1.3.1. Business Aims & Objectives

Aims- the strategic goals of a business; for example to grow and expand the business

Objectives - specific steps; for example to increase market share by 5% over the next year

Aims and objectives can help the business to:
- ❑ Set specific targets which can measure the performance of a business
- ❑ Objectives can be used to motivate staff
- ❑ Can be used to help decision making

Objectives for a Start Up Business
The objectives for a start up business can be split into financial (measured in monetary terms) and non-financial objectives. See table below:

Financial	Non-Financial
❑ Survival	❑ Social Objectives
❑ Profit	❑ Personal Satisfaction
❑ Sales	❑ Challenge
❑ Market Share	❑ Independence
❑ Financial Security	❑ Control

1.3 Putting A Business Idea Into Practice

Financial Objectives (Start up business)
- ❑ **Survival-** surviving the first year in order to build a customer base. This may mean low profits
- ❑ **Profit-** Maximise profit by increasing revenues and decreasing costs
- ❑ **Sales-** increase sales to encourage customers to repeat buy.
- ❑ **Market Share** – increase market share, take business from competitors. Could be via heavy promotion.
- ❑ **Financial Security-** for the entrepreneur as they may have given up their job. This means they will have bills etc. to pay which means the business must make money.

Non- Financial Objectives (Start up business)
- ❑ **Social Objectives-** some businesses trade for social or environmental purposes. These are different to a charity as social enterprises run on trade whereas a charity runs on donations.
- ❑ **Personal Satisfaction**- a business owner may simply have wanted to gain personal satisfaction from owning their own business
- ❑ **Challenge-** Entrepreneurs may start a business and view it as a challenge
- ❑ **Independence-** An entrepreneur may want complete freedom and may not want to work for someone else
- ❑ **Control -** Entrepreneurs may want more control over their own working lives. Owning a business gives flexibility in terms of; days off, holidays, working hours etc. They also get control over products and promotions for the business.

Why Aims And Objectives Differ Between Businesses.

Private Sector Businesses
Businesses which are not run by the government are the private sector
Their objectives are likely to be:
- ❑ Maximise profits by increasing sales and reducing costs
- ❑ Increase market share
- ❑ Expand the business

Public Sector businesses
These are businesses run by the government like state schools, the NHS, BBC, Police etc.
Their objectives are to be:
- ❑ Meet targets
- ❑ Keep costs low

Non-profit / Voluntary Sector
These are businesses which are classed as charities and social enterprises.
They may have objectives such as:
- ❑ Increase revenue from donations
- ❑ Reduce costs
- ❑ Help those in need

1.3.2 Business Revenues, Costs And Profits

Sales Revenue

This is the money which is coming into the business through sales of products and services. E.g. a bakery's revenue will be made up of the foods that have been sold. The formula for revenue is:

Revenue = Price x Quantity Sold

Fixed Costs

These are the costs which will not change, these are costs which need to be paid even if a business makes 0 sales. E.g.:

- ❑ Rent
- ❑ Insurance
- ❑ Advertising costs

Variable Costs

These are costs which can change depending on the output of a business. E.g. A bakery may need more flour if they are making more cakes. Some examples of variable costs include:

- ❑ Raw Materials
- ❑ Distribution Costs
- ❑ Temporary Staff

Total Costs

The total costs for a business are the sum of all the fixed costs and variable costs.

Total Costs = Fixed Costs + Variable Costs

1.3 Putting A Business Idea Into Practice

Profit

Profit plays a major role in most businesses, it is the money left over once all bills and expenses have been paid. The owner can decide how to use the profits e.g. putting more money back into the business, or alternatively they can spend on advertisement.

Below are the formulas for gross and net profit.

Gross profit = revenue – cost of goods sold

Net profit = Gross profit – expenses

Interest

If a business needs to money it is most likely that they will opt for a loan from a bank.

However when paying the loan back to the bank they will charge interest which is a percentage on top. This is the cost of borrowing.

