys.
3. Discuss how brainstorming, observations, and notebooks can be used to develop new business venture ideas.

SOURCES OF IDEAS FOR BUSINESS VENTURES

If you want to be an entrepreneur, you should be alert at all times for new or more efficient ways to meet the needs and wants of customers. These ideas can come from many sources, and they can appear at any time. Some people find ideas for new business ventures while reading newspaper or magazines. Others discover ideas while they are pursuing a hobby or when they are attending a merchandise show or a craft and hobby show.

Newspapers

A convenient way to begin the search for new enterprise ideas is to read your local newspaper. When reading, pay attention to the classified section. **Classified advertising** (often called *want ads*) consists of advertising messages grouped together in one part o the newspaper under headings such as *Help Wanted, Cars for Sale, Business Opportunities,* and *Business Services.* The most helpful headings when looking for enterprise ideas are *Business Opportunities* and *Business Services.*

Business Opportunities. People wanting to sell their businesses often advertise them in the business opportunities section of classified advertisements. **Business opportunity advertisements** usually describe the enterprise to be sold, the location, and sometimes the selling price. One way to become an entrepreneur is to buy an existing business. Therefore, you should now what businesses are for sale in your community.

Business opportunity advertisements can be important to you for other reasons. For example, if you have decided to study entrepreneurship opportunities in a particular industry, the ads can help you select a specific type of enterprise.

Assume you are interested in opening a food service establishment. By reading advertisements, you can get a good idea of the variety of business ventures available in the food service industry. Once you are aware of what is available, you can determine if any match your interests or abilities.

If your career plans are uncertain, business opportunity advertisements can offer a lot of clues to what your interests are.

Business Services. Persons with specialized business or technical skills to sell reach potential customers through **business services advertisements**. IN these ads, it is the service that is for sale, not the enterprise providing the service.

Business services advertisements can be helpful as you think about your future. You may have taken a bookkeeping or accounting course at one time because you thought about working in a bank or in another local business. Did you realize that you could also use these skills in your own enterprise? Business services advertisements have helped many people become aware of new career paths.

Newspaper Articles. Entrepreneurs must be alert to the world around them, and they can stay informed by reading newspapers regularly. Ideas for new business ventures are found frequently in newspaper articles. Look for articles describing new types of businesses.

If you are going to start a new business enterprise, you may want to concentrate your efforts on products or services with large sales potential. Pay attention to news items that signal changes in consumer needs. Such changes often mean that consumers will buy either more or less of certain products or services. For example, you may read that there is more interest in physical fitness. Therefore, look for new enterprise ideas that are related to physical fitness, such as selling sporting goods or health foods. Other examples are health spas and organic farming.

Magazines

Special-interest magazines and trade publications have other ideas for new business ventures.

Special-Interest Magazines. Articles and advertisements in specific areas of interest appear in **special-interest magazines**. An article in a camping magazine may prompt you to ask, “Why isn’t there a camping supply store in my town?” Your pursuit of an answer to the question may be the starting point for a new enterprise. Likewise, you may get the idea to rebuild and sell used dirt bikes from reading a motorcycle magazine.

To find special-interest magazines you like, check with relatives, friends, and the school and public libraries. Many special-interest magazines are sold by subscription and on newsstands and magazine racks in stores.

Trade Publications. Magazines and newspapers designed for people working within a particular business or field are known ad **trade publications**. They contain helpful information regarding new products or services likely to become popular soon. You will find information in the articles as well as the advertisements. Trade publications are available in many libraries.

Hobbies

Hobbies are activities you pursue for pleasure and relaxation. They are often the source of ideas for new business ventures. For example, if you enjoy buying and selling antiques and other collectibles, you may be able to expand you hobby into a profitable full-time enterprise. A business related to your hobby will enable you to spend more time doing what you enjoy most.

Merchandise Shows

Another way to find ideas for new business ventures is to attend merchandise shows sponsored by manufacturers and distributors. Two types of merchandise shows are public and trade. Each serves a different purpose.

Public Shows. Places where manufacturers and distributors display and demonstrate their products to the public are called **public shows**. They are open to all persons who wish to attend. An admission fee may be charged in some cases, and shows may last several days. Public shows are often held in fairgrounds buildings, convention centers, or sports arenas. Watch for newspaper advertisements about public shows.

When you go to a public show, you will see salespersons and product demonstrators who will answer your questions. Leaflets and brochures describing products are usually available.

By visiting a public show, you may discover an enterprise idea that matches your interests and abilities.

Trade Shows. Often exhibits of products from many suppliers will be organized by groups of manufacturers or wholesalers. These are known as **trade shows**, and they are open only to people engaged in a particular line of business or trade. Salespeople are on hand not only to accept orders and set up delivery dates but also to discuss the latest trends and products. Shows are held in trade areas such as apparel, furniture, hardware, house wares, sporting goods, books, jewelry, computers, and office equipment.

Trade shows can be sources of new enterprise ideas. After attending a show of computer equipment, for example, you might decide to look for entrepreneurship opportunities in that field because of its growth potential.

You must realize that trade shows are not held everywhere. They are most frequently found in the larger cities. Remember that admittance to trade shows is limited to members of the trade and that there may be an admission fee. If you would like to attend a show and are not working in the trade, a friend in the appropriate trade area may take you as a guest.

Craft and Hobby Shows

Crafts and hobby shows are places where people show others what they do in their spare time. For example, con collectors may display their collections for all to see. Those who work with pottery may demonstrate the craft for others.

You may get ideas for new business ventures by observing activities at craft and hobby shows. You usually do not have to look too far to find a craft or hobby show. They ar held frequently in local shopping malls, convention centers, exhibit halls, or parks. Be alert for newspaper announcements that tell the place, date, and time for a show in your area. You should also be prepared to pay a small admission fee at some of these shows. What craft and hobby shows are held in your community?

METHODS OF GENERATING NEW BUSINESS VENTURE IDEAS

Some new enterprise ideas are found by chance. Most, however, come from the entrepreneur's conscious efforts. You can generate ideas for new business ventures by conducting surveys, brainstorming, making observations, and keeping a notebook.

Conducting Surveys

One way to stimulate ideas for new business ventures is to find out what consumers need and want. You can obtain this information from surveys. A **survey** involves asking a number of people a series of questions and then summarizing their answers. Surveys can be either informal or formal.

Informal Surveys. You can conduct an **informal survey** by talking to your family and friends. You may ask them what new businesses they think are needed in town, or you may ask if there are products or services they are not able to purchase locally. Another way to get some information is to ask: If you were to start your own business, what would it be? What products or services would you offer? Why? Answers to these questions may give you new enterprise ideas to think about.

When you observe business activity in the community, you are conducting an informal survey. Observation might reveal the need for particular business ventures. Perhaps there is no bicycle repair shop in town, and there appear to be many bicyclists in the area. Maybe you have noticed that a catering service I needed for parties. If you live near a tourist or resort area, you may be able to sell items made by local artisans.

Formal Surveys. A **formal survey** involves their interviewing many people or asking them to complete a questionnaire. Contact persons from throughout the community, especially those who are potential customers for the new enterprise. Formal surveys are useful in identifying shortcomings or weaknesses in existing business ventures and in determining needed products or services.

Brainstorming

Another method of generating ideas for new business ventures is brainstorming. **Brainstorming** is a technique used to solve a problem by generating as many ideas as possible. You may use brainstorming in a group or by yourself.

As you search for new enterprise ideas, you will probably brainstorm by yourself. However, you may be able to do this more effectively if you first learn how this technique works in a group.

You can get practice in brainstorming by getting together with two or three people. One person should be the leader and another the recorder. The recorder's job is to list the ideas as they are stated. Compile the ideas on a chalkboard or flipchart for everyone to see.

Brainstorming begins with a question from the leader. Someone in the group suggests an answer, then everyone else changes it or adds to it. Each idea leads to one or more ideas. The result is a chain reaction of ideas.

In addition to getting the session started, the leader must keep it going. The leader should be ready to add an idea when others run out of ideas. This often restarts the process. Follow these rules in the brainstorming group:

1. *Don't criticize another person's ideas.* Group members will tend to talk less if this happens. This means fewer ideas will be expressed.
2. *Encourage freewheeling.* The wilder the ideas, the better. It is easier to tame down a wild ideas than it is to think up another one.
3. *Try for quantity.* The larger the number of ideas, the better the chance of getting good ones.
4. *Combine and improve.* Group members should state their own ideas. They should also suggest how the ideas of others could be turned into better ideas. Sometimes two or three ideas can be joined to form still another idea.

Even though brainstorming is used most often in groups, you can also use it alone. Follow these rules for individual brainstorming:

1. *Don't judge your own ideas until you have finished the list.* Never erase or scratch out an idea.
2. *Do some freewheeling.* Don't be afraid to write down some unbelievable ideas.
3. *Try for quantity.* Remember, by writing down many ideas, you increase your chances of getting good ideas.
4. *Combine and improve.* Write down all ideas that come to mind. Then add to the list by combining and improving ideas.

Making Observations

An idea for a new enterprise may come from observing your own needs and wants or by observing the needs or wants of the people around you.

How observant are you? Before you answer that question, see if you can answer these questions:

- On which corner is the name of your street posted?
- Is there a stairway in your home or school? How many steps does it have going from the first to the second floor?

Even if you answered these questions correctly, you may still agree that people do not always observe their surroundings. Observation is an active process. If you are not actively trying to observe, you probably will not observe.

Sharpen your observation skills, and you will improve your chances of finding new enterprise ideas. You can do this by the following actions:

1. *Watch trends, particularly those in food, clothing, and leisure-time activities*. Entrepreneurs have responded to people's interest in physical fitness by providing exercise clothing, equipment and instruction. Some restaurants provide nutritional information for their menu items. Be alert. Trends in other parts of the country and the world may be clues to future trends in your area. What foods or clothing styles are moving from one part of the country (and the world) to another?
2. *Observe faults or shortcomings in existing products, services, or businesses*. Did the store where you bought a gift provide a box for the item, and was gift-wrapping service available? If not, you may have discovered the need for a new business—an enterprise that would wrap gifts and, if needed, pack the item for shipping to another city. Busy people are willing to pay for these services.
3. *Look for new associations among objects, processes, and ideas*. See if you can take the idea from one line of business and use it in another. Pizza parlors have provided home delivery for years. Fast-food restaurants serving hamburgers or chicken, on the other hand, have generally offered this service. Combine the two ideas to create a new concept, that of a hamburger or chicken restaurant that delivers to the home.
4. *Observe that some things that used to be done very well are not done any more*. At one time, gasoline stations could handle practically any automobile repair problem. Should somebody establish full-service gasoline stations in areas where they no longer exist?
5. *Try out your idea on other people*. Ideas must be tested. When you get an idea for a new product or service, plan to develop and refine it. This could take weeks, months, or even years. Tell your idea to your friends. Observe how they react to the idea and listen to what they say. Are they enthusiastic? Do they encourage you to keep working on the idea? Most important, do they think your product or service is a gimmick, or do they believe it has value?

Keeping A Notebook of Ideas

Ideas for new business ventures can come to you at any time. They often come at times when you least expect them, such as while you are eating lunch, riding in a car, or watching television.

At the moment an idea appears it may seem that it would be impossible to forget it. Yet in a very short time it becomes blurred or is forgotten. Be prepared to catch ideas while they are alive and fresh in your mind. As soon as you get an idea, write it down. Keep track of your ideas in a notebook. If you get an idea when you do not have your notebook with you, write it down on a scrap of paper. Then add the idea to the list in your notebook as soon as you can.

Plan to spend time at least once each month or review your notebook of ideas and to answer these questions:

1. What are the advantages or benefits of each enterprise idea?
2. What are the disadvantages or drawbacks of each idea?
3. Does the great idea you had a few weeks ago still seem great?
4. Do the ideas have anything in common? For example, are several ideas related to computer or electronics?
5. Does the list of ideas suggest that your interests are changing? Perhaps the enterprise idea you had several weeks ago was to start a small retail store. However, now you may be setting your sights on a large-scale manufacturing business.
6. What is the best idea in the notebook? Why?

Questions to Answer:

Part I.

Kindly answer the following questions.

1. How can business opportunity advertisements help you if your career plans are uncertain?
2. What types of newspaper articles should you read when looking for new enterprise ideas?
3. Why are trade publications good sources of new enterprise ideas?
4. Describe the differences between public shows and trade shows. Give an example of each type of show.
5. List two ways you can make an informal survey.
6. What is the meaning of this statement: “The existence of several businesses of one type does not necessarily mean you should not start a similar enterprise”?
7. Explain the rules for individual brainstorming.
8. What are way to sharpen your observation skills? Describe briefly.

9. List six questions you should answer when reviewing your notebook of ideas.

Part II.

Analyze the following case and answer the questions.

LUZVISMIN PARTNERS

Ann, Bob, Charlie and Diane have been friends for almost two years. They met when they were all assigned to the same unit at Camp Aguinaldo in Quezon City. Within the next six months, they will all be completing their enlistments, and they will be leaving military service. Charlie and Ann each have sixty days left to serve. Diane has four months left and Bob has almost six month.

The four friends agree that their military service has been a valuable experience. At the same time, each of them is looking forward to pursuing a career as a civilian. They often talk of starting their own businesses. Recently, they have been talking about going into business together. This is a possibility because they all want to stay in Quezon City.

At lunch on Monday, Charlie said, "Let's meet for at least two hours each week to talk about a business we could open together. At least for now why don't we call ourselves the Luzvismin Partners. It's a good name because each one of us grew up in a different part of the Philippines."

With only sixty days to prepare for his return to civilian life, Charlie is eager to plan his career. He continued, "If we're serious about going into business together, and I think we are, we should get some plans on paper real soon." Ann said, "I agree, but we can't start planning until we decide what business we want to start. I think we should do some brainstorming when we meet next week. That should give us many business ideas to consider." "Great suggestion," Charlie added, "but I think we should agree on some rules for the brainstorming meeting; otherwise it'll get out of hand. I was in one of those meetings once. The whole discussion went off in several directions." Bob came into the discussion and said to Charlie, "Go ahead and suggest some rules." "All right," Bob said, "here are two rule: First, we should each come prepared with a list of ideas so we won't waste time trying to think up ideas at the meeting. Second, no wild ideas will be allowed. If we follow these rules, I think we'll have a good brainstorming session."

Questions:

1. Do you agree with Charlie that each person should come to the brainstorming meeting with a list of ideas? Why or why not?
2. What will happen if wild ideas are not allowed? Explain.
3. Describe how you would set up and conduct the brainstorming meeting.

MODULE 4

ANALYZING MARKETS AND COMPETITORS

Customers do not buy *things*, they buy *solutions to problems*. One person may buy a bicycle to solve a transportation problem. Another person may buy a bicycle to solve an exercise, or lack-of-exercise, problem. The purpose of business, therefore, is to help people solve problems.

Your enterprise will be just one of many businesses competing for customers. To survive and prosper, you will have to look constantly for better ways to help people solve their problems. Maybe you will provide a new service, make a new product, or design a new and more convenient package for an old product. Whatever you do, you will need customers, preferably many of them. Without customers who want your product or service and are willing and able to pay your price, there is no need to be in business.

