# Essentials of Finance for Entrepreneurs

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*Hussain Moosajee*

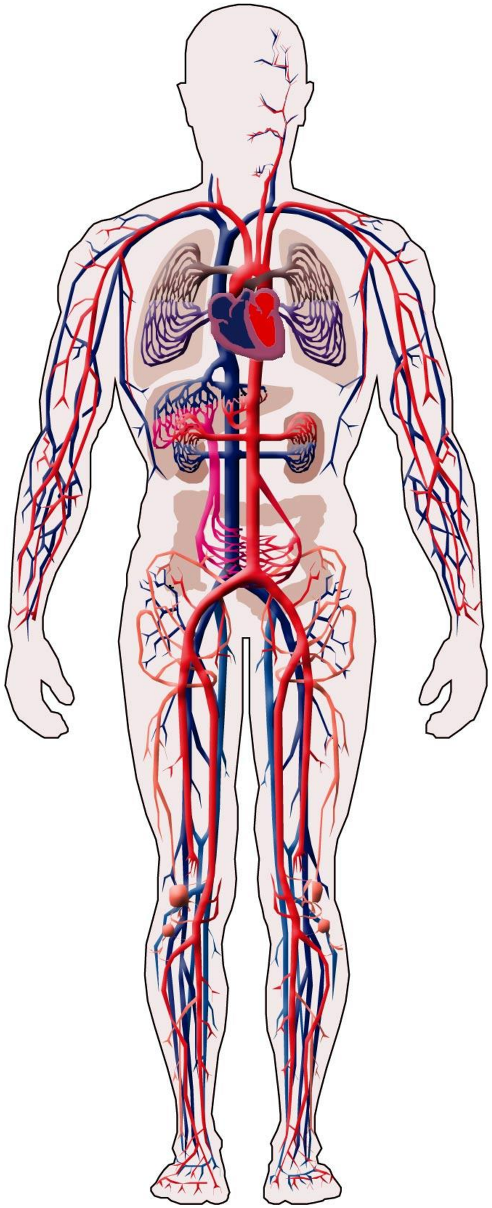
Experience the difference

**Confused**
**???**

- Ask questions
- Clarify doubts

# Our **Focus** for today ……..

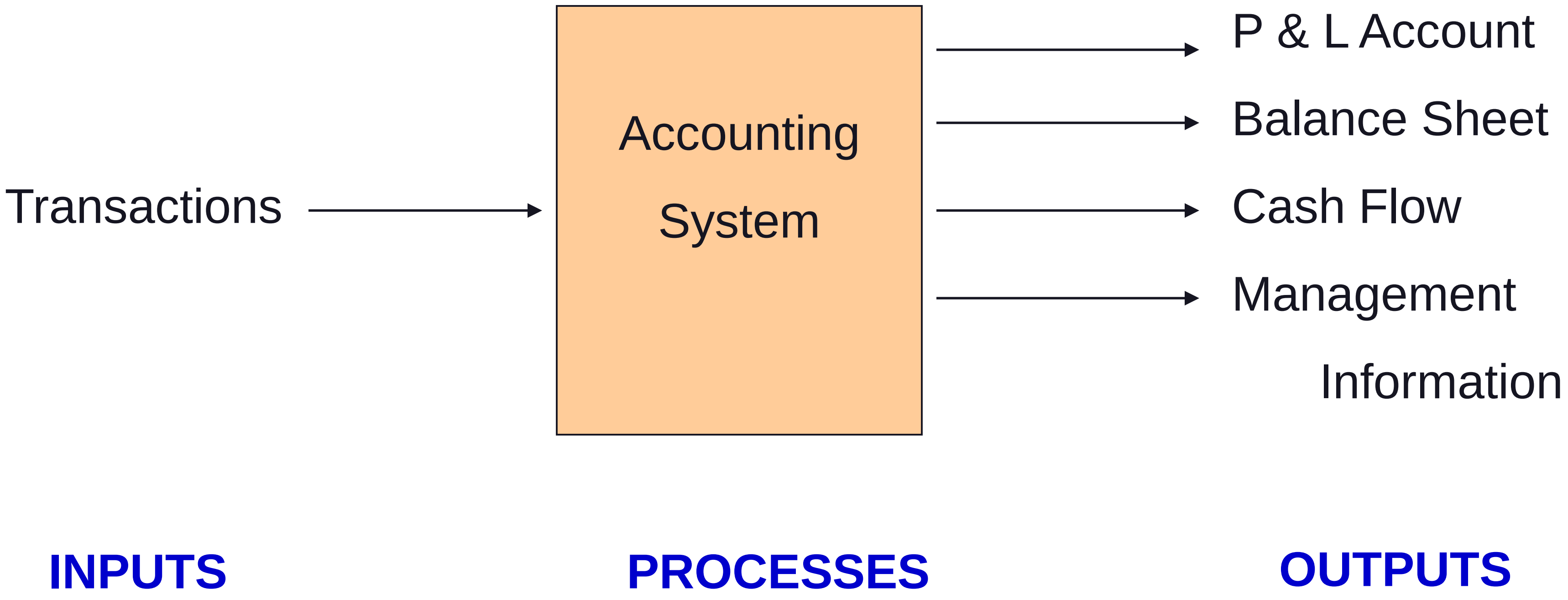
- Overview of Accounting Terminologies used
- Distinction of Cash vs. Profit
- Structure of Financial statements
  - Profit & Loss Account
  - Balance Sheet – what it means
  - Cashflow statement
- Projections
- Governance procedures
- Burn rate
- Basics of valuations in general



- Why would you think **Finance** is important to understand your business

# Accounting system

## a basis for providing information