Below is the formula to calculate the interest percentage

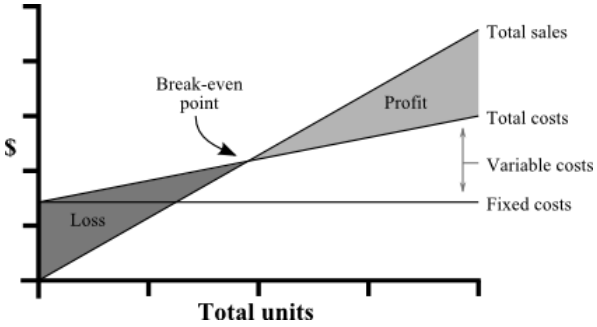
$$\text{Interest \%} = \frac{\text{Total Repayment – Borrowed amount}}{\text{Borrowed amount}} \times 100$$

Break-Even

When a new business starts up there will be large costs and little revenue. The business will need to calculate their break-even, ***this is the point at which the business makes neither a profit or a loss. (where total costs = total revenue)***

The formula to calculate break-even is:

$$\text{Break-Even} = \frac{\text{Fixed Costs}}{\text{Selling Price – Variable Costs (Per Unit)}}$$



Margin of Safety (MoS)

The difference between the actual level of output and the breakeven output.

The formula is:

MoS = Actual sales – break-even sales

The Margin of Safety

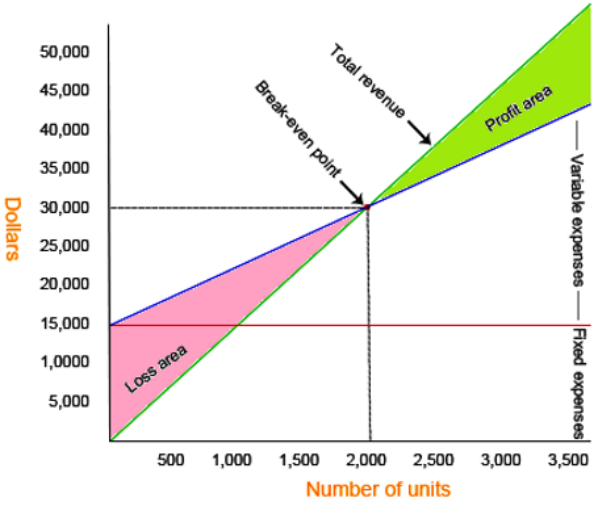
If we assume that Racing Bicycle Company has actual sales of $250,000, given that we have already determined the break-even sales to be $200,000, the margin of safety is $50,000 as shown.

	Break-even sales 400 units	Actual sales 500 units
Sales	$ 200,000	$ 250,000
Less: variable expenses	120,000	150,000
Contribution margin	80,000	100,000
Less: fixed expenses	80,000	80,000
Net operating income	$ -	$ 20,000

Interpretation Of Break-Even Diagrams

The break-even diagram is a graphical representation of costs and revenue.

The point at which neither profit nor loss is made is known as the "break-even point" and is represented on the chart below by the intersection of the two lines:



As you can see from the diagram above the break-even point for this particular business will be once 2,000 units have been sold.

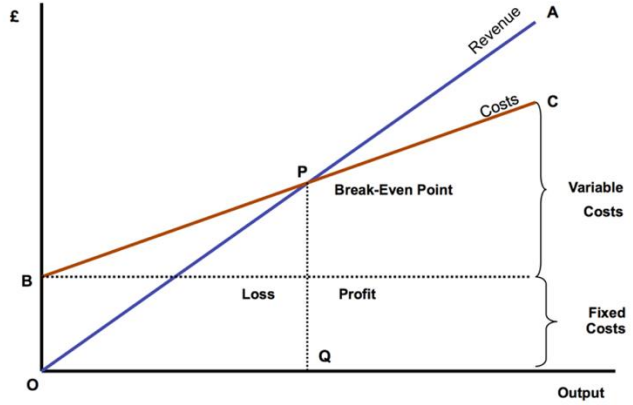
This is the point at which total costs = the total revenue.