To help customers solve their problems, you will have to learn about the customers and the markets of which they are a part. Because other businesses will probably be trying to do the same thing, you will also have to find out as much as you can about the other businesses. In this module, you will learn methods of analyzing your markets and your competitors.

OBJECTIVES:

After studying this module, the student should be able to:

1. Describe the process of market segmentation.
2. Explain sales forecasting.
3. Identify the characteristics of a good location.
4. Evaluate the competition.

ANALYZING MARKETS

The word **market** is sometimes confusing because it seems to have so many meanings. IN newspaper headlines you may have read "Investors put more money into the stock market," "Job market tight in many cities," or "Commercial real estate market improves." Television newscasters often mention the new car market or the international market. We buy groceries in a supermarket and food from the wet market. These are just a few of the markets you hear everyday.

The Market for a Business Venture

Before you decide to start a new enterprise, you will have to identify your market. In this sense, **market** refers to the groups of people, businesses, or organizations seeking the types of products ore services you sell. Customers must also be both willing and able to pay the price you charge; otherwise, they would not be a part of your market.

Persons or households that buy products and services for personal or family use are called **consumers**. They buy products from a wide variety of sources, including retail stores, mail-order companies, and door-to-door salespeople. Consumers also buy services from such business ventures as auto repair shops, restaurants, cable television companies, and photography studios.

Business users are companies or institutions that buy products and services to use in running their businesses, to resell, to produce other products or to provide services. Schools buy desks, floor wax, and paper. Sporting good stores buy basketballs, athletic shoes, and tennis rackets to resell to customers. Wholesale grocers buy from producers to resell to supermarkets, Furniture manufacturers buy wood and upholstery fabric to make tables, chairs, and sofas. These are examples of the many purchases businesses users make each day.

Market Segments

Some entrepreneurs start out trying to meet the needs of every possible customer. In other words, they try to be "all things to all people." They scatter their efforts and energy. In the end, they do not serve anyone very well. A better way is to concentrate your efforts on market segments. **Market segments** are groups of people with similar needs and characteristics. Think of the market as a pie and a market segment as a slice of that pie.

Market Segmentation

Dividing the market for a product or service into segments is **market segmentation**. Each segment consists of customers who are alike in many ways. The particular group to whom you wish to sell your products or services is your **target market**.

Large corporations offering different products often have several target markets. Car manufacturers, for instance, produce several models. Each model is usually designed to meet the needs and preferences of people in a particular target market. However, when starting a new business, the best advice is to select just one target market. When, and if, you are successful in serving that one group, you can start thinking about other target markets.

Learn as much as possible about your target market. You can do this by asking yourself these questions:

1. Will my customers be consumers or business users?
2. If they are consumers, how old are they? How much money do they earn? Where do they live? Are they in cities, suburbs, or rural areas? Are they more likely to men or women?
3. If they are businesses users, are they extractive, manufacturing, wholesaling, retailing, or service ventures?
4. What needs will the product or service satisfy for customers?
5. How many potential customers are in the area where I will open my business?
6. Where do these potential customers now buy the products or services I want them to buy from me?

7. What price are the customers wiling to pay?
8. What can I do for customers that competitors are not doing for them?

Develop a mental picture of customers in your target market. Then try to put yourself in their place an see your enterprise as they see it. Do this when you start your business and do it every day you are in business. Never stop studying your market because it will continually change. Neighborhoods change, customers' needs and buying habits change, and new products replace old products.

Sales Forecasts

Forecasting sales is essential for every business enterprise, regardless of its size or the field of activity. The forecast is the basis of sound planning. Without it, you will not know how much merchandise or raw material to buy, how many employees to hire, or how much money you will need.

What Is a Sales Forecast? A **sales forecast** is an estimate of sales, in pesos or units, for a specific time period. The forecast may be for a specific item or service, or for the enterprise's total sales volume. One year is the most widely used time period. However, some entrepreneurs prepare sales forecasts for periods of three or six months.

Forecasts of less than a year are often desirable when sales fluctuate widely from month to month. Sellers of seasonal products or services often find that it is not practical to look ahead a full year. Some product examples are summer and rainy day clothing, Christmas decorations, and home appliances such as room air conditioners.

Review sales forecasts frequently and revise them as necessary. New competitors, or price changes by existing competitors, can make your estimates obsolete. Therefore, many business persons review their annual sales forecasts monthly. In this way, they can respond quickly to changes that affect the enterprise.

How Is a Sales Forecast Prepared? The first step in forecasting sales is to estimate the market potential for your products and services. The term **market potential** refers to the total sales of all similar businesses in your area. In other words, market potential is the total of your sales and those of your competitors.

To determine market potential, be prepared to go to several sources for information. Start by visiting the local chamber of commerce and the library. Also, contact the trade association of your line of business. Virtually every industry has such an association; ask those who are already in business for the address. The information from these sources is usually in the form of nationwide averages. That is, the information may not refer specifically to your local area. Nevertheless, the information is useful because it can give you the background for further study of your market.

Next, you should seek the help of a banker or an accountant. These individuals are familiar with the sales and finances for a wide range of business ventures. For this reason, they can help you to estimate the potential for your market.

Other potential sources of information are those businesses that sell to a business venture similar to yours. Examples are manufacturers, wholesalers, and suppliers who conduct business regularly in the community. Finally, locate an entrepreneur in your line of business but not in your community. Because you will not be competitors, this person may be willing to share information about the market potential.

After you have estimated the market potential, you should estimate your share of the market. This will be your sales forecast. The estimate is important because it is the basis for almost all other decisions you will make.

Suppose, for example, that you are starting a printing business. You want to specialize in business cards, letterheads, envelopes, and business forms. You find that P10,000,000 is spent on this kind of printing each year in your community. This is the market potential.

There are four printing shops, but when you open yours, there will be five competing businesses. To compute **average market share**, divide market potential by the number of competing business. Using the numbers from the example, the computation would be as follows:

$$\text{Average Market Share} = \frac{\text{Market Potential}}{\text{Number of Competing Businesses}}$$

$$= \frac{\text{P10,000,000}}{5}$$

$$= \text{P2,000,000}$$

The average market share is P2,000,000. You should not assume that you will reach this level of sales your first year. You are new and the other businesses are established. However, you should try to estimate how much of that P2,000,000 you can get. You can do this by observing your competitors to find answers to these questions:

1. What are their successful sales points?
2. What are their weaknesses?
3. What can you provide that they do not provide?
4. How much business can you actually take away from competitors?

Avoid the tendency to overestimate these figures, however.

Based on these answers, you may estimate that your sales will be P1,400,000 for the first year. The estimate is not as high as average market share, but you are just getting established. Review your initial estimate no later than three months after opening. At that time, you may have to adjust the estimate either upward or downward.

For example, because of superior products or services, you may be taking more business away from competitors than originally planned; or the total market potential may have increased because there are new customers in the area. These factors would cal for an increase in your sales forecast. On the other hand, you may have to decrease the forecast if for instance a new competitor appeared, or not all your equipment was installed on time.

Location

Location is the place where you have your main base of operation. Wherever you locate, make sure the community needs the business you want to start. Deciding on the location for a new enterprise involves three steps. You must (1) choose a community or city, (2) choose an area within the community or city, and (3) choose a specific site in the area.

Choose a Community or City. Certain communities are more desirable than others as locations for new business ventures. In choosing a community, you should consider (1) personal factors, (2) population, (3) level of employment, (4) competition, and (5) legal considerations.

Personal Factors. One of the advantages of being an entrepreneur is that you can choose where you will work. You are free to pick a place where it would be pleasant to work and probably live. Factors that make a community pleasant often make it a good place for conducting business. Look at the general appearance of the town. Are most homes neat, and are streets and parks well maintained? What about public transportation and public utilities (such as water, electricity, and sewage)? Do these services meet local needs? Determine the quality of schools as well as police and fire protection. In short, find out if residents take pride in their community.

Population. A community's population is an important factor in location. Are there enough customers for your products or services? Is the population growing or declining? Given the choices, you will probably want to locate in a fast-growing city. Construction of new homes, apartments, and shopping facilities is an indication of growth.

Level of Employment. Spending for some goods and services is low in cities where many persons are unemployed. Places with unemployment problems tend to be poor locations for businesses intending to sell to local consumers. The same cities, however, could be good locations for other businesses. One example is the entrepreneurs who will hire many employees for a manufacturing company. Or if you intend to put up an employment agency, such a place will be a good location for your endeavor. Local conditions, however, would not affect a product sold in other cities.

Competition. Overcrowding occurs in many fields of business activity. Therefore, you should be concerned with the nature and amount of local competition. Determine the number, size, and quality of competitors. Then decide if there is likely to be room for your new enterprise.

Legal Considerations. Some cities and provinces try to attract new businesses by offering tax advantages. Others have unusually high taxes or restrict certain businesses. Taxes and restrictions mean higher costs of operating a business. You should, therefore, inquire about these items when considering a location. Also, check on zoning ordinances that limit your selection of sites in the town.

Choose An Area Within the Community or City. After choosing a city in which to locate, the next step is to choose an area within the city. Your goal will be to find an area that is suited to your type of enterprise.

The location decision is more important for some types of business than for others. For instance, a variety store should be conveniently located for shoppers. If it is hard to find, customers will not make the effort to shop there. On the other hand, a plumbing service's location is of minor importance. Why? Because the service is performed in the home, and customers do not have to go to the place of business.

Your location decision will depend on whether your enterprise is manufacturing, wholesaling, retailing, or services. Extractive business ventures are usually locked into a fixed location where products are found in nature.

Manufacturing. Manufacturers usually need access to low-cost forms of transportation. For example, trucking companies should be nearby. This makes it convenient for receiving raw materials and shipping finished products. Access to utilities, such as electricity, water, and sewers, is also important.

Wholesaling. Like manufacturers, wholesalers should have access to various transportation facilities. They should also be located in the middle of the market they serve. The wholesalers will then be conveniently located for quick shipments to all customers.

Retailing. Retail store locations are largely determined by the type of merchandise carried. For example, clothing stores are commonly located near department stores. As another example, home furnishings stores and furniture stores are located near each other. Preferred locations for other retailers are on the main traffic thoroughfares. Examples are supermarkets and drugstores.

If you go into retailing, locate in an area where customers are most likely to shop for the kinds of goods you sell.

Services. Personal services and repair services have many of the location requirements of retail stores. Dry cleaners, travel agencies, and car repair shops must be located where customers can come conveniently. Likewise, business services, such as equipment rental firms and accounting firms, usually locate in the business districts nearest their customers.

Choose A Specific Site. Choosing a specific site is more critical for retail and service businesses. Therefore, te following discussion on site choice applies primarily to those fields of business activity.

You may find very few specific sites that are vacant. This could mean that you will have to take whatever site is available. Before you make a final decision, you should answer these questions:

1. Is parking space adequate for the enterprise?
2. Is the building, as well as those nearby, attractive and well maintained?
3. Can cars enter and leave the parking lot with ease?
4. Is there an ample flow of traffic on nearby streets?
5. Is the rent or building cost high or low in relation to the area?
6. Are there any restrictions on the use of the property?

You should use an evaluation sheet when assessing different sites. The following are some of the factors that may appear on an evaluation sheet. Start with this evaluation sheet, then eliminate factors or add new factors to meet your needs.

Score Sheet on Sites Grade each factor: "4" for excellent, "3" for good, "2" for fair, and "1" for poor.		
Factor		**Grade**
1.	Centrally located to reach my market.	________
2.	Merchandise or raw materials available readily	________
3.	Nearby competition situation	________
4.	Transportation availability and rates	________
5.	Quantity of available employees	________
6.	Prevailing rates of employee pay	________
7.	Parking facilities	________
8.	Adequacy of utilities (sewer, water, power)	________
9.	Traffic flow	________
10.	Taxation burden	________
11.	Quality of police and fire protection	________
12.	Housing availability for employees	________
13.	Environmental factors	________
14.	Physical suitability of building	________
15.	Type and cost of lease	________
16.	Provision for future expansion	________
17.	Overall estimate of quality of site in 10 years	________

STUDYING THE COMPETITION

Practically all business ventures in the country face competition. **Competition** is the effort of two or more businesses to win the same group of people as customers. Individual firms involved are called **competitors**. A new enterprise will survive only if it offers some competitive advantages. Examples are better service, superior products, lower price, or shorter delivery time. Customers buy from a particular enterprise for these and other advantages. It is important, therefore, to include a study of competition in your business plan. This study should include the number of competitors as well as their strengths and weaknesses.

Number of Similar Businesses

Who are your competitors? How many are there? You should be aware that not all competitors are located in your community. For example, if you open a gift shop, you may be competing with companies selling gifts by mail order; or you may have local competitors whose businesses are not exactly like yours. As an example, the gift department tin a department store could be a major competitor. When planning your enterprise, you must identify the competition.

You should also determine if the local area already has too many businesses like the one you plan to open. A relationship exists between the number of people in a community and the number of businesses of various kinds.

Strengths and Weaknesses of Competitors

Once you have identified your competitors, you should determine the strengths and weaknesses of each. Visit each competitor’s place of business. Observe the competitor’s operation and the way customers are treated.

After each visit, make notes of your observations. Then summarize the information when you have completed the series of visits. Even though a comparison of competitors can be helpful, the information can become outdated. Competitors may make changes in their businesses. One may lower its prices while another increase the number of services it offers to customers. New competitors may open their doors, while others close theirs forever.

What will other businesses do when you start your business and begin competing against them? You should expect other businesses to react. Be prepared to take action. Plan ahead by writing scenarios. A **scenario** is an outline of a chain of events that an individual believes could possibly occur in the future. Collect all the information you can to prepare informed opinions. Ask experts for their opinions. Then write scenarios about your competition.

Because it is an attempt to describe the future, a single scenario will not be 100 percent accurate, nor is it expected to be. Write at least two scenarios: one for the worst case and one for the probable case. In a **worst-case scenario**, try to imagine a situation as bad as t could get. A worst-case scenario might be as follows: Competing convenience stores open up on each of the other three corners. The products they sell are very much like yours; their prices lower than yours. The new businesses advertise more than you do. The events described in the scenario may not occur. Nevertheless, you should think about what you would do if you actually had competitors across the street.

A **probable-case scenario** describes what is more likely to occur. Let's continue with the convenience store example to determine a probable-case scenario: Competing businesses open up in the area, but the closest one is at least half a kilometer from your location. One of the stores that starts out with lower prices gradually increases prices and now charges what you charge. You lose some customers to competitors, but you gain other customers by promoting your store and providing good customer service.

Questions to Answer:

Part I.

Match the following terms with the statements that best define the terms. Write the letter of your choice in the space provided.

