# TOPIC 1.3 PUTTING A BUSINESS IDEA INTO PRACTICE

tutor2u

START

**1** **Define** the following terms:

a) Aim

b) Objective

**2** In relation to a business setting objectives **state** what is meant by the acronym SMART.

**3** **Explain**, with examples, the difference between financial and non-financial aims & objectives.

**4** Using the data drop provided, **calculate** the total revenue assuming Chris completes jobs for 750 customers.

**14** Chris is optimistic about year two for 'Green Fingers'. He has now established a strong customer base from homeowners and has been approached by 3 local primary schools to maintain their school fields and gardens. Chris is keen to pursue this but will need an additional £15,000 of capital. **Explain** which source of finance would be the best for his expansion.

**13** Chris has worked hard to build strong relationships with his suppliers over the last 12 months however he is still having to use his arranged overdraft facility in order to pay cash for his materials. **Outline** the benefits to Chris of using trade credit as an alternative means of short term finance.

**12** **Explain** the importance of cash flow to Chris.

**11** **Chris is concerned about the seasonal nature of his business. Since the end of October he has watched his closing balance continue to decrease and is worried he may experience negative cash flow. Outline two options for Chris to help him deal with this problem.**

**10** Chris calculated his closing balance for November to be £3,500. Using the data drop provided **calculate:**

a) The net cash flow for December

b) The closing balance for December

**9** Chris thinks that the variable cost per job is going to increase by a further £1.50. **Explain** the impact of this on break-even. You may use calculations to support your answer.

**8** Using either the data drop provided, or your answers to questions 4 and 5, **calculate** the profit made by Chris based on the 750 customer jobs completed.

**5** **Calculate** the total costs for Green Fingers using the data drop provided and assuming 750 jobs are completed.

**6** Costs can be classified as fixed or variable. **Explain**, using a suitable example for Green Fingers, what is meant by the terms:

a) Fixed costs

b) Variable costs

**7** Using the data drop provided:

a) **Calculate** the break-even level of output for Green Fingers.

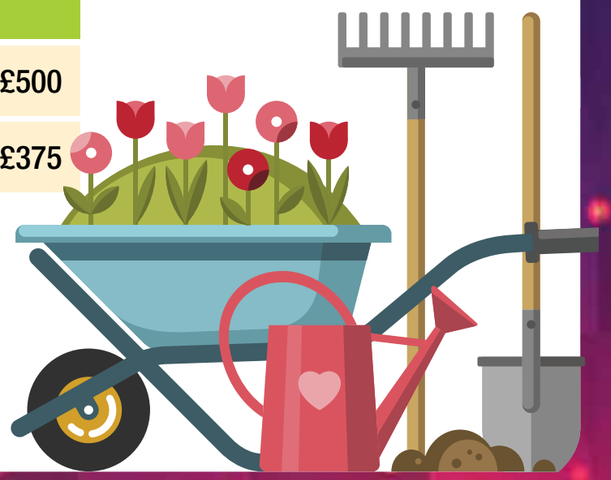
b) **Calculate** the margin of safety based on Chris completing 750 jobs.

## BUSINESS PROFILE

## Green Fingers

Green Fingers is a small gardening business set up and run by Chris Green. Chris borrowed £10,000 from the bank to purchase his van and equipment and is paying this back in fixed instalments over the next 5 years. Chris has had a successful first year and despite some issues with seasonal demand, he is looking to expand his services as he moves into his second year of operation.

| Data Drop | | | |
|---|---|---|---|
| Average price per customer | £20 | Cash inflows - December | £500 |
| Fixed Costs | £4500 | Cash outflows - December | £375 |
| Variable cost per job | £5 | | |



# ENTERPRISE & ENTREPRENEURSHIP SUGGESTED ANSWERS

**1** *Aim – a general statement about the direction of a business.*

*Objective – a clear measurable goal to judge success or failure by.*

**2** *Specific, Measurable, Achievable, Realistic and Time-bound.*

**3** *Financial objectives relate to making money and can include profit, sales, market share.*

*Non-financial do not involve the business making money but reflect the social objectives, challenge or personal satisfaction that can be gained from running a business.*

**4** *TR = SP x Q*

*TR = 20 x 750 = £15,000*

**14** *Chris will be looking at long term sources to finance this amount of money needed. It is unlikely that he will have any personal savings left, he has already taken out a loan, and there will be insufficient profit from the business to source the expansion. Chris would therefore be advised to approach the bank to get another loan based on the success of his first year and the future orders he has been offered.*

**13** *Trade credit would be negotiated with a supplier to allow Chris to delay his payment for materials. This could allow him the chance to carry out a job and receive payment before he has to pay his suppliers, therefore improving his cash flow position. Unlike an overdraft, trade credit will not cost Chris anything to use, although he may miss out on possible cash discounts by using trade credit.*

**12** *Cash flow is important to Chris to ensure that his business survives and has enough inflow to meet day to day expenditures. Chris has a bank loan and needs to ensure that he has sufficient cash available to keep up with the monthly repayments on the loan. In addition Chris needs to have cash available to pay his suppliers on time and pay overheads e.g. the cost of his mobile phone – essential to Chris so customers can contact him with bookings.*

**11** *To improve cash flow Chris can:*
*Increase his credit terms with his suppliers to enable him to delay payment. This will reduce cash outflow during the period when inflows are lower.*

*Cut his stock levels and therefore reduce the money he has tied up in any materials especially during the winter when there is less demand.*

## TIME TO REVIEW YOUR LEARNING...

List three content points that you are confident with and three that require some attention.

| Confident with | Requires attention |
|---|---|
| 1 | 1 |
| 2 | 2 |
| 3 | 3 |

**10** a) *Net cash flow = inflow – outflow = 500 – 375 = £125*

b) *Closing balance = opening balance + net cash flow = 3,500 + 125 = £3,625 closing balance for December*

**9** *New VC = £5 + £1.50 = £6.50*
*New contribution per unit =*
*SP – VC = 20 – 6.50 = £13.50*
*New Break even = 4500 / 13.50 = 333.33 jobs -*
*Chris needs another 34 jobs in order to break even.*
*His margin of safety will be reduced = 750 – 334 = 416 customers*
*He could increase prices but this may impact on demand*

**5** *TC = FC + TVC*

*TC = 4500 + (5 x750) = £8,250*

**6** a) *Fixed costs do not change as output changes e.g. Chris will be making a fixed repayment on his bank loan, this means it will be the same each month.*

b) *Variable costs will change directly with the output of the business e.g. Chris may will pay for items like weed killer, or lawn treatments or plants.*

**7** a) *Break-even* $= \frac{FC}{SP - VC}$

*Break even* $= \frac{4500}{20 - 5}$

*Break-even = 300 customers.*

b) *Margin of safety = Current output – break-even quantity = 750 customers – 300 customers*
*M.O.S = 450 customers*

**8** *Profit = TR – TC*

*(20 x 750) – (4500 + (5 x 750) ) = £6,750 profit*