1.3 Putting A Business Idea Into Practice

Drawing Break Even Diagrams

To draw a chart the following steps need to be followed:

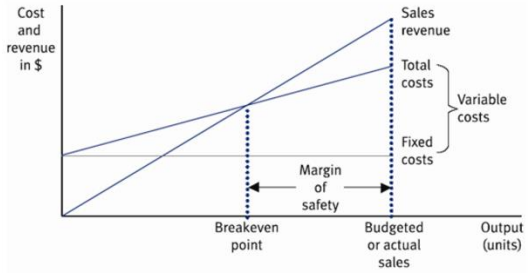
1. Label the vertical axis ”Costs in pounds”, label the horizontal axis " Units Sold".
2. Decide upon the scales you are to use on your chart.
3. Plot two points from the data for the sales revenue line and then draw a straight line for sales revenue
4. Draw a horizontal line for total fixed costs starting at the point on the vertical axis at the level of costs.
5. At the same starting point it is possible to draw the total costs line. Total costs are fixed costs plus variable costs. Draw the straight line starting at the same point as the fixed costs started.
6. Where the sales revenue crosses the total costs line is the break-even point. Read off the units of sales to give the break even level of sales.
7. The gap between the total costs line and sales revenue line after the breakeven point represents the level of profit.



Margin of Safety on the Break-Even Diagram

As stated previously the margin of safety is the difference between the actual level of output and the breakeven output.

This is shown below on the break even diagram:



Why The Margin Of Safety Is Important

The margin of safety formula is calculated by subtracting the break-even sales from the actual sales.

This formula shows the total number of sales above the breakeven point.

In other words, the total number of sales that can be lost before the company loses money.

1.3.3 Cash And Cash-Flow

Cash-money available in the business to pay the bills, cash may not come in the same month as it goes out

Profit- total revenue minus total costs, the money that is left once all bills have been paid.

The Importance Of Cash To A Business

Cash is very important to a business for the following reasons:

- **Paying Overheads-** These are the costs of a business that do not contribute to the production or performing of a service e.g.:
  - Administration Costs
  - Accounting Costs
  - Bills (Gas, Electric Water etc.)
  - Advertising Costs
- **Paying Suppliers-** suppliers are the companies which provide a business with stock or other materials e.g. wood for a furniture company. If the suppliers are not paid on time its most likely they will not supply you in the future.
- **Paying Employees-** If a business doesn't pay its staff they will leave the company and possibly take legal action. Also costs will be increased to recruit new staff.
- **Prevent Business Failure (Insolvency) -** Insolvency is the state of being unable to pay the money owed, by a person or company. Businesses need to make sure that its invoices are paid on time so they have cash to pay suppliers. If they run out of cash they will become insolvent.

1.3 Putting A Business Idea Into Practice

Calculation & Interpretation Of Cash-flow Forecasts

Cash Flow Forecast- A Cash flow forecast predicts the net cash flows of the business over a future period. The forecast estimates what the cash inflows into the bank account and outflows out of the bank account will be. Negative numbers are represented in brackets.

Cash Flow – This is the money which flows in and out of the business. Some examples for a Festival are shown below:

Inflows	Outflows
❑ Sales from tickets	❑ Cost to book performers
❑ Sales from stalls	❑ Cost to hire site
❑ Sales from parking	❑ Cost of security
	❑ Cost of administration
	❑ Cost of accountants

Uses Of A Cash Flow Forecast

- Allows the business to budget for the future
- Shows where businesses may have a shortfall(not enough money)
- All business to organise cash borrowing in case of a shortfall

Opening and Closing Balances

The opening and closing balance is shown on a cash flow forecast.