A. Market
B. Consumers
C. Business users
D. Market segments
E. Market segmentation
F. Target market
G. Sales forecast
H. Market potential
I. Average market share
J. Location
K. Competition
L. Competitors
M. Scenario
N. Worst-case scenario
O. Probable-case scenario

	1	An outline in which you try to imagine a situation as bad as it could get.
	2	Dividing the market for a product or service into segments.
	3	The number obtained when market potential is divided by the number of competing businesses.
	4	Companies or institutions that buy products and services to use in running their businesses, to resell, to produce other products, or to provide services.
	5	An estimate of sales, in dollars or units, for a specific time period.
	6	The place where you have your main base of operations.
	7	Groups of people with similar needs and characteristics.
	8	Individual firms involved in trying to win the same group of people as customers.
	9	The particular group to whom you wish to sell your products or services.
	10	The groups of people, businesses, or organizations seeking the types of products or services you sell.
	11	An outline of a chain of events that could possibly occur in the future.
	12	The effort of two or more businesses to win the same group of people as customers.
	13	Persons or households that buy products and services for personal or family use.
	14	An outline that describes what may occur.
	15	The total sales of all similar businesses in your area.

Part II.

Kindly answer the following questions.

1. What is the difference between consumers and businesses users?
2. One of your friends asks, “Shouldn’t a business try to be all things to all people?” What is your answer?
3. List eight questions you can ask to learn as much as possible about your target market.
4. Why is a sales forecast important to a new enterprise?
5. Describe the steps in the sales forecasting process.
6. List the five factors you should consider when selecting the community or city in which to locate a new enterprise.
7. What two items should be included in a study of competition?
8. What is a scenario? How can a scenario be used to analyze competitors?

MODULE 5

PLANNING A NEW BUSINESS VENTURE

Knowing what you want to accomplish is the first step in planning a new enterprise. Once you have a clear idea of the enterprise, you can develop guidelines for action.

OBJECTIVES:

After studying this module, the student should be able to:

1. Write a definition of your planned business.
2. Compare the legal forms of business enterprise.
3. Explain plans for getting the work done.
4. Identify sources of assistance for planning the enterprise.

DEFINITION OF THE BUSINESS

Your first step in starting a business is to turn your idea for a business into a plan of action. You will do this by writing a business plan. A business plan is a written description of every part of the new enterprise. Beginning with a definition of the business you intend to conduct, you will map out the course for the enterprise.

A definition of the business contains a description of the industry, your company, the products or services you will offer, and the image you desire.

The Industry

All the firms that offer a particular product or service make up an **industry**. IBM, Apple Computer, and the other computer manufacturers make up the computer industry. Likewise, PepsiCo, Inc. and Coca-Cola Co. are two of the companies in the soft drink industry.

A definition of the business should include the outlook for the industry. Discuss changes or trends that could affect your business either positively or negatively. Are people buying more or less of the industry's product? Will new products from another industry make it harder or easier to sell your products?

Your Company

A definition of the business must contain a description of the company you intend to start. Here is an example of a definition of a company:

> The store will sell a complete line of office supplies and custom-printed forms to consumers and to businesses. No other local firm offers such an extensive line of products. Offices, banks, and other users will be given both discounted prices and free delivery service when they place large orders.

The business name is a part of the description of your company. You should explain the business name in the business plan. Because the name may be difficult to change later on, take care in selecting the name in the beginning. Your answers to the following questions should be helpful when deciding on a business name:

1. Does the name tell people what my company makes or sells?
2. Is any other company or organization using the name I am considering? Is anybody using a similar name? Two or more companies using the same or similar names can be confusing to customers. You may also find yourself in legal difficulty if you use an established firm's name.
3. Am I aware of the problems that may arise when I put my own name on the business? Having your name on the business could be embarrassing to you and your family if the business fails. On the other hand, if the business is successful, you may have difficulty selling it because prospective buyers may not want a business with someone else's name on it. If you are successful in selling it, you may not like what the new owner does to your name through dishonesty or poor treatment of customers.
4. Is my company's name linked to a current fad, catchword, or anything else that could lose it popularity? If so, the name may someday tell customers that the business, along with its products and services, is outdated.

Products and Services Offered

You can look at products and services from two different viewpoints: the seller's and the consumer's.

Seller's Viewpoint. The **seller's viewpoint** is a narrow definition of products and services. That is, many sellers see products as physical objects only. They think of the products in terms of the component parts and materials used in manufacturing. In a similar way, sellers may see services as consisting only of the tasks performed.

Consumer's Viewpoint. From the **consumer's viewpoint**, products and services are seen in terms of the benefits derived from their use. They key idea is that consumers buy what the products or services will do for them. Therefore, entrepreneurs should see themselves as sellers of benefits. Consumers shopping for a microwave oven are buying more than just an oven. They are buying convenience and the ability to get meals on the table quickly. When you buy a car, you are probably buying more than a means of transportation. You may also be buying a symbol of status, taste, and achievement.

How will you answer the question, "What is your business?" Some examples may help you think of a response. The owner of a tire store may answer, "I sell more than tires, I sell customer safety." The operator of a fast-food restaurant may say, "I sell more than food, I sell family fun and convenience at a low price."

Image Desired

An enterprise can also be described in terms of its **image**, which is how customers feel about doing business with the enterprise. It is a personality and identity that makes customers think immediately of the business when they want the particular kind of products or services it offers. What makes or creates the image of a business? Image is the result of the total business and all its parts. You will determine the image when you (1) plan to sell specific products and services, (2) plan what customer services to offer, (3) select a location, and (4) hire employees.

Specific Products and Services. After you select the type of enterprise you want, you must choose specific products and services to offer. You must define exactly what you are going to sell.

It is not enough to say that you will open an auto parts store. What parts will you keep in stock? Will you specialize in certain types of cars? Answers to these questions will help determine the image. If you stock parts for American-made cars, you will have one image. If you limit your inventory to parts for imported cards, you will have another image. You will have a third type of image if you specialize in parts for antique and restored cars.

You will have to make similar decisions if you open a service enterprise. As an example, the policy of one photographer might be to serve people who want pictures taken at weddings, family reunions, and other special occasions. Another photographer's services might be limited to taking portraits in the studio. In a similar way, owners of travel agencies, motels, and movie theaters must define exactly what services they sell.

Customer Services. ***Customer services*** are the extra benefits that a business provides for its customers. For example, some grocery stores provide custom trimming of meat at no extra cost, neighborhood bulletin boards, and a courtesy booth for the payment of utility bills. Another example is clothing sores that offer free alterations to customers.

Customer services are often associated with, but not limited to, retail stores. Think of the mail-order firms that permit a thirty-day trial of merchandise, the muffler shops that guarantee their product for as long as you won the car, and dry cleaners that offer one-hour service.

You must make definite plans about the customer services that you will offer. Your decision will affect the image of the enterprise.

Location. Where will the enterprise be located? A jeweler who wants to convey a quality image should locate near fashionable stores. On the other hand, a building materials discount store could be appropriately located in a warehouse district. In addition, customers should have easy access to the business with ample and convenient parking. When selecting a location, ask yourself this question: How will my customers feel about coming to this location?

Employees. The attitude of employees affects the image of the business. A restaurant with excellent food will acquire a poor image if meals are not served promptly and courteously. An efficient appliance repair service may lose its clientele if employees are not polite when entering customers' homes.

You may be the only employee in the beginning. When you are ready to hire others, remember what image you want to establish for the enterprise. Then, hire only those employees who will help you achieve that image.

LEGAL FORMS OF BUSINESS VENTURES

The three principal legal forms of business enterprise are (1) sole proprietorship, (2) partnership, and (3) corporation. One of the entrepreneur's most important decisions is choosing the appropriate legal form for the business. Before making this decision, prospective entrepreneurs should consider these questions:

1. How soon do I want to get the enterprise started?
2. Am I willing to share the profits with others?
3. Do I want complete control in running the enterprise?
4. How much liability am I willing and able to assume?
5. Will one particular legal form of business enterprise result in lower taxes?
6. Am I able to provide all the capital needed to get the enterprise started?
7. Is my enterprise based on a secret process or formula?
8. Do I want the enterprise to continue when I am no longer able to run it myself?

The legal form of organization affects most areas of the enterprise. Therefore, the entrepreneur should understand all three forms and be familiar with the advantages and disadvantages of each. At the same time, entrepreneurs should know they may be required to comply with certain regulations, regardless of the legal form of the enterprise. For example, the law generally requires every business with one of more employees to obtain an Employer Identification Number is obtained by filing Form SS-4 with the Internal Revenue Service. This identification number is not the same as the Social Security number required on individual income tax returns.

An entrepreneur should also realize that the legal form of the business can be changed as the enterprise develops and grows. For instance, a new business may begin as a sole proprietorship and develop into a partnership. Some proprietorships and partnerships may later become corporations.

Sole Proprietorship

A **sole proprietorship** is an enterprise that is owned by only one person. It is sometimes referred to simply as a proprietorship. This is by far the most popular legal form. Proprietorships exist in just about every filed of business activity. However, they are dominant in the areas of services, retail trade, and construction. Proprietorships generally have small sales volumes and employ only a few workers.

Advantages of Sole Proprietorships

Proprietorships are popular because of several advantages: (1) profits to owner, (2) easy start-up, (3) complete control and flexibility, (4) tax benefits, (5) satisfaction, (6) secrecy, and (7) easy dissolution.

Profits to Owner. A proprietor owns the business. A proprietor is the sole owner of any profits earned and does not have to share them with anyone else. This is not the case with other legal forms. In partnerships and corporations, some portion of the profits will be distributed to others.

Easy Start-up. Many people prefer the proprietorship because it is the easiest and simplest form of business to start. Generally, no legal document is necessary to establish a sole proprietorship. It exists as soon as business is conducted. For example, you can be the proprietor of your own carpet cleaning service as soon as you purchase the appropriate equipment and cleaning supplies. In other words, you could be in business and ready to serve your first customer by tomorrow.

Depending on the type of enterprise you open, you may have to obtain a license. For example, restaurant must usually be approved by the local board of health.

Complete Control and Flexibility. Since a sole proprietor does not have to get anyone else's approval, decisions affecting the business can usually be made more quickly. In partnerships and corporations, important decisions are generally made only after consulting others.

Consider a painting contractor who has an opportunity to buy paint at a bargain price. The order must be for a large quantity, and the order must be placed by the end of the day. In a sole proprietorship, the entrepreneur could make the decision in a matter of minutes. In a partnership or corporation, the entrepreneur might not be able to consult with the others by the deadline. As a result, the chance to save money would be lost.

Tax Benefits. Sole proprietors are taxed as individuals; the business itself is not taxed. Special taxes that are levied against a corporation do not apply to proprietorship.

The proprietorship's tax return is similar to any other individual taxpayer's. Personal and family deductions and exemptions are listed on the Internal Revenue Service Form 1040. In addition, proprietors file Schedule C to deduct business expenses from business income. **Business income** is total dollars received for all goods and services sold during the year. **Business expenses** are ordinary and necessary costs of operating the business. Generally, a sole proprietor may deduct expenses such as employees' wages and salaries, interest on business debts, insurance premiums, bad debts, and rent on buildings, trucks, and other equipment.

Satisfaction. The proprietor of a successful business enjoys a sense of accomplishment by applying skills, making personal sacrifices, and making decisions that often overcome obstacles. The satisfaction of knowing that one is largely responsible for the success of the enterprise is a reward in itself. If this reward must be shared with others, as in the other legal forms, the same feeling of satisfaction may not result.

Secrecy. Sole proprietorship offers the best possibility for keeping information confidential. This may be important it the success of the enterprise depends on a secret process of formula. Also, the owner does not have to tell anyone other than the Internal Revenue Service what the profits are.

Easy Dissolution. Proprietorship are easy to start, and they are almost as easy to dissolve. All a proprietor must do is sell the equipment, inventory, and other assets used in the enterprise. To protect the credit rating, a proprietor should make sure employees and creditors are paid in full.

Disadvantages of Sole Proprietorship.

Sole proprietorships have these disadvantages: (1) unlimited liability, (2) limited life, (3) difficulty in obtaining capital, (4) management difficulty, and (5) little incentive for employees.

Unlimited Liability. Proprietors may keep all the profits of their businesses, but they also have unlimited liability. **Unlimited liability** means that they are personally liable for all business debts. A proprietor may have to use personal savings, investments, or belongings to settle debts. Therefore, proprietors risk not only their invested business capital but also their personal assets.

Limited Life. A proprietorship has limited life because it is directly tied to the life of the owner. **Limited life** means that the business will be dissolved upon the death, imprisonment, or bankruptcy of the proprietor. In addition, an extended illness of physical disability may force the owner heir wanting to continue the business. Instead of continuing the former enterprise, a new sole proprietorship would have to be established.

Difficulty in Obtaining Capital. Sole proprietors have two sources of funds for starting the business. One source is their own personal funds, which may not be adequate. The other source is borrowed funds. However, lenders often hesitate to grant loans to sole proprietors because of the risk involved in a new enterprise. Having insufficient operating funds can severely limit the enterprise's growth and may cause it to fail.

Management Difficulty. Management difficulty occurs because the proprietor carries the entire burden of managing the business. Some entrepreneurs describe this situation as "spreading themselves too thin." Someone must make the products, help customers, complete tax forms, write advertisements, collect overdue bills, and order merchandise. One person seldom does all these things equally well, but usually it is the proprietor who must do them alone. Spending time on these necessary tasks leaves less time for planning the future.

Little Incentive for Employees. By definition, a proprietorship does not have partners or part owners. Therefore, employees can never be more than employees. They cannot but, or be given, a share of the ownership. This may cause a highly competent employee to quit and possibly start a competing business.

Partnership

A partnership is a business enterprise owned by two or more persons. This legal form of ownership overcomes some of the limitations of sole proprietorship. The name of the business often indicates a partnership: for example, Smith and Jones's Hardware or Bill and Tom's TV Repair. Several types of partnership arrangements exist. However, the following discussion deals with the more common type known as a **general partnership**. All partners in a general partnership have unlimited liability for the enterprise's debts.

Advantages of Partnership

Partnerships usually have these advantages: (1) easy start-up, (2) added capital, (3) combined management skills, (4) tax benefits, and (5) employee incentives.

Easy Start-up. A partnership is almost as easy to form as proprietorship. The enterprise is ready to start once the partners have agreed on various details about the partnership. For example, they must decide how much money each will invest, how profits and losses will be shared, and how assets will be divided if the business is dissolved. These and other important points should be included in a written agreement known as articles of partnership. This agreement is not required by law, but its use can prevent misunderstandings and legal difficulties.

Added Capital. Many partnerships are formed because two or more people can assemble more money than one person can. This makes it possible to start a larger business and have reserve funds for unexpected expenses. Also, lenders may be more willing to grant loans because more persons are available to repay the debt.

Combined Management Skills. Each partner can contribute a skill to the enterprise that the other may not have. One partner may be an outstanding chef. The other may be a skilled manager who likes to keep records and supervise employees. By combining their skills, the two partners could open a restaurant. Together in a partnership they could be successful, where alone they might fail.

Tax Benefits. The partnership itself is not taxed. Instead, partners pay income tax on their individual portions of the enterprise's profits.

Employee Incentives. Partners can encourage competent employees to remain with the business by inviting them to become partners. Articles of partnership should be modified to reflect any changes.

Disadvantages of Partnership

The strong points of the partnership may be overshadowed by one or more of the following disadvantages: (1) unlimited liability of the partners, (2) limited life, (3) divided authority, and (4) frozen investment.

Unlimited Liability of the Partners. Each partner is liable for all partnership debts. That is, creditors may sue any of the partners to settle the debt. This is true even if one partner has incurred the debt on behalf of the business.

Limited Life. The life of a partnership is limited and uncertain. Any change among the partners can cause the partnership to dissolve. The death or withdrawal of one partner will bring the enterprise to an end. However, the remaining partners may start a new partnership. Of course, this assumes they have enough money to buy the former partner's share of ownership.

Divided Authority. Because authority is shared by all partners, there is potential for disagreement. Each partner could have different ideas about hiring employees, buying merchandise, or advertising and sales promotion programs. Many otherwise successful business ventures have been dissolved because partners could not work together. The possibility that problems will occur increases with the number of partners.

Frozen Investment. It is often difficult to withdraw a partner's investment from a partnership. Even if the other partners are willing to buy one partner's share, the partners may struggle to agree on a fair price. Therefore, when going into a partnership, entrepreneurs should invest only those funds they can live without for a while.

Corporation

A **corporation** is an enterprise that has the legal rights, duties, and powers of a person. Because a corporation exists independently of its owners, a corporation is an artificial being or "person." A corporation may own property in its own name and may also enter intro contracts, borrow money, and perform other day-to-day business activities.

Corporations are established by obtaining a charter from the state in which the business is to be located. The **charter** is a written document outlining the conditions under which the corporations will operate. The owners are called **stockholders**. Individuals become owners by buying shares of **stock**, which represent shares of ownership in the corporation. Some large corporations have thousands of stockholders, representing people from a variety of occupations. Generally, these people are interested in the business only as an investment. However, in small business ventures, the stockholders and the managers are the same individuals. To them, the business is more than an investment; the business represents their careers.

Advantages of Corporation

Corporations are often thought of as large businesses. However, because of the advantages, many entrepreneurs have chosen this form of ownership for their business ventures. The main advantages are (1) limited liability, (2) continuous life, (3) easy transfer of ownership, (4) ability to attract funds, and (5) specialized management.

Limited Liability. In a corporation, the most a stockholder can lose is the amount of money invested in the business. Because a corporation is a separate entity, the corporation, rather than the owners, owes the debts. Therefore, personal savings and belongings will not be taken to pay debts of the corporation. This is a major advantage of the corporate form of ownership.

Continuous Life. When a proprietor or a partner dies, the business is ended legally. This is not true of corporations. A corporation's existence is not affected by the death or incapacity of an owner. The enterprise can operate indefinitely as long as it is profitable.

Easy Transfer of Ownership. Ownership in a proprietorship or partnership may be difficult to transfer to another person. This usually involves closing the enterprise and reorganizing it. In a corporation, however, stockholders can sell their stock to another person.

Ability to Attract Funds. Corporations are able to acquire additional funds by selling shares of stock. Individuals may be more willing to invest in corporations than in partnerships because their liability is limited. For these reasons, corporations usually have more opportunities to expand. They are able to et money fro new buildings, equipment, and inventories.

Specialized Management. Proprietors and partners must perform a wide variety of functions. However, because they are frequently larger than other legal forms, corporations can have **specialized management**. This means that each person can concentrate on one set of duties. One manager may oversee the manufacturing of the product while another specializes in accounting.

Disadvantages of Corporation

The disadvantages of the corporate form of ownership are (1) complicated formation, (2) double taxation, (3) government regulation, (4) charter restrictions, and (5) little secrecy.

Complicated Formation. Getting a corporation started usually requires more time and money than other legal forms of ownership. For example, the corporation must conform to certain laws to obtain a character from the state. Thus, a lawyer's services are needed in filing the necessary papers. In addition to the lawyer's fees, a corporation will probably have to pay fee to the state.

Double Taxation. Perhaps the major disadvantage of the corporate form of ownership is the problem of ***double taxation***. This means that profits are taxed twice. A corporation must pay taxes on its profits. Stockholders also have to pay personal income taxes on their share of the profits.

Government Regulation. Federal and state regulations of corporations have increased over the years. Depending on the state in which a corporation is chartered, various reports are required each year. The corporation must also register in all other states in which it does business. This often involves the payment of a special tax.

Charter Restrictions. A charter for a corporation indicated the type of business the corporation will pursue. The charter permits the enterprise to engage in only those business activities stated in the document. Therefore, a corporation cannot make a major change in its line of business until the charter is amended. This eill take time and involve additional legal fees.

Little Secrecy. The more owners a corporation has, the more difficult it will be to maintain confidentially. All stockholders are entitled to now sales, profit, and asset figures each year. A special production method may be impossible to keep secret.

ORGANIZATION OF THE ENTERPRISE

Planning how to get the work done is an important step in starting an enterprise. This involves deciding what tasks must be performed to make the enterprise a success. If there are other partners of employees, an entrepreneur must decide who will perform each task. An entrepreneur should also realize the importance of personnel management.

What Skills Are Required by the Enterprise?

The first step in organizing the work of the enterprise is to determine what tasks should be performed. Some duties are necessary in almost all business ventures: making or buying products, providing services, setting prices, waiting on customers, paying bills, advertising, cleaning and maintenance, and preparing accounting and tax statements.

List every task that comes to mind. Do not worry about how small the task seems to be. Also, you need not follow a particular order or sequence. Just keep adding to the list until you believe it is complete.

Who Will Perform Each Task?

After an entrepreneur has identified the necessary tasks for the enterprise, the entrepreneur should indicate who will perform each task. This can be done with an organization chart. An **organization chart** is a diagram that shows how one job in the enterprise fits in with others. Of course, a one-person enterprise does not need an organization chart. Some small businesses start out with a few employees and grow larger. The organization chart should be on paper and explained to all members of the enterprise.

What is Personnel Management?

The single most important resource in an enterprise is its people. Therefore, an entrepreneur must be prepared to manage this resource. The purpose of **personnel management** is to build a motivated and effective work force. The activities that make up this process are (1) hiring, (2) training, (3) determining compensation, and (4) determining employee benefits.

Hiring. The **hiring** process involved deciding if a prospective employee is suitable for the job. Employers interview job applicants and also contact persons listed as references on the employment application form. As the firm grows in size, however, additional methods may be used. For instance, persons applying for jobs may be required to take written tests or demonstrate that they can perform the work.

Training. The purpose of **training** is to improve job performance. All new employees require a certain amount of training. Those without prior experience must be taught the skills to do the job. Employees with related job experience probably were hired because they have the skills. However, they still need training. For instance, they may have to learn the procedure for handling customer complaints or making bank deposits.

Determining Compensation. Compensation refers to wages and salaries paid to employees. **Wages** are payments to workers on an hourly basis. **Salaries** are fixed peso amounts paid regularly such as weekly or monthly. Consider the following questions as you set your compensation policy: What are you willing to pay? Are you willing to pay above the minimum required by law? What must you pay to get the employees you want?

Determining Employee Benefits. Employees may receive **fringe benefits** in addition to regular compensation. Entrepreneurs offer fringe benefits to compare effectively for good employees. A popular benefit is health insurance in which the employer pays all or part of the health insurance premium. Other fringe benefits are paid vacations and holidays, life insurance plans, and pensions. Some employees get a discount on purchases.

SOURCES OF ASSISTANCE

Starting a business is a complex process, regardless of whether you start from scratch, buy an existing business, or buy a franchise. As a prospective entrepreneur, you should obtain the assistance of advisers in business matters. Advisers you should contact include (1) attorneys, (2) accountants, (3) bankers, and trade associations.

Attorneys

Some persons visit an attorney only when they are involved in a lawsuit. However, many entrepreneurs have learned to consult an attorney on other matters as well. An attorney can help set up the business and give advance warning of potential legal problems. Compliance with local and national laws can be best assured with legal advice. An entrepreneur should study documents such as licenses, permits, and equipment purchase and lease agreements. When considering a franchise, a franchisee should examine carefully the contract used by the franchisor. Paying an attorney for these services is usually money well spent. If possible, select an attorney who is familiar with small business.

Accountants

Records of sales, expenses and profits are necessary in managing an enterprise. Accountants can assist in setting up the records system to provide this information. They can also advise on tax problems and prepare tax returns. A prospective franchisee should discuss the franchisor's financial records with an accountant. With an accountant's help, a prospective franchisee can find out if the franchisor's estimates of sales and profits are realistic.

Bankers

Bankers are best known as lenders of money. However, they can also provide valuable information on starting a business. Bankers are able to do this because they keep in close touch with the business community. Bankers can help in comparing franchises or in checking credit ratings of customers. Although bankers are not experts inv every area, they can usually help select other professional advisers. For instance, they can give you names of attorneys to consider.

Trade Associations

Another source of assistance is a trade association. A **trade association** is a group of businesses that have joined together to benefit a particular line of business. These groups assist members by offering ideas and information that will contribute to better management.

Questions to Answer:

Part I.

Match the following terms with the statements that best define the terms. Write the letter of your choice in the space provided.

A. Industry
B. Seller's viewpoint
C. Consumer's viewpoint
D. Customer services
E. Sole proprietorship
F. Business income
G. Business expenses
H. Unlimited liability
I. Limited life
J. Management difficulty
K. Partnership
L. General partnership
M. Articles of partnership
N. Corporation
O. Charter
P. Stockholders
Q. Stock
R. Specialized management
S. Double taxation
T. Organization chart
U. Personnel management
V. Hiring
W. Training
X. Compensation
Y. Wages
Z. Salaries
AA. Fringe benefits
BB. Trade association

	1.	Problems arising from having to carry the entire burden of managing the business.
	2.	Total money received for all goods and services sold during the year.
	3.	Wages and salaries paid to employee.
	4.	A diagram that shows how one job in the enterprise fits in with others.
	5.	Personal responsibility for the debts of the enterprise.
	6.	Building a motivated and effective work force.
	7.	A form of ownership in which all the owners have unlimited liability for the enterprise's debts.
	8.	The extra benefits that a business provides for its customers.
	9.	A written document outlining the conditions under which the corporation will operate.
	10.	Seeing products and services in terms of the benefits derived from their use.
	11.	What employees may receive in addition to regular compensation such as paid vacations and life insurance plans.
	12.	A business enterprise owned by two or more persons.

	13. All the firms that offer a particular product or service.
	14. Having to pay taxes on profits twice.
	15. Payments to workers on an hourly basis.
	16. An enterprise that has the legal rights, duties, and powers of a person.
	17. Shares of ownership in the corporation.
	18. Ordinary and necessary costs of operating a business.
	19. A group of businesses that have joined together to benefit a particular line of business.
	20. A means of improving job performance.
	21. A characteristic of certain forms of ownership that requires dissolution of the business upon the death, imprisonment, or bankruptcy of the proprietor.
	22. A narrow definition of products and services.
	23. A written agreement describing how much money each person will invest, how profits and losses will be shared, and how assets will be divided if the business is dissolved.
	24. An enterprise that is owned by only one person.
	25. Fixed dollar amounts paid to employees regularly such as weekly or monthly.
	26. The owners of a corporation.
	27. Assignment of a different set of duties to each manager.
	28. The process of deciding if a prospective employee is suitable for the job.

Part II.

Write a short answer to each of the questions below.

1. What should a definition of the business contain?
2. List four decisions of the entrepreneur that will affect the image of the enterprise.
3. What is the first step in planning how to get the work done in the enterprise?
4. Why would an organization chart be useful in an enterprise with five employees?
5. List four types of advisers to contact when starting a new business.

6. Compare the three legal forms of business enterprise by writing the advantages and disadvantages of each in the spaces provided on the next page. Select your answers from the list below. Some terms will be used more than once.

- Easy start-up
- Difficulty in obtaining capital
- Complicated formation
- Easy transfer of ownership
- Owner profits
- Little incentive for employees
- Satisfaction
- Unlimited liability
- Little secrecy
- Frozen investment
- Limited liability
- Combined management skills
- Management difficulty
- Easy dissolution
- Limited life
- Double taxation
- Ability to attract funds
- Complete control and flexibility
- Employee incentives
- Divided authority
- Secrecy
- Continuous life
- Government regulation
- Added capital
- Charter restrictions
- Tax benefits
- Specialized management

MODULE 6

MARKETING THE PRODUCT OR SERVICE

The previous modules gave you ideas on the various products or services that you can offer in your business. It has helped you identify your target market as well. Now you should consider how you will reach these potential customers.

OBJECTIVES:

After studying this module, the student should be able to:

1. Define marketing
2. Distinguish between consumer products and services and industrial products and services.
3. Describe the channels of distribution.
4. Explain methods of pricing products and services.
5. Discuss ways of promoting your product and services.

Marketing is a set of business activities that provides products and services to satisfy consumer needs and wants. Marketing connects those who produce the product or service with those who use it. The methods you use in reaching the target market comprise your **marketing strategy.**

The marketing concept is a way of thinking about a business in terms of consumer needs and wants. This concept is based on three basic beliefs:

1. An entrepreneur should plan the business activities of an enterprise with consumers in mind.
2. An entrepreneur should bring together the marketing efforts to fit the target market.
3. An entrepreneur should pursue profit as one of the enterprise's goals.

In other words, entrepreneurs should be concerned with both consumers and profits. Five elements of the marketing process are important to the new enterprise: (1) identifying the products or services that consumers need and want, (2) recognizing the differences between consumer products and services and industrial products and services, (3) selecting the path that the product will follow from producers to users, (4) providing products or services at prices customers are able and willing to pay, and (5) informing and persuading people that the enterprise aims to serve them.

You have already identified the products or services that consumers need and want—the first element of the marketing process. You did this when you chose an idea for a new enterprise. The remaining elements of the marketing process will be discussed in this module.

TYPES OF PRODUCTS AND SERVICES

Products and services can be divided into two large groups: consumer products and services and industrial products and services. The marketing strategy you use will depend on the type of product or service you will provide.

Consumer Products and Services

Consumer products are products individuals and families buy for their personal use. Many Filipino consumers enjoy a level of income enabling them to buy many different products. This spending power allows many people to try new products as their needs and wants change. These changes, together with amazing advances in technology, stimulate a constant flow of consumer products both into and out of the marketplace. New products and improved versions of old products appear daily on the counters and shelves of retail stores. At the same tome, other products disappear from the stores because they are no longer in demand.

Consumer products are classified as convenience goods, shopping goods, or specialty goods. These categories are based on the buying habits of consumers.

Consumer Goods. Inexpensive items that consumers buy often and with little shopping effort are convenience goods. These are sold in convenience stores or what we call “sari-sari” stores. With goods in this category, the cost of comparing quality and price of similar items is greater than the benefits received. Shopping costs are measured in terms of both the time and money spent looking for a particular product.

Potato chips and milk are convenience goods. How much could you save, if anything, on these items by driving from store to store trying to find the lowest prices? If you find a lower price, how much lower is it likely to be? Would the savings be worth the time and gasoline used?

Disposable ball pens, candy, and bread are other examples of convenience goods. Once you realize that your pen is running out of ink, you wish to buy a new one with the least possible trouble. You know exactly what you need and you want to buy a new ball pen without going a great distance.

A manufacturer of convenience goods will want to have the products available in as many locations as possible. Consumers do not wish to use much energy or effort to locate and buy these items. If these products are not widely available, manufacturers will lose sales to companies whose products are sold in convenient locations for customers.

Shopping Goods. Items people buy after comparing the price, quality, and other features of similar items are shopping goods. With goods in this category, the benefits of comparing products are greater than the shopping costs. In other words, the time and money spent looking for a particular item are worth it. Consumers of shopping goods do not have a clear idea of what to buy. Instead, they wish to compare the offerings of several stores to help them decide what to buy and where to buy it. Examples of shopping goods are stereo equipment, personal computers, cars, furniture, shoes, and clothing. Compared to convenience goods, shopping goods usually are more expensive and are bought less often.

If you plan to sell shopping goods, choose a location where customers can compare what you offer with that offered by other store, you may have noticed that one furniture store is likely to be located near another furniture store. The same is true for new car dealerships. Also, the last time you walked through a large shopping mall, you probably saw several shoe stores. Generally stores selling similar shopping goods should be located near each other because consumers want it that way.

Specialty Goods. Products that consumers will make a special effort to buy are specialty goods. The attraction of **specialty goods** lies in the particular features that distinguish the goods from similar products. Consumers of specialty goods know what they want, and they do not wish to go to several stores comparing items. Prestige brands of clothing, household appliances, and stereo equipment are examples of products often purchased as specialty goods. Lesser-known brands of these types of products are usually shopping goods.

Specialty goods may or may not be higher-priced items. Brand preference is often the reason for the purchase. For example, some people like a particular brand of imported chocolate so much that they will go to out-of-the-way stores to buy that brand.

A manufacturer of specialty goods should select one or only a few stores to sell the items in a given community. Because customers are willing to travel several kilometers to buy the product, the retail location is not a major factor in the successful marketing of specialty goods.

Consumer services are tasks individuals and families pay others to do or provide for them. Services are intangible; you cannot touch them. Examples of business ventures providing consumer services include travel agencies, day-care centers, hotels and motels, and video movie rental stores.

Industrial Products and Services

Industrial products are products that one business buys from another business. The business buys the industrial goods to produce other products, to provide services, to resell, or to use in daily operations. These items are often bought in large quantities, and many are made according to special orders. Users of industrial products include extractive firms, manufacturers, wholesalers, retailers, and service business ventures. Examples of industrial products include wood and varnish used by furniture shops, paper and ink used by printing companies, and computer equipment used by offices.

Industrial products are classified according to how they are used by the purchasing company. Three categories are (1) raw materials, processed materials and parts; (2) supplies; and (3) installations and accessory equipment.

Raw Materials, Processed Materials, and Parts. Products that are in their natural state when businesses buy them are called **raw materials**. Other than what is necessary to transport them, these materials have not been processed in any way. Some raw materials are harvested or removed from where they are found in nature. Examples are minerals, timber and agricultural commodities such as fruits, vegetables, cotton, wheat, and raw milk.

Products that are produced by one business, but will be changed into another form by other businesses, are called **processed materials.** Because of processing, you cannot recognize these materials in the finished products you buy. For example, you do not see the individual ingredients in the bakery products you buy. Chemicals and plastics are other examples of processed materials.

Parts are items incorporated into a finished product with little or no change. Examples of parts include buttons and zippers used on clothing, and tires and batteries used on cars. As soon as these items arrive at the factory, the manufacturer can install them on the product which is to be sold.

Supplies. Items that aid in a firm's operations but do not become a part of the finished product are **supplies**. Examples are lubricating oil, pens and pencils, stationery, and heating fuel. Other supplies used in day-to-day operations are cash register tape, computer diskettes, and cleaning products.

Installations and Accessory Equipment. Major items used to produce a product or to provide a service are called **installations**. Compared to other categories of industrial products, installations have a long useful life. Examples include factory building and expensive pieces of equipment such as mainframe computers and large printing presses. Other items in this category are jet airplanes used by airlines, transmitting equipment used by radio and television stations, and generators used by electric power companies.

Accessory equipment is also used in operating a business, but its useful life is short compared to that of installations. Hand tools and small power tools used by mechanics, forklift trucks used by warehouse employees, and electric floor sweepers used in a shopping mall are all examples of accessory equipment.

Industrial services, also called **business services**, are tasks one business pays another business to perform for it. Examples of business ventures providing these services are public accounting firms, advertising agencies, computer consultants, event planners, and agencies supplying temporary employees.

CHANNELS OF DISTRIBUTION

The path that a product follows from the producer to consumers or business users is called a **channel of distribution**. Every extractive, manufacturing, wholesaling, retailing, and service enterprise is part of a channel of distribution. Businesses that aid in transferring goods from the producer to the user are called **intermediaries.** Intermediaries are often able to perform marketing activities, such as transporting and storing large quantities of goods, more efficiently than producers. Channels of distribution differ depending on whether they are for consumer or for industrial products.

Services are not included in the following discussion of channels of distribution because intermediaries are not often used in the marketing of services. Services are produced and consumed at the same time. For example, a hairstylist performs the service while the customer sits in the chair. The channel of distribution for services, therefore, is direct from producer to consumer.

Channels for Consumer Products

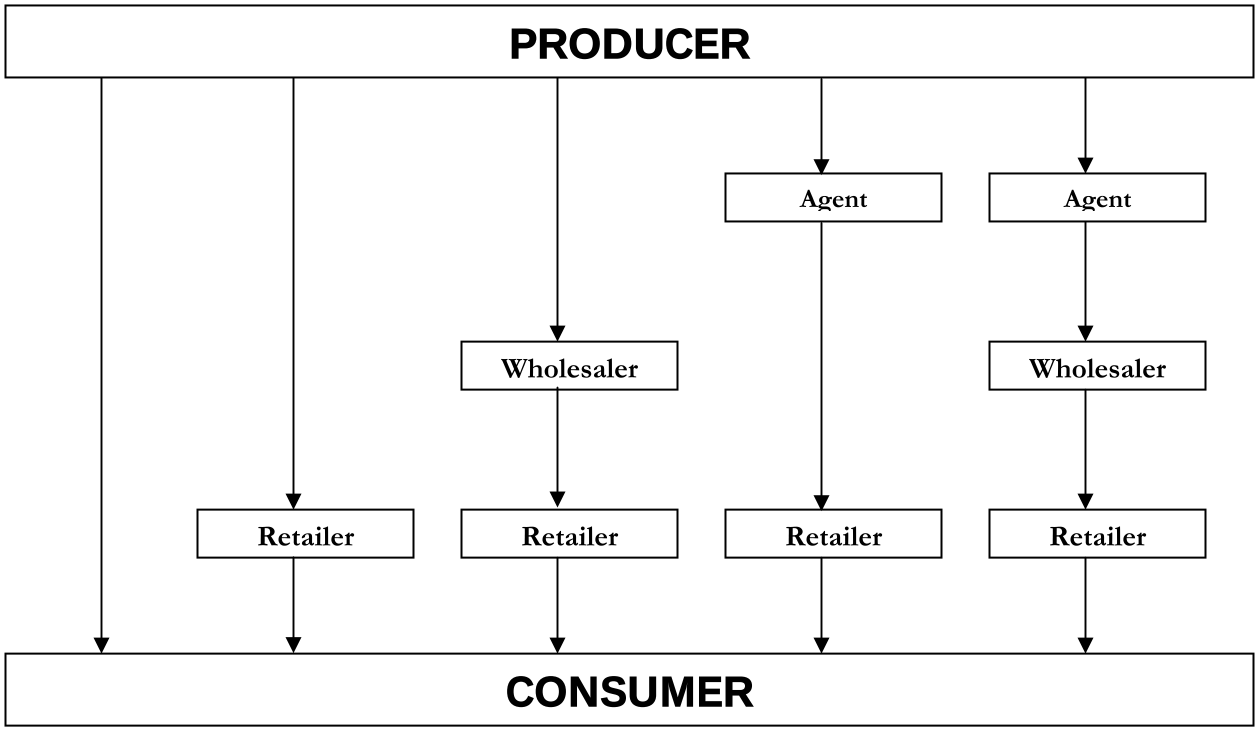
Five channels of distribution widely used in the marketing of consumer products are (1) producer-consumer, (2) producer-retailer-consumer, (3) producer-wholesaler-retailer-consumer, (4) producer-agent-retailer-consumer, and (5) producer-agent-wholesaler-retailer-consumer.

Producer-Consumer. The shortest and simplest channel of distribution for consumer products is from the producer to the consumer. Producers sell door-to-door or by mail order.

Producer-Retailer-Consumer. Producers selling to large retail firms, such as the SM or Rustan's, often use this channel. In addition, some manufacturers of furniture, clothing, and other products have established their own retailer stores.

Producer-Wholesaler-Retailer-Consumer. This is the most common channel used by producers of convenience goods. Manufacturers with only a few products in their line cannot afford to personally contact the thousands of stores who sell the items. Instead, they sell through wholesalers. These wholesalers buy related products from many manufacturers and then sell an assortment of goods to retailers.

<u>Channel of Distribution for Consumer Products</u>



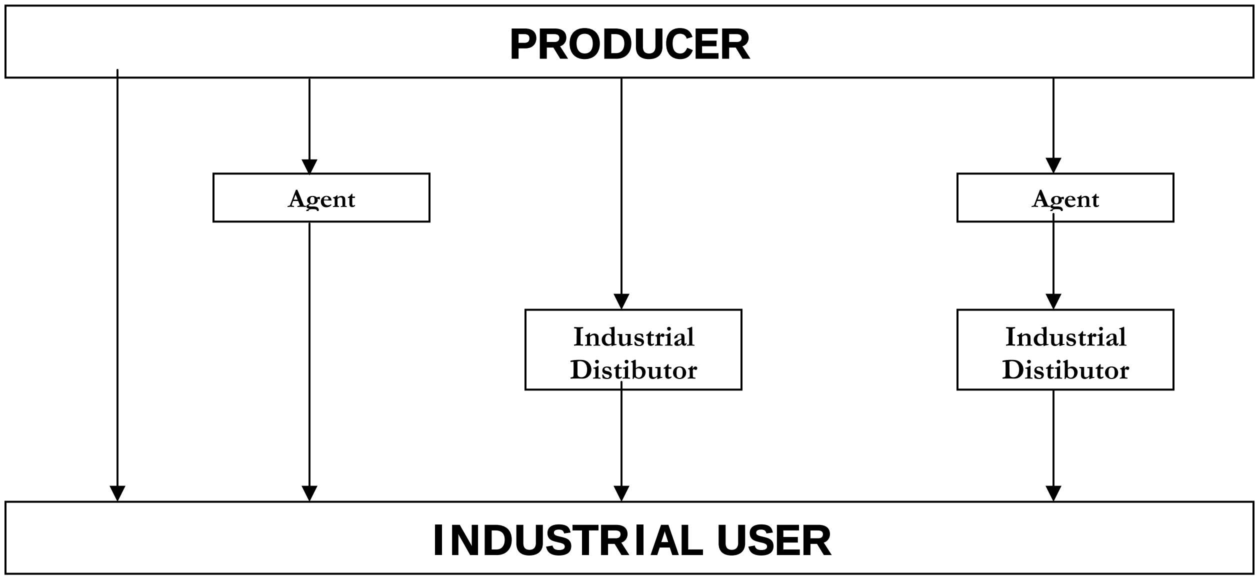
Producer-Agent-Retailer-Consumer. Some producers sell to **agents**, who assist in the sale of products without owning the products. Agents bring buyers and sellers together. Sometimes agents work for manufacturers who are looking for stores to carry their products. At other times, they help retailers find sources of supply for certain goods.

Producer-Agent-Wholesaler-Retailer-Consumer. Producers often use this channel when selling to many wholesalers who are scattered throughout the country. Agents can be helpful in locating the wholesalers.

Channels for Industrial Products

Four common channels of distribution for industrial products are (1) producer-industrial user, (2) producer-agent-industrial user, (3) producer-industrial distributor-industrial user, and (4) producer-agent-industrial distributor-industrial user.

Channel of Distribution for Industrial Products



Producer-Industrial User. This direct channel accounts for the largest peso volume of industrial products sold. Manufacturers of installations, such as mainframe computers and large printing presses, usually sell directly to the users.

Producer-Agent-Industrial User. Some manufacturers do not employ their own salespeople. Instead, they rely on agents to locate buyers for their products. Companies having their own sales forces may use agents to sell a new product or to enter a new market.

Producer-Industrial Distributor-Industrial User. Some manufacturers find the services of industrial distributors helpful in reaching their customers. **Industrial distributors** are wholesalers who buy products from manufacturers and sell them to industrial users. They usually handle supplies and lower-priced accessory equipment.

Producer-Agent-Industrial Distributor-Industrial User. This channel is used for inexpensive industrial products, particularly those that producers sell through many industrial distributors. Here, as is the case in consumer channels, agents bring buyers and sellers together. The producer is the seller and the industrial distributor is the buyer.

PRICING

What is price? **Price** is the exchange value of products and services stated in terms of money. Very simply, the price of a shirt is the amount of money required to buy the shirt. However, there is more to understanding price than merely finding out how much an item costs.

Manufacturers, wholesalers, retailers, and service business ventures use various methods of pricing products and services. Some pricing principles apply to all business ventures. In addition, each field of business has its own pricing practices. Extractive business ventures engage in diverse activities such as farming and commercial fishing. Therefore, specific pricing methods are difficult to identify. If you want to start an extractive enterprise, study pricing in the other fields of business. Then use those methods that best fit your enterprise.

Common Pricing Principles

All entrepreneurs should be aware of three basic or common pricing principles: (1) all costs must be covered, (2) prices affect image, and (3) prices affect sales volume.

All Costs Must Be Covered. No entrepreneur wants to stay in business unless enough money is received to cover costs and make a profit. Your price, then, must reflect the cost of goods or services; all expenses including employee wages, rent, and utilities; and some profit.

In manufacturing, the cost of goods sold is what it costs to make the product. In wholesaling and retailing, the cost of goods sold is what it costs to purchase the goods from others. In service business ventures, the cost of the service varies according to the amount of time and materials used.

Prices Affect Image. Prices charged usually result in a certain price image for the enterprise. Some firms try to give the image that they offer quality products or services at low or discount prices. This practice is successful in some instances and unsuccessful in others.

As an example, you may not hesitate to buy a radio with a well-known brand name at a low price. But would you go to a hairstylist whose prices were much lower than those of most others in town? If your answer is no, you probably believe that quality and price are related and that you should examine the quality when prices are low. Therefore, when setting prices, you should determine what your target market believes about how price and quality are related. This answer depends both on the person and on the specific product or service involved.

Prices Affect Sales Volume. In many cases, as price increases, the amount of the product or service sold decreases. On the other hand, as price decreases, the amount sold increases.

As a result, you are faced with these three decisions:

1. Should you charge low prices and try to obtain more sales?
2. Should you charge high prices? The number of sales would be lower, but the profit on each one would be greater.
3. Should you set prices somewhere between the low and high figures?

Here again, you must find out how each price would be accepted by the target market. Avoid the trial-and-error method of changing prices to see what happens to sales. This confuses customers and may damage your image.

Pricing by Manufacturers

The manufacturer's price must cover the cost of goods sold, all other costs, and a profit.

In this kind of enterprise, the cost of goods sold includes more than the cost of raw materials. It also includes the wages of factory workers and such costs as wear and tear on machinery. An entrepreneur must consider every item of cost before setting the prices.

Pricing by Wholesalers

Wholesalers usually base their prices on the cost of goods sold plus a markup. **Markup** is the amount that is added to the cost of an item in arriving at the selling price. Markup, then, covers all the other costs plus a profit.

The cost of goods includes the cost of shipping the goods from the manufacturer to the wholesaler. Other major costs that must be covered by markup are rent, all wages and salaries, utilities, and delivery costs.

Pricing by Retailers

Most retailers try to establish guidelines that help make pricing decisions simple and routine. This becomes more important as the number of items carried in stock increases.

Retail pricing is usually accomplished by taking a markup on cost. Using this method, the retailer adds a markup to the delivered cost of goods. The **delivered cost of goods** is the cost of merchandise itself plus shipping costs. The markup method can be shown as follows:

Retail Price = Delivered Cost of Goods + Markup

Choosing the amount of markup is, of course, the important decision. If the overall store markup is too high, your products may be too expensive for your target market. As a result, you will lose customers to the competition. If the markup is too low, you may not be able to cover costs and earn a profit.

As a starting point, find out what the average markup percentage is for your line of retailing. Then adjust the rate to fit your situation as you learn more about your target market and your competitors.

Most retailers find it necessary to price some merchandise at other than average markup. You may decide to take a lower markup on some items to meet competitors' prices. On other items, you may take a higher markup because of customer services associated with them.

Markup is easy to calculate. For example, assume you paid PhP 100 for an item, and you wish to take a 40 percent markup on it. Calculate the retail price as follows:

Cost x Markup Percentage	=	Markup
PhP100 x 40%	=	PhP40.00
Cost + Markup	=	Retail Price
PhP100 + PhP40	=	PhP140

Pricing by Service Business Ventures

The service enterprise category includes a wide variety of businesses. Although the pricing methods vary among the service business ventures, many share one common concept. This concept is that service firms generally charge an hourly fee for the number of hours spent in providing the service.

In addition to hourly fees, charges are made when materials, parts, or supplies are used. Repair businesses and the construction trades often use this approach to pricing.

Some service business ventures use specific charges for specific services. For instance, preparers of income tax returns usually charge a standard fee for completing a tax form. This is true no matter how long the preparer worked on the form. The price of a tune-up for a six-cylinder engine is the same even though it takes longer on some cars than others.

Pricing a New Product or Service

Deciding what to charge is not usually a problem when your product or service is the same as that of competitors. Whether they are buying consumer products or services or industrial products or services, customers will not often pay a price higher than that charged by other businesses. Entrepreneurs can match competitors' prices and then make sure they keep their costs down to where they can earn a profit.

Setting a price can be a problem, however, when introducing a new product or service. The practice of pricing according to what others charge will not work. An entrepreneur should use either a skimming policy or a penetration pricing policy.

Skimming Pricing Policy. With a s**kimming pricing policy**, an entrepreneur would charge a relatively high price for the new product or service and expect to sell a low volume. The price would be high in relation to prices of comparable items. One purpose of this pricing policy is to try to recover as soon as possible the costs of developing the product. A disadvantage is that competitors will see a chance to make a profit from also selling the high-priced item. Realize that competition will eventually drive the price to a lower level. This is what happened to the prices of microwave ovens, pocket calculators, personal computers, and DVD players. An entrepreneur should also watch the sales of the product closely to see if the high price discourages customers from buying it.

Penetration Pricing Policy. With a **penetration pricing policy**, the entrepreneur sets a low initial price to attract customers quickly. The lower price discourages other business from introducing the same product or service. An entrepreneur charges a low price and expects to sell a high volume of products or services.

PERSONAL SELLING, ADVERTISING, AND SALES PROMOTION

The final element of the marketing strategy is promotion. Through **promotion,** you inform customers of your offerings and persuade them to buy the products and services you have for sale. The two most widely used methods of promotion are personal selling and advertising. Another method is sales promotion, which is designed to supplement and coordinate personal selling and advertising.

Personal Selling

In **personal selling**, a salesperson makes direct contact with a customer. The purpose is to help customers buy that which will fulfill their needs and wants.

The goal of a marketing strategy is to increase profitable sales. Personal selling is by far the major method of promotion used to reach this goal. Personal selling includes the activities of inside salespersons in retail, wholesale, and serving business ventures. It also includes outside salespersons who call on places of business as well as on consumers.

A good personal selling program can give the new enterprise an advantage over larger competitors. Many businesses are too large to give the friendly, personal service that small business ventures can provide.

Three basic personal selling skills which you and your employees must develop are:

1. The skill to determine the needs and wants of customers;
2. A solid foundation of product knowledge, including the product's uses, advantages, and limitations; and
3. The ability to convince customers that the product or service will fulfill their needs and wants.

Advertising

Advertising is any non-personal presentation of information about products or services that is paid for by an identified sponsor. The written or spoken words of an advertising message are contained in **advertising copy.** The **media** are the carriers of the advertising message, such as newspapers, radio, magazines, and television. You should look for the most effective means to carry your message to your target market. Ask media representatives for your information about their services and what results you can expect for your money.

The two types of advertising are product and institutional. **Product advertising** features specific products and services for the purpose of creating immediate sales volume. An advertisement for rubber shoes is an example. **Institutional advertising** focuses on the enterprise itself and is designed to create a favorable image and to build goodwill. For example, a retail store may advertise that it offers many customer services.

Entrepreneurs may attempt to achieve these goals through advertising:

- Encourage potential customers to visit stores or showrooms.
- Explain how products can be used.
- Announce the availability of parts or services.
- Invite requests for catalogs.
- Introduce new products or services.
- Explain new uses for old products.
- Encourage requests for samples of products.
- Depict the entrepreneur as a good citizen in the community.
- Explain product or service warranties.
- Announce locations where the enterprise's products or services may be purchased.

To plan an advertising program, you must identify the goals you want to achieve. Then you can choose the messages and media that will help reach the goal.

Because you may not have much money to spend, try to get the maximum value for each dollar of advertising. To do this, you must first determine how much you will spend on advertising in the first year. Then check this against what similar business ventures spend. Trade associations usually have this information. In new business ventures, advertising expenditures are often slightly above average for the line of business. If the figure is too high, adjust it to fit your budget.

Sales Promotion

Sales promotion includes all those activities which are designed to build sales by supplementing advertising and personal selling. Sales promotion activities are directed toward your customers, whether they are individuals or other businesses.

Sales promotion activities designed for consumers include coupons, in-store product demonstrations, free samples, store counter and window displays, contests, and information booklets.

Various services that one business performs for another are a type of sales promotion. The purpose of these services is to encourage retailers or dealers to carry certain products. Examples include booths set up at trade shows, free merchandise, training programs for salespeople, installing displays, sales manuals, and other selling aids.

Questions to Answer:

Part I.

Match the following terms with the statements that best define the terms. Write the letter of your choice in the space provided.

A.	Marketing	**R.**	Intermediaries
B.	Marketing strategy	**S.**	Agents
C.	Marketing concept	**T.**	Industrial distributors
D.	Consumer products	**U.**	Price
E.	Convenience goods	**V.**	Markup
F.	Shopping goods	**W.**	Delivered cost of goods
G.	Specialty goods	**X.**	Skimming pricing policy
H.	Consumer services	**Y.**	Penetration pricing policy
I.	Industrial products	**Z.**	Promotion
J.	Raw materials	**AA.**	Personal selling
K.	Processed materials	**BB.**	Advertising
L.	Parts	**CC.**	Advertising copy
M.	Supplies	**DD.**	Media
N.	Installations	**EE.**	Product advertising
O.	Accessory equipment	**FF.**	Institutional advertising
P.	Industrial services	**GG.**	Sales promotion
Q.	Channel of distribution		

	1.	Tasks individuals and families pay others to do or provide for them.
	2.	Inexpensive items that consumers buy often and with little shopping effort.
	3.	The path that a product follows from the producer to consumers or business users.
	4.	The methods you use in reaching the target market.
	5.	Equipment used in operating a business but having a useful life shorter than that of installations
	6.	Products individuals and families buy for their personal use.
	7.	Products that consumers will make a special effort to buy.
	8.	A type of advertising designed to create a favorable image and to build goodwill for the enterprise.
	9.	The method of promotion in which a salesperson makes direct contact with a customer.
	10.	The exchange value of products and services stated in terms of money.

	11.	Items incorporated into a finished product with little or no change.
	12.	The process of informing customers of your offerings and persuading them to buy your products or services.
	13.	The practice of charging a relatively high price for a new product or service.
	14.	Tasks one business pays another business to perform for it; also called business services.
	15.	Businesses that aid in transferring goods from the producer to the user.
	16.	The written or spoken words of an advertising message.
	17.	Items which aid in a firm's operations but do not become a part of the finished product.
	18.	A way of thinking about a business in terms of consumer needs and wants.
	19.	Participants in the channel of distribution who assist in the sale of products without owning the products.
	20.	The cost of the merchandise itself plus shipping costs.
	21.	All those activities which are designed to build sales by supplementing advertising and personal selling.
	22.	Any non-personal presentation of information about products or services that is paid for by an identified sponsor.
	23.	Products that are in their natural state when businesses buy them.
	24.	Items people buy after comparing the price, quality, and other features of similar items.
	25.	A type of advertising that features products or services for the purpose of creating immediate sales volume.
	26.	Products that are produced by one business but which will be changed into another firm by other businesses.
	27.	Major items used to produce a product or to provide a service.
	28.	The practice of setting a low initial price to attract customers quickly.
	29.	Carriers of the advertising message, such as newspapers, radio, magazines, and television.
	30.	A set of business activities that provides products and services to satisfy consumer needs and wants.
	31.	The amount that is added to the cost of an item in arriving at the selling price.
	32.	Wholesalers who buy products from manufacturers and sell them to industrial users.
	33.	Products that one business buys from another business.

Part II.

Write a short answer to each of the questions below.

1. The marketing concept is based on three basic beliefs. List and explain each.
2. What five elements of the marketing process are important to the new enterprise?
3. Products and services can be divided into what two large groups?
4. What five channels of distribution are widely used in the marketing of consumer products?
5. Name four common channels of distribution for industrial products.
6. What is the meaning of the statement "You should determine what your target market believes about how price and quality are related"?
7. List the three methods of promotion and give and example of each.

MODULE 7

OBTAINING CAPITAL

An entrepreneur needs money to start a business. In addition, an entrepreneur must be able to manage the money to ensure that the enterprise reaches its fullest potential. The money and credit required to run a business are its capital. Some entrepreneurs go into business with the few pesos they have saved, only to find that this is not enough money. Unfortunately, they do not become aware of the problem until faced with a financial crisis, such as not being able to pay their employees or suppliers. Entrepreneurs should not expect to avoid all money problems. However, by anticipating their financial needs, entrepreneurs can plan ahead for the problems that may arise.

OBJECTIVES:

After studying this module, the student should be able to:

1. Estimate start-up costs for a new enterprise.
2. Identify sources of funds.
3. Describe differences between short-term and long-term capital needs.
4. Identify factors in need for additional capital.
5. Suggest tips for requesting loans.

ESTIMATING START-UP COSTS

How much money will you need to start your new enterprise. There is no standard answer to this question because each new business is different. For example, money needs vary according to the field of business activity—that is, extractive, manufacturing, wholesaling, retailing, or service. Another determining factor is the size or scale or operations. Obviously your immediate costs will be higher if you have several employees from the start than if yours is a one-person business.

To determine starting costs, you need to estimate your sales volume for the first year. Since your estimate is likely to differ from the actual sales volume, you should select a conservative estimate. A **conservative sales estimate** is one that is ore likely to be too low than too high. This is desirable because a high estimate will lead you to invest too much money at the beginning.

You should also select a conservative figure when estimating expenses. A **conservative expense estimate** is one that is more likely to be too high than too low. By overestimating expenses, then, you are less likely to get caught short of money.

The two categories of start-up costs are one-time costs and continuing costs. **One-time costs** are expenses that will not have to be repeated once the business is under way. The purchase of a sign to be place don the building is an example. On the other hand, **continuing costs** must be paid both at the beginning ad throughout the life of the enterprise. Examples are rent, telephone, and advertising expenses. Plan to have enough cash on hand to pay continuing costs for more than just the first month. Some experts say you should be prepared for at least the first three months' expenses.

TYPES OF FUNDS

The two types of funds for businesses are equity funds and debt funds. In operating their businesses, most entrepreneurs use a combination of these two types.

Equity Funds

Equity is another word for ownership. Thus, **equity funds** consist of money or capital contributed by owners. Entrepreneurs' personal sources of money include savings, retirement benefits, sale of a home, or inheritance. If sufficient start-up money cannot be obtained from personal sources of equity, an entrepreneur may take in a partner or form a corporation and sell shares of stock. Since, in many cases, there is not enough equity money available, entrepreneurs resort to debt funds.

One-time Costs

Equipment, machinery, fixtures
Charges for installing equipment, machinery, fixtures
Decorating and remodeling costs
Beginning inventory of merchandise or raw materials
Deposits for utilities
Fees for accountants and lawyers
Licenses and permits
Advertising and sale promotion for "grand opening"
Cash for unexpected needs

Continuing Costs

Salaries for proprietor or partners
Salaries and wages for other employees
Rent
Advertising and sales promotion
Delivery or shipping expenses
Supplies and materials
Utilities (telephone, gas, water, electricity)
Insurance of all types
Taxes (federal, state, local)
Interest on debt
Repairs and maintenance
Fees for accountants and lawyers
Employee training costs
Unexpected needs

Debt Funds

Debt funds are dollars or capital you borrow. Banks, other financial institutions, and individuals are all sources of debt funds. The privilege of paying for goods and services after they have been delivered or provided is **credit**. Suppliers of merchandise or equipment may sell to business on credit terms. When entrepreneurs borrow money or use credit, a charge is involved known as **interest.**

Comparison of Funds

An entrepreneur should use both equity funds and debt funds for sources off capital. The type of funds used depends on these factors: risk, control, and availability.

Risk. There is little risk to the enterprise with equity capital. Owners do not have to be repaid. By contrast, great risk is involved with debt funds. Failure to make loan payments when they are due could cause lenders to require that the loan be repaid in full immediately. An entrepreneur may have to sell real estate or other business property to obtain sufficient money to repay a loan, or lenders may take ownership of the entire business.

Control. An owner’s degree of control is usually directly related to the percentage of ownership. That is, the more ownership an entrepreneur has, the more authority the entrepreneur will have regarding the operation of the business. Entrepreneurs lose some control of their businesses every time they take in a partner or sell shares of stock. An entrepreneur who started a business to be a boss may suddenly feel as though others are in control. On the other hand, lenders do not ordinarily get actively involved in the operation of their borrowers’ businesses.

Availability. At a particular time, either debt funds or equity funds could be difficult to obtain. Debt funds may not be available to the business because of high interest rates, the entrepreneur’s poor personal credit record, or a history of low earnings or losses for the enterprise. The only sources of available funds may be to obtain equity from new partners or to sell stock. In other situations, an entrepreneur may be unable to find equity investors, leaving the entrepreneur with no alternative buy to borrow the money.

