

BUSINESS FEASIBILITY - MONEY

Develop Your Sales Forecast

In evaluating how much of the market you can get, concentrate on why customers will buy from you and not your competition. You must offer the customer a good reason to switch to your business.

Data on selected industry sales is included in "Sales and Marketing Management's Survey of Buying Power" (in Reference List at the end of this document). Information is given by state, county, and metropolitan areas. This publication is updated annually.

Consult the Census of Retail Trade, Census of Wholesale Trade, Census of Manufacturing, and Census of Service Industries (www.census.gov) for industry data on sales receipts and value of shipments. This data is presented on a statewide and, sometimes, county-wide basis.

An excellent predictor of sales volume for a storefront operation can be obtained from Dollars and Cents of Shopping Centers (See Reference List). Another great source is www.bizstats.com. Both references provide data on median sales per square foot and median size of location. Multiply the sales figure by your potential location's square footage to arrive at an estimated annual sales volume. You should also compare your potential location's size to the median to determine if your site's size is in line with the industry. This data is very useful even if your location is not in a shopping center. Remember: During the first year of business, it is unlikely that you will reach average sales levels, so be conservative.

Another valuable source of information on what level of business to expect is other business owners and owners of similar businesses that failed. Don't expect competitors to share this data with you. Owners of similar businesses outside your market area may, however, since you will not be in competition with them. Contact business owners in similar-size markets outside your area. You may be able to obtain valuable information and advice, based on their experiences.

Answer the following questions about your possible sales volume.

What price(s) will I charge for my products/services? Why?

How many "units" of my products/services will I sell each month? Will monthly sales be fairly even or fluctuate because of seasonal factors?

What will my total sales revenue be for the first year? (Total units multiplied by your selling price).

What are the total sales for my type of product/service in the industry or market area (whichever applies)?

Of the estimated total sales in my industry or market area, what amount can I expect to get for my business?

Why will customers buy from me and not from my competitors? Will customers know or care that I'm offering something with a difference?

What will my competition do in response?

Does my estimate of sales seem reasonable based on the sales volumes of my competitors?

When will my sales increase and slow down, and why? What steps can I take to minimize the peaks and valleys that occur during my sales year?

Identify Your Start-up Expenses

You will incur many costs to open your business. Some of these expenses will be of a continuing nature, such as rent, utilities, and insurance; others will be non-recurring (one-time) expenses, such as equipment purchases, security deposits, and the like. Create a VERY DETAILED, itemized list of startup costs.

These start-up costs must be identified as you analyze your business idea's feasibility. Only by knowing the total costs to get your business to an operating stage can you decide whether you have enough personal financial capacity to approach lenders about debt financing for the remainder of the money that you need.

Besides specific expenses that must be paid, you also need operating cash to support the business until it begins to generate enough cash to meet continuing costs. The amount of operating cash you need depends on the amount of your recurring monthly expenses and the number of months it takes for the business to generate a positive cash flow (that is, cash received exceeds cash paid out).

The amount of time required to begin generating a positive cash flow varies due to many factors. The type of business influences the length of the cash cycle, as do the payment terms you offer to customers and suppliers offer to you. Remember, in a start-up environment, it takes time for customers to find out about your business, decide to give you the opportunity to sell to them, and finally make a purchase.

Your past experience can affect the amount of time needed to generate a positive cash flow. For example, if you have operated a business for someone else and plan to open a competing business, you may have loyal customers who will follow you.

It is wise to be conservative when projecting the operating cash you will need during the start-up phase of your business enterprise. In other words, have more cash than you think you will need. One of the worst things for any new business is to have only enough cash to operate for one or two months. Rarely can a new business begin to support itself so quickly. If your business will be somewhat seasonal, opening during the "slow season" will require more operating cash than if you opened during the busy season.

Since the amount of operating cash required depends on your projected sales and expenses, you should not attempt to estimate a dollar figure now. After you have projected your sales and expenses for the first twelve months of operation, you can estimate an amount. You probably

will want to have cash to cover at least four months of total expenses (cost of goods sold + total operating expenses) or more, if expenses will be high and sales low during initial months of operation.

The following worksheet identifies common start-up costs. Use this form to develop an estimate of the amount of money you will need to get started. Omit or add items to suit your business. Check with trade associations and franchisors for industry data on start-up costs for your potential business. You may also want to ask other business owners outside your market area for guidance.

ESTIMATED START-UP COSTS

Balance Sheet Items:

Land \$

Building

Furniture & Fixtures

Counters, display stands, shelves, tables

Window display fixtures

Storage shelves and cabinets

Outside sign

Autos

Machinery & Equipment

Cash register

Computer

Tools

Machines

Other (specify)

Starting Inventory, Merchandise

Starting Inventory, Raw Materials

Starting Inventory, Supplies

Decorating & Remodeling

Installation of Fixtures and Equipment

Deposits (utilities, lease, etc.)

SUBTOTAL \$

Profit & Loss Statement Items:

Licenses and Permits

Legal and Accounting Fees

Other Professional Fees

Advertising for Opening, etc.

Promotions (door prizes, etc.)

Printing

Other (specify)

SUBTOTAL \$

TOTAL START-UP COSTS \$

Estimate Your 12-Month Operating Budget

The operating budgets for your business are summaries of the business's projected sales and expenses, cash flow, and balance sheet. They are the road maps by which you project and chart the business's future, compare actual performance to your expectations, and adjust the business's operations as needed to stay on course.