- **Opening Balance**– cash which is available at the start of the month
- **Closing** - cash which is available at the end of the month (this will be the next months opening balance)

Minimising a shortfall

- Cut costs
- Arrange an overdraft
- Do not give credit to customers
- Promotions
- Cheaper suppliers
- Apply for credit with suppliers

Example Cash flow Statement

	August (£)	September (£)
Receipts	17 400	21 770
Raw materials	8 050	9 340
Fixed costs	2 120	2 340
Total payments	10 170	11680
Net cash flow	7230	10 090
Opening balance	5 300	12 530
Closing balance	12 530	22 620

- Receipts are the total sales for the month
- Total payments is all of your costs (fixed and raw materials in this case)
- Net cash flow is the total sales (receipts) minus the total costs
- Opening balance is your balance at the start of the month
- Closing balance is your opening balance plus your net cash flow

1.3 Putting A Business Idea Into Practice

Revision Questions

These questions are based around the previous slides. Test your knowledge to see if you can answer them!

1. What is the definition of an aim and objective?[2]
2. What are some of the financial objectives for a start up business?[4]
3. What are some of the non financial objectives for a start up business?[4]
4. What would be some of the aims and objectives for a business in the private sector?[3]
5. What would be some of the aims and objectives for a business in the public sector?[3]
6. What would be some of the aims and objectives for a business in the non-profit / voluntary sector?[2]
7. What is meant by a fixed cost give an example[2]
8. What is meant by a variable cost give an example [2]
9. What is meant by the margin of safety?[1]
10. What is meant when a company breaks even?[1]
11. Why is cash important to a business? [4]
12. What is the purpose of a cash flow forecast?[1]
13. What is meant by the opening and closing balances on a cash flow forecast?[2]
14. How can a business minimise its shortfalls on its forecast?[4]

15. What is the formula to calculate revenue?[1]
    - ❑ Revenue = Price x Quantity Sold
    - ❑ Revenue = Price x Total Costs
    - ❑ Revenue = Price – Total Costs

16. What is the formula to calculate Gross Profit?[1]
    - ❑ Gross Profit =Revenue – Cost Of Goods Sold
    - ❑ Gross Profit =Net Profit – Cost Of Goods Sold
    - ❑ Gross Profit =Revenue – Margin of Safety

17. What is the formula to calculate Net Profit?[1]
    - ❑ Net Profit = Gross Profit – Expenses
    - ❑ Net Profit = Gross Profit – Total Costs
    - ❑ Net Profit = Gross Profit – Revenue

18. What is the formula to calculate Total Costs?[1]
    - ❑ Total Costs = Fixed Costs * Variable Costs
    - ❑ Total Costs = Fixed Costs + Variable Costs
    - ❑ Total Costs = Fixed Costs - Variable Costs

19. The formula for interest is: [1]

$$\text{Interest \%} = \frac{\text{? – Borrowed amount}}{\text{Borrowed amount}} \times 100$$

    - ❑ Total Cost
    - ❑ Profit
    - ❑ Total Repayment

20. What is the formula to Break Even?[1]
    - ❑ Break Even = Fixed Costs / Selling Price – Variable Costs Per unit
    - ❑ Break Even = Total Costs / Selling Price
    - ❑ Break Even = Fixed Costs / Selling Price * Variable Costs

Tips

For an essay style question use the following tips to ensure that you are maximizing your marks:

- ❑ Read through the question underlining any key points
- ❑ For these types of questions an extended answer is expected.
- ❑ Discuss both the advantages and disadvantages of the given context if needed
- ❑ When discussing a point ensure that you contextualise your answer. This means give examples which relate to the scenario

21. Liat is currently trying to work out her break even point using the following data:
    - ❑ Fixed Costs = £550
    - ❑ Variable Costs Per Unit = £2.50
    - ❑ Selling Price(Per unit) = £4.50

    According to her figures she should break even after selling 300 units, Create a break even graph and explain whether Liats calculation is correct. [10]