SOURCES OF FUNDS

Equity funds are invested in the business by an entrepreneur, one or more partners, or stockholders. These people are owners and are usually willing to wait months or years to be repaid. Therefore, equity funds are usually considered to be long-term funds. In contrast, some debt funds are short-term and must be repaid quickly, while others are long-term.

Businesses need both current assets and fixed assets. **Current assets** are cash and any other assets that can be easily and quickly turned into cash. Inventory and accounts receivable are examples of current assets. **Inventory** may include raw materials, finished goods, or supplies. **Accounts receivable** are sums of money owed to the business by customers.

Fixed assets are items that the business expects to own for more than one year. These items are not used up, or converted into cash, in a short period of time. Typical examples are land, buildings, equipment, and trucks.

The key to successful business financing is to obtain current assets with short-term loans or credit and to obtain fixed assets with long-term loans. For example, an entrepreneur should consider a 90-day bank loan to buy inventory or a 15-year loan to buy property.

Short-Term Loans or Credit

Short-term loans and credit are available from vendors, commercial banks, commercial finance companies, and factors.

Vendors. Vendors are businesses from which entrepreneurs buy products. While vendors do not usually lend money, they will often supply merchandise and allow businesses to pay for the merchandise by a specified date. Under this arrangement, known are **trade credit**, entrepreneurs may have 30 or more days to pay their bills. The exact credit terms depend on the line of trade and the credit rating of the enterprise. To those who have satisfactory payment records, a vendor may extend credit interest-free. An advantage of trade credit is that an entrepreneur may sell the merchandise to obtain the money needed to pay a vendor’s bill.

Commercial Banks. Local commercial banks are one of the best sources of short-term loans. The primary short-term loan is the **commercial loan**, usually made for 90 to 180 days. This loan is generally made without any specific **collateral**, which is something of value the borrower pledges to the bank as security for the loan. Commercial loans are advanced to profitable businesses with good credit ratings. Entrepreneurs are required to repay commercial loans in a lump sum.

When many of the current assets are held in unpaid customer accounts and the enterprise needs more cash, an accounts receivable loan may be the answer. Available from commercial banks, **accounts receivable loans** involve the pledging of accounts receivable as collateral for a short-term loan. This type of loan allows an entrepreneur to convert unpaid customer accounts into cash. Banks usually advance up to 80 percent of the value of the accounts receivable, allowing themselves some protection for uncollectible accounts. Typically, the accounts receivable loan is set up as a revolving line of credit for the business borrower. In a **revolving line of credit**, funds are continually advanced to the enterprise, repaid, and advanced once again. The entrepreneur pays interest on the remaining balance of the loan.

Commercial banks also engage in inventory financing. With **inventory financing**, an entrepreneur pledges inventory as collateral for short-term funds to receive a revolving line of credit. Entrepreneurs repay inventory loans as cash flows into the enterprise from the sale of items in inventory.

When an established business is profitable, the enterprise may qualify for an unsecured line of credit. For this type of loan, no collateral is pledged. Generally, an entrepreneur may borrow, repay, and borrow again within a one-year period.

Commercial Finance Companies. Commercial finance companies are specialists in accounts receivable and inventory loans. They often combine the collateral of accounts receivable and inventory loans to provide a business with a larger line of credit. They seldom make unsecured loans to small businesses.

Factors. Entrepreneurs may pledge account receivable as collateral for a loan, and they can also sell accounts receivable to obtain short-term funds for the business. Selling accounts receivable is called **factoring**. Financial firms that buy accounts receivable are **factors.** Factors purchase the accounts receivable at less than face value and then collect the full amounts from customers when payments are due. While this service has a cost, businesses obtain funds without waiting for customers to pay their bills.

Long-Term Loans

In most cases, part of the financing of the new enterprise will consist of long-term loans, also known as **term loans.** Term loans are extended fro more than one year and are usually to obtain land, buildings, equipment, and other fixed assets. Some commercial banks and commercial finance companies make both short-term loans and long-term loans. Equipment manufacturers and distributors also provide long-term financing.

Commercial Banks. One of the Primary sources of long-term loans, particularly those extended for three to five years, is the commercial bank. The bank's installment loan department generally processes long-term loans. Most commercial banks require a written loan agreement for a long-term loan. The agreement may limit the amount of salary entrepreneurs pay themselves or require entrepreneurs to obtain approval form the bank before borrowing money from other sources. The bank may also require a compensating balance. A **compensating balance** is a sum of money deposited in the bank for the duration of the loan to serve as collateral. Commercial banks may offer term loans with personal guarantees, equipment loans, and real estate loans.

Term Loans with Personal Guarantees. Through **personal guarantees**, borrowers agree to pay the unpaid balance of the loan if the business, including a corporation, is unable to repay it. Asking for a personal guarantee is standard procedure for small business loans, especially when the business is not yet operating. This permits the bank to recover its money if the business fails. The personal guarantee is also a measure of the entrepreneur's confidence in the business.

Equipment Loans. Equipment loans enable an enterprise to buy new equipment or to obtain funds when the firm does not qualify for unsecured credit. Most banks limit their equipment loans to between 60 and 80 percent of the value of the equipment. The loans are usually repaid in monthly installments for a maximum of five years, depending on the useful life of the equipment.

Real Estate Loans. Real estate loans are usually made for up to 75 percent of the value of the land and/or buildings and repaid over 10 to 20 years. The bank will require a **first mortgage** as security for the real estate loan. If the borrower fails to make the payments, ownership of the property will be transferred to the bank.

Commercial Finance Companies. The three types of long-term financing offered by commercial finance companies are equipment loans, real estate loans, and equipment leasing. Equipment loans are provided in the same form as those granted by commercial banks. The loan period is determined by the useful life of the equipment. The equipment serves as collateral for the loan, and the funds are advanced to cover up to 80 percent of the cost of the equipment.

Likewise, commercial finance companies offer real estate loans similar to those offered by the commercial banks. However, these loans are not available from all commercial finance companies.

Through **equipment leasing**, individuals may obtain and use equipment without owning it. Rather than paying for equipment in one lump sum, lease payments are made as the equipment is used. Cash that would otherwise be tied up in a fixed asset is available to buy inventory or pay current expenses.

Equipment Manufacturers and Distributors. To encourage entrepreneurs to buy their equipment, manufacturers and distributors often will finance the purchase. This can be an important source of funds but only for the amount of the purchase price. Usually a down payment is required, and the balance is paid in monthly installments. The payment period may extend over one of more years, depending on the type and price of the equipment.

FACTORS IN NEED FOR ADDITIONAL CAPITAL

As a business grows, so does the need for more and more capital. Some of the more common factors creating this need are sales growth, expansion of the business, opportunities to reduce costs, seasonal factors, and economic conditions.

Sales Growth

To keep up with an increasing sales volume, entrepreneur will have to continually buy more inventory. Because the goods must be available and ready for sale when customers want them, an entrepreneur must buy inventory at a rate faster than the increase in sales.

Sales growth can create a larger volume of accounts receivable. In addition, sales growth requires the business to have larger amounts of cash to pay wages to more employees and to pay wages to more employees and to pay increased expenses brought about by increased sales. The business must sometimes borrow money until customers pay their bills.

Expansion

When entrepreneurs expand to open an office at an additional location or to include a new product or service line, they need more capital. Sometimes these expenses equal or exceed the initial start-up costs of establishing the business.

Opportunities to Reduce Costs

Sometimes entrepreneurs must be prepared to spend money to save money in the long run. For example, an entrepreneur may have the opportunity to buy new machinery t hat will lower the cost of producing the firm’s primary product. Another example is spending money for more efficient heating and cooling equipment to reduce the firm’s utility bill.

An entrepreneur may receive substantial savings by taking advantage of quantity discounts on inventory purchases. A **quantity discount** is a reduction in price as a result of the amount purchased. The discount could be based on the amount of one particular item ordered or on the total amount of all items. For example, an order for 500 items at PhP 10 each instead of a usual order of 100 items may qualify the buyer for a 5 percent discount. The discount saves the buyer 50 centavos per item. However, the entrepreneur must have cash or be able to arrange credit to take advantage of the discount offer.

Seasonal Factors

Rather than having a constant level of sales from month to month, many businesses experience peaks and valleys in their sales volumes. For instance, Toy manufacturers sell a large part of their annual production in a few months each year. Retailers and wholesalers order toys in the spring and summer months for delivery prior to the Christmas gift buying season. Likewise, suppliers of school supplies sell a major portion of their products for delivery just prior to the beginning of the school year. As a result, large amounts of cash flow into these businesses in some months, while little or no cash flows in during other months. Seasonal needs can create a need for additional capital. To prepare for major selling seasons, entrepreneurs may have to borrow money to buy additional materials and supplies and to hire more employees.

Economic Conditions

Local or national economic conditions may cause temporary decreases in sales and profits. For example, other businesses in the community suffer when manufacturing plants close, leaving employees without jobs. The jobless people do not have the spending ability they once had, thereby reducing the sales of other businesses in the community. Business owners may need to borrow money to pay expenses until conditions improve. Rent, utilities, and wages must be paid, even when the sales volume is low.

TIPS FOR REQUESTING LOANS

Entrepreneurs should prepare themselves for meeting with a lender to ask for a loan. While this discussion deals with commercial banks, many of the suggestions also pertain to obtaining loans from other types of lenders.

Tips that may improve the entrepreneur's chances of obtaining a bank loan are (1) selecting a bank carefully, (2) preparing financial statements, (3) making an appointment, (4) preparing to answer typical questions, and (5) preparing the guarantee the loan.

Select the Bank Carefully

Some banks deal mostly with large corporations. Others aim to serve consumers and perhaps small businesses. Entrepreneurs should select banks that specialize in making loans to businesses, particularly those banks having a history of working with firms similar in size and type to theirs. Loan processing time may be reduced when the banker is familiar with the industry, the products and services sold, and the customers.

If, for reasons beyond their control, entrepreneurs are unable to make loan payments on time, a banker who understands the business may be willing to make other arrangements for repayment. Other lenders may not be as willing to discuss alternatives for repaying the loan.

Prepare Financial Statements

The lending officer of the bank will ask to see a complete set of financial statements. Although some entrepreneurs prepare these statements themselves, it is wiser to have an accountant prepare the financial statements to be assured of a thorough financial file. Without assistance from an accountant, an entrepreneur may not borrow enough money in the beginning. Having to return for additional loans later could make the lending officer suspect that the entrepreneur does ot know how to operate the business and may be a poor risk.

Make An Appointment

People walk into banks and apply for credit cards and car loans every day. This is the common practice for these transactions. When seeking a business loan, however, it is customary to make an appointment. Entrepreneurs who ask for appointments show they are business-minded.

Prepare to Answer Typical Questions

The lending officers of commercial banks will ask questions to determine if the borrower qualifies for a loan. Entrepreneurs should be prepared to answer these typical questions:

- *How do you plan to spend the money?* The funds should be used for equipment, inventory, or other expenses directly related to the sales and profits of the business. A loan request is generally approved only if the money will be used directly I the business of if the plan is to start a low-risk venture.
- *How much money do you need?* Entrepreneurs should request neither too much nor too little money. The more specific borrowers are in the answering this question, the more likely they are to get the loan.
- *When do you need the money?* A committee will review loan requests. Because committee reviews of loan applications take time, borrowers should apply early for a bank loan before their funds are gone. Lenders look more favorably on those who plan ahead.
- *When will the loan be repaid?* The shorter the period of time the money is needed, the better the chances of getting the loan. Bankers associate shorter time periods with lower risk.
- *What is the source of the money for repaying the loan?* Bankers will need to know how an entrepreneur plans to repay the loan. Money borrowed to buy inventory, for example, can be repaid when the inventory is sold.

Prepare to Guarantee the Loan

Even the best credit prospects should be prepared to personally guarantee their loans. If the business fails, the entrepreneurs may have to sell personal and family property to repay a business loan. Clearly, this involves risk. On the other hand, if entrepreneurs are not willing to risk their assets, why should banks risk theirs?

Questions to Answer:

Part I.

Write a short answer to each of the questions below.

1. Why should conservative sales estimates and conservative expense estimates be used?
2. Explain the difference between one-time costs and continuing costs. Give an example of each.
3. What is the difference between equity funds and debt funds?
4. What factors should the entrepreneur consider when deciding whether to use debt funds or equity funds in a particular situation? Explain each of these factors.
5. What types of assets should be obtained with short-term loans or credit? Which assets should be obtained with long-term loans?
6. List four sources of short-term loans or credit.
7. List three sources of long-term loans.
8. Give five reasons why businesses may need more and more capital as they grow.

Part II.

Analyze the case and answer the questions

GONZALES CONSTRUCTION COMPANY

In six months or less, Sara and Roy Gonzales plan to have their construction company in operation. They have twelve years of construction experience between them, and they believe they know what it takes to run a successful company.

Roy prepared a list of rough estimates of all the one-time costs and continuing costs for the new enterprise. Sara, an experienced accountant, closely reviewed each item on the list and revised the figures where necessary. Finally Sara and Roy reviewed the list together until they were confident that each cost estimate was as accurate as possible. Now that the couple know what their costs will be, they are not certain how or where they will obtain the funds to start the business.

Roger Santos, a former construction company owner, contacted Sara and Roy. He offered to invest in their business and become their partner. Santos' investment would be larger than Sara and Roy's investment. The Gonzales couple are flattered that someone would come to them and offer to buy into their business. They also like the idea that, with Mr. Santos' investment, they would not have to borrow any money. At the same time, they do not want to accept anyone's investment until they have had the chance to think about all the alternatives available to them. They are also wondering why Mr. Santos is interested in their business when it is not yet in operation.

Before Sara and Roy accept Mr. Santos' offer, they are considering visiting a bank to discuss the possibility of obtaining a loan.

Questions:

1. Would you advise the Gonzales couple to use only equity funds in starting their business Why or why not?
2. Why do you believe Roger Santos wants to invest in the Gonzales Construction Company?
3. What should the Gonzales couple do to prepare to meet with the loan officer at the commercial bank?

MODULE 8

PREPARING FINANCIAL STATEMENTS

Some entrepreneurs run into financial difficulty even when they attain high sales volumes. Their concern with the day-to-day operation of their business ventures causes them to overlook the part of the business plan that will tell them if, and when, they will make a profit. They have neglected financial planning. You will learn about this critical part of the business plan in this chapter. Through **financial planning**, you will describe your business plan in terms of dollars.

OBJECTIVES:

After studying this module, the student should be able to:

1. Prepare a cash budget, an income statement, and a balance sheet.
2. Describe how price, volume, cost of sales, and operating expenses affect net profit.
3. Set a goal for a new enterprise.

FINANCIAL STATEMENTS

Financial statements can take various forms depending on how you want to use them. Their purpose is to document important facts about the enterprise's operation. The business plan for a new enterprise should include three financial statements: a cash budget, an income statement, and a balance sheet.

Cash Budget

A **cash budget** is a measure of changes in the cash an enterprise will have available from month to month. Businesses use cash budgets to estimate cash needs for a period in the future, usually twelve months.

The first step in preparing a cash budget is to determine the **cash balance** at the beginning of the month. This shows how much cash is on hand (e.g., in cash registers) and in the bank.

The second step is to estimate cash receipts. **Cash receipts** include all funds that will be received from cash sales, collection of credit sales, and loans. This estimate will be based on your sales forecast. When cash receipts are added to the cash balance, the sum is the total cash available for use by the business during the month.

The next step in the budget process is to estimate **cash disbursements.** These refer to cash that will have to be paid out during the month for purchases and operating or continuing expenses. The largest cash outlays are usually for merchandise and wages and salaries.

Finally, when you subtract the total cash disbursements from total cash available, the result is the cash balance at the end of the month. This figure then becomes the beginning cash balance for the next month.

The cash budget formula is:

Beginning Cash Balance for MONTH 1
+ Cash Receipts .
= Total Cash Available
- Total Cash Disbursements .
= Cash Balance at End of MONTH 1
= Beginning Cash Balance for MONTH 2

To further explain how a cash budget is prepared, let us assume that Christian and Manuel are planning to open a T-shirt shop on July 1. All the one-time costs of start-up have been paid and they have PhP20,000 in cash.

Christian and Manuel have decided to sell only on a cash basis, at least for the time being. They estimate their sales for the first three months as follows: PhP30,000 in July, PhP40,000 in August, and PhP48,000 in September. They believe their cash disbursements for those months will be PhP32,000, PhP41,000, and PhP49,000 respectively.

As their cash budget shows, sales increase each month, but the cash balance decreases because their expenses increase each month. This may be a signal that the business is heading for trouble. Without the cash budget, the partners might not have learned of the problem until it was too late. At least now they have time to do something about it. Fore example. They should find out if they are overspending in some areas. Maybe they have spent too much on merchandise, or they may want to arrange for a loan in case the cash balance continues to slide. The loan could then be repaid when the cash situation improves.

Income Statement

The **income statement** shows how a business has performed over a certain period of time. It is also referred to as a **profit-and-loss statement.**

Some entrepreneurs prepare income statements just once a year; others do so more frequently. An entrepreneur of a new enterprise should prepare an income statement every month, or at least every three months. You will then have a better idea of how the business is operating. If problems occur, you will be able to take quick action.

The parts included in an income statement are sales, cost of sales, gross profit, expenses, and net profit.

The term **sales** refers to all income that flows into the business from sales activity. Extractive business ventures, manufacturers, wholesalers, and retailers obtain this income from the sale of goods. Service businesses derive their sales income from fees charged when services are provided.

Cost of sales represents the cost of the products or services sold in a given time period. Cost of sales is called **cost of goods sold** by retailers and wholesalers. It represents what they pay for products they sell. In manufacturing, cost of sales is known as **cost of goods manufactured.**

It includes only those costs directly associated with making the product. A service business may calculate the **cost of services sold** based on wages paid to persons providing the service.

Gross profit, known as **gross margin** when stated as a percentage, is determined by subtracting cost of sales from sales. Gross profit should not be confused with net profit, a term to be described below. The formula for calculating gross profit is:

Gross Profit = Sales – Cost of Sales

Expenses are all the costs of running an enterprise, other than those included in the cost of sales. Many continuing costs are expenses. Some of the items included are advertising, insurance, rent, utilities, and interest on debt.

Net profit is the income remaining after paying all expenses, including taxes.

The parts of an income statement are related as follows:

Net Profit = Sales – Cost of Sales – Expenses

or

Net Profit = Gross Profit – Expenses

A **projected income statement** is based on the entrepreneur's estimates of sales, cost of sales, and expenses for the first year. Such a statement should be included in every business plan. Without a projected income statement, the entrepreneur will not be able to determine the profit potential of the new enterprise.

When the business is actually in operation, data will be available to prepare a regular income statement. That is, the statement would be based on *actual* rather than *projected* figures.

Balance Sheet

The **balance sheet** is used to keep track of what an enterprise owns, what it owes, and what the owner has invested. A balance sheet is like a picture of the enterprise's assets and claims against those assets for a particular date.

This financial statement is called a balance sheet because assets balance with, or are equal to, liabilities plus net worth. This is shown as follows:

Assets = Liabilities + Net Worth

Assets are items or possessions used in the business which have monetary value. On the balance sheet, assets are divided into three groups: current assets, fixed assets, and intangible assets.

Current assets are those which the enterprise would not expect to hold longer than one year. This group includes cash as well as other items that can be easily and quickly converted to cash. Examples are merchandise in inventory and **accounts receivable**, which are sums of money owed to the enterprise by customers.

Fixed assets are items that the business expects to own for more than one year. These items are not used up, or converted into cash, in a short period of time. Typical examples are land, buildings, equipment, and trucks.

The third group of assets is **intangible assets.** These assets have value and are useful to the enterprise, but they do not exist in a physical sense. A common example is goodwill, which you may have to pay for when buying an existing enterprise. **Goodwill** is extra money paid because the enterprise has a good reputation. Other intangible assets found in balance sheets are copyrights, patents, and franchises.

Liabilities are debts of the enterprise. They are usually divided into two groups: current liabilities and fixed liabilities.

Current Liabilities are debts that are due to be paid in one year or less. Debts commonly included in this category are:

Accounts payable - Amounts owed to suppliers for goods and services provided.

Notes payable - Short-term loans that have to be repaid within a year.

Accrued expenses - Expenses incurred but not yet paid, such as wages that have been earned but not yet paid.

Debts that are due to be paid in more than a year are called **fixed liabilities**. They are also known as **long-term liabilities**. Mortgages and long-term loans are examples.

The excess of the value of the assets over the value of the liabilities is called **net worth.** This includes all money invested by owners, known as **owner's capital,** plus accumulated profits less withdrawals. The method for computing net worth is:

Net Worth = Total Assets – Total Liabilities

The balance sheet is important because it reveals the enterprise's ability to repay both long-term and short-tem debts. For this reason, bankers and other lenders often ask to see this financial statement before lending money.

BASIC PROFIT VARIABLES

Entrepreneurs make countless decisions about how their businesses are to operate. Some decisions are made infrequently and have long-term effects. An example is the decision to select a location for the enterprise. Other decisions, such as setting the price for an item, are made more frequently and have short-term effects. Ultimately, however, all decisions are related to the four basic profit variables of price, volume of sales, cost of sales, and operating expenses. A change in any one of the variable affects net profit.

As shown in Figure A, the owners of Fiesta Chair Store estimate that they will sell 1,000 chairs at a price of Php100 each. Total sales for the year will be Php100,000. The owners also expect to pay Php60 for each bicycle and to incur Php35,000 in operating expenses during the year.

Fiesta Chair Shop
Projected Income Statement
For Year Ended December 31, 2006

	Original Estimate
Sales (1,000 units @ 100)	100,000
Cost of Sales (1,000 unites @ 60)	60,000
Gross Profit	40,000
Operating Expenses	35,000
Net Profit	5,000

Figure A

Assume the Fiesta's owners want to see how changes in the basic profit variables would affect the original estimates shown in Figure A. The series of income statements in Figure B through E will illustrate the impact of these changes.

A Change in Price

One way to increase profits is to raise prices. Assume that the owners of Fiesta Chair Shop could raise prices by 5%, or Php5, and still sell 1,000 chairs during the year. Perhaps they are able to do this because their prices are not as high as their competitors' prices. With the price increase of 5%, the selling price for each chair would be Php105. The sales figure on the income statement would be determined as follows: 1,000 chairs x Php105 = Php105,000. The effect on net profit is shown in Figure B.

Fiesta Chair Shop
Projected Income Statement
For Year Ended December 31, 2006

	Change in Price	Original Estimate
Sales (1,000 units @ 105)	105,000	100,000
Cost of Sales (1,000 unites @ 60)	60,000	60,000
Gross Profit	45,000	40,000
Operating Expenses	35,000	35,000
Net Profit	10,000	5,000

Figure B

The percent by which a number increases or decreases can be determined by following two steps. First, find the peso amount of the increase or decrease from the original estimate. Second, divide the peso amount of the increase or decrease by the original estimate. The answer is the percent by which the number increased or decreased.

Notice that if the owners raised prices 5%, net profit would increase by 100%, from Php5,000 to Php10,000. This example points out the importance of making sound pricing decisions. Even small increases in prices can improve profits. Charging prices that are too low can lower profits or cause losses.

A Change in Volume of Sales

Prices charged for individual products and the number of products sold, or **volume**, together that determine the sales figure appearing on the income statement. Rather than increasing their prices, assume now that the owners of Fiesta Chair Shop want to see what would happen if they lower their prices. Specifically, they believe that they could sell 1,200 chairs, instead of 1,000, if they lower the price by 5%, or Php5. The selling price becomes Php95. On the income statement, the sales figure would be the product of multiplying Php95 by 1,200, or Php114,000. The effect on net profit of this change in sales volume is shown in Figure C.

Net profit will increase from Php5,000 to Php7,000 if the shop can sell 200 more chairs at the lower price of Php95. Note that the increase in sales volume was accompanied by an increase in cost of sales. This, of course, is a result of the need to buy 200 additional chairs for resale. In this example, the selling price was reduced by Php5, while sales volume increased by 20% and profit increased by 40%.

Fiesta Chair Shop
Projected Income Statement
For Year Ended December 31, 2006

	Change in Volume	Original Estimate
Sales (1,200 units @ 95)	114,000	100,000
Cost of Sales (1,000 unites @ 60)	72,000	60,000
Gross Profit	42,000	40,000
Operating Expenses	35,000	35,000
Net Profit	7,000	5,000

Figure C

A Change in Cost of Sales

Another way to increase net profit is to reduce cost of sales. Assume that Fiesta Chair Shop's owners have decided to replace the chairs they now carry with another manufacturer's chair. The new product is equal in quality to the current product, but it costs 5% less, or Php57 per chair. In Figure D, sales are Php100,000 and the cost of sales is Php57,000. Notice the effect of the change in cost of sales.

As a result of a 5% decrease in the cost of each unit sold, Fiesta Chair Shop's owners would see their net profit change from Php5,000 to Php8,000, an increase of 60%.

A Change in Operating Expenses

A fourth way to increase net profit is to reduce operating expenses. Assume that the owners Fiesta Chair Shop have studied every operating expense, such as wages, salaries, and rent, and they have decided that they could reduce some of those expenses to save Php5,000 during the year. Most of the savings would come from reducing the number of hours worked by their part-time employees and working more hours themselves. As shown in Figure E, the Php5,000 reduction in operating expenses results in a Php5,000 increase in net profit.

When other factors remain the same, net profit increases with:

Fiesta Chair Shop
Projected Income Statement
For Year Ended December 31, 2006

	Change in Cost of Sales	Original Estimate
Sales (1,000 units @ 100)	100,000	100,000
Cost of Sales (1,000 unites @ 57)	57,000	60,000
Gross Profit	43,000	40,000
Operating Expenses	35,000	35,000
Net Profit	8,000	5,000

Figure D

1. An increase in price.
2. An increase in volume.
3. A decrease in cost of sales.
4. A decrease in operating expenses.

With the exception of sales volume, which is accompanied by a change in cost of sales, the other variables operate independently of one another. That is, a change in one variable does not affect another variable.

Fiesta Chair Shop
Projected Income Statement
For Year Ended December 31, 2006

	Change in Operating Expenses	Original Estimate
Sales (1,000 units @ 100)	100,000	100,000
Cost of Sales (1,000 unites @ 60)	60,000	60,000
Gross Profit	40,000	40,000
Operating Expenses	30,000	35,000
Net Profit	10,000	5,000

Figure E

SETTING YOUR GOAL

As you finish reading this final module, you may have realized that you want to become an entrepreneur. If so, choose a tentative date for starting your enterprise. It may be next week, next year, or a few years away. The important thing is that you give yourself a target date. Then think about these questions:

1. What will you be doing between now and the day you begin the enterprise? What work experience and further schooling can you obtain to prepare for a career in entrepreneurship?
2. What can you do to make sure you are financially prepared to create your own enterprise? How much money can you save in the meantime?

If you are serious about becoming an entrepreneur, you can use your business plan as a guide in reaching your goal.

Questions to Answer:

Part I.

Match the following terms with the statements that best define the terms. Write the letter of your choice in the space provided.

A.	Financial planning	**P.**	Balance sheet
B.	Cash budget	**Q.**	Assets
C.	Cash balance	**R.**	Current assets
D.	Cash receipts	**S.**	Accounts receivable
E.	Cash disbursements	**T.**	Fixed assets
F.	Income statements	**U.**	Intangible assets
G.	Sales	**V.**	Goodwill
H.	Cost of sales	**W.**	Liabilities
I.	Cost of goods sold	**X.**	Current liabilities
J.	Const of goods manufactured	**Y.**	Accounts payable
K.	Cost of services sold	**Z.**	Notes payable
L.	Gross profit	**AA.**	Accrued expenses
M.	Expenses	**BB.**	Fixed liabilities
N.	Net profit	**CC.**	Net worth
O.	Projected income statement		

	1.	A financial statement that shows how a business has performed over a certain period of time; also known as a profit-and-loss statement.
	2.	Assets that have value and useful to the enterprise but do not exist in a physical sense.
	3.	All the costs of running an enterprise other than the cost of sales.
	4.	Describing your business plan in terms of pesos.
	5.	Amounts of money owed to suppliers for goods and services purchased.
	6.	Income flowing into the business from sales activity.
	7.	Debts of the enterprise.
	8.	A measure of changes in the cash an enterprise will have available from month to month.
	9.	Expenses incurred, but not yet paid.
	10.	A figure that includes only those costs directly associated with making the product.
	11.	The income remaining after paying all expenses, including taxes.

	12.	A figure based on wages paid to persons providing a service.
	13.	Debts that are due to be paid in one year or less.
	14.	The excess of the value of the assets over the value of the liabilities.
	15.	Funds received from cash sales, collection of credit sales, and loans.
	16.	A financial statement based on estimates of sales, cost of sales, and expenses.
	17.	Items or possessions used in the business which have monetary value.
	18.	The total of cash on hand and in the bank.
	19.	The cost of the products or services sold in a given period of time.
	20.	Assets the enterprise would not expect to hold longer than one year.
	21.	What retailers and wholesalers pay for products they sell.
	22.	Cash paid out for purchases and for operating or continuing expenses.
	23.	Items that the business expects to own for more than one year.
	24.	The difference between sales and cost of sales; known as gross margin when stated as percentage.
	25.	Short-term loans that have to be repaid within a year.
	26.	Sums of money owed to the enterprise by customers.
	27.	The extra money paid to buy an existing enterprise because the business has a good reputation
	28.	Debts that are due to be paid in more than a year; also known as long-term liabilities.
	29.	A financial statement used to keep track of what an enterprise owns, what it owes, and what the owner has inbested.

Part II.

Write a short answer to each of the questions below.

1. What financial statements should be included in the business plan?
2. Describe the cash budget formula.
3. Show how the parts of an income statement are related.

4. Explain why one type of financial statement is called a balance sheet.
5. Describe each of the four basic profit variables.
6. What questions should you ask yourself after setting a tentative date for starting a new enterprise?