Be conservative and realistic as you develop your operating budgets. It is much better to outperform your projections than to try to explain why you didn't meet them, especially if you must explain that to your banker.

Some types of businesses may not achieve a profit in the first year. Extend your profit or loss projection up to the point where your projected figures show an annual profit. For example, a fish farm takes as much as nine months to grow its first "crop" of fish for market. Production costs have been incurred all that time, so expenses may exceed total sales in the first year. If they do, the result is a net loss for the year.

The projected profit or loss statement should include all the normal costs associated with the day-to-day operation of your business. Some of these expenses are "fixed" that is, they continue whether or not the business has sales (rent, utilities, office salaries, insurance). Others are "variable" and are controllable and, sometimes, directly dependent on the business's sales volume (inventory, materials, production worker salaries). Be sure to plan for miscellaneous expenses - all the things you have not thought of or anticipated.

It is important that you obtain reliable estimates wherever possible. For example, public utility companies can give you estimates on monthly bills for your proposed location. Your insurance agent can give you advice on the types of coverage you need and estimated costs for that coverage.

Once you have completed the projections, study them for any changes you may want to make. For example, if your profit margin is below industry standard, can you increase your price? You might consider operating out of your home. Do you need to decrease your salary?

Use worksheets to project the expected sales and expenses of your business in its first year of operation. Detailed worksheets are provided for estimating sales, cost of goods sold, labor-related expenses, and operating expenses. Transfer these amounts to the Profit or Loss Statement, then complete it. The expense categories shown are those typical for most businesses; add any other expenses that you know will apply to your business, but are not shown.

Once you have estimated sales and expenses using the worksheets, return to this document to continue with your evaluation of the issues related to money as they affect the feasibility of your potential business.

Financial Ratios Worksheet

It is important to compare the projected performance of a proposed business to the "industry averages" for that type of business. This comparison will confirm whether the projected financial performance is expected to be in line with, better than, or worse than industry norms.

The results of the comparison can be very useful. If, for example, your projected figures are comparable to industry norms, you would appear to have realistic expectations about your projected earnings. If your figures are at wide variance, you will need to account for the difference(s) by re-evaluating your estimates or by showing why your business will perform differently from others in the industry.

There are several sources of industry data, but a commonly available one is Annual Statement Studies, published by Risk Management Association. This book is available at the SBDC as well as many public and university libraries.

Use the following worksheet to compare the projections you have developed to industry standards.

Industry ratios obtained from:			
SIC Code for my business is:			
	Column 1 (My \$\$)	Column 2 (My %)	Column 3 (Industry %)
Net Sales 100.0 100.0			
Gross Profit			
Operating Expenses			
Operating Profit			
All Other Expenses			
Profit Before Taxes			

Column 1 = My projected business income and expense data

Column 2 = Data converted into "Percent of Net Sales"; divide each item by Net Sales and multiply by 100

Column 3 = Industry average percentages for my type of business

Reference List

These sources will provide answers to your research needs:

1. Survey of Buying Power. Arlington, VA: CACI Marketing Systems.

This resource uses census data combined with marketing data to produce effective buying income; total retail sales to market data; and projections for population, effective buying income and retail sales. Organized by state, county, and MSA.

2. Census of Retail Trade. Washington, DC: U.S. Department of Commerce.
Census of Wholesale Trade. Washington, DC: U.S. Department of Commerce.
Census of Manufacturing. Washington, DC: U.S. Department of Commerce.
Census of Service Industries. Washington, DC: U. S. Department of Commerce.
Use this data to locate potential markets and to analyze your own production and sales performance relative to industry or area averages. It gives data by specific industry including number of establishments, sales, and payroll.

3. Dollars & Cents of Shopping Centers. Washington, DC: Urban Land Institute (ULI).
Excellent source for data on sales per square foot and median size of storefront businesses.
Lists lease arrangement, average rental rates per square foot, and other costs to retail and service stores located in shopping centers. Information is sorted by type of store and type of shopping center.

4. George C. Michael. Sales Forecasting. Chicago, IL: American Marketing Association.
This book was written specifically for business decision makers who have need of forecasts yet are uncomfortable with the forecasting process.

5. Entrepreneur Magazine. Boulder, CO: Published monthly.
This periodical regularly highlights new businesses and gives start-up details. The Entrepreneur Magazine Group also publishes start-up guides for over 100 businesses.

6. (RMA) Annual Statement Studies. Philadelphia, PA: Risk Management Association (updated annually).

7. Industry Norms and Key Business Ratios, Murray Hill, New Jersey: Dun and Bradstreet Information Services (updated annually).

8. Almanac of Business and Industrial Financial Ratios. Englewood, NJ: Prentice Hall (updated annually).

9. Small Business Sourcebook. Detroit, MI: Gale Research Incorporated, 1994.
This handbook lists information sources for over 200 businesses including associations, services, and assistance available.

10. Encyclopedia of Business Information Sources. Detroit, MI: Gale Research Incorporated.
This is an extensive bibliography with topics arranged alphabetically.

11. U.S. Industrial Outlook. Washington, D.C: U.S. Department of Commerce.
Industry reviews, analyses, and forecasts for 350 industries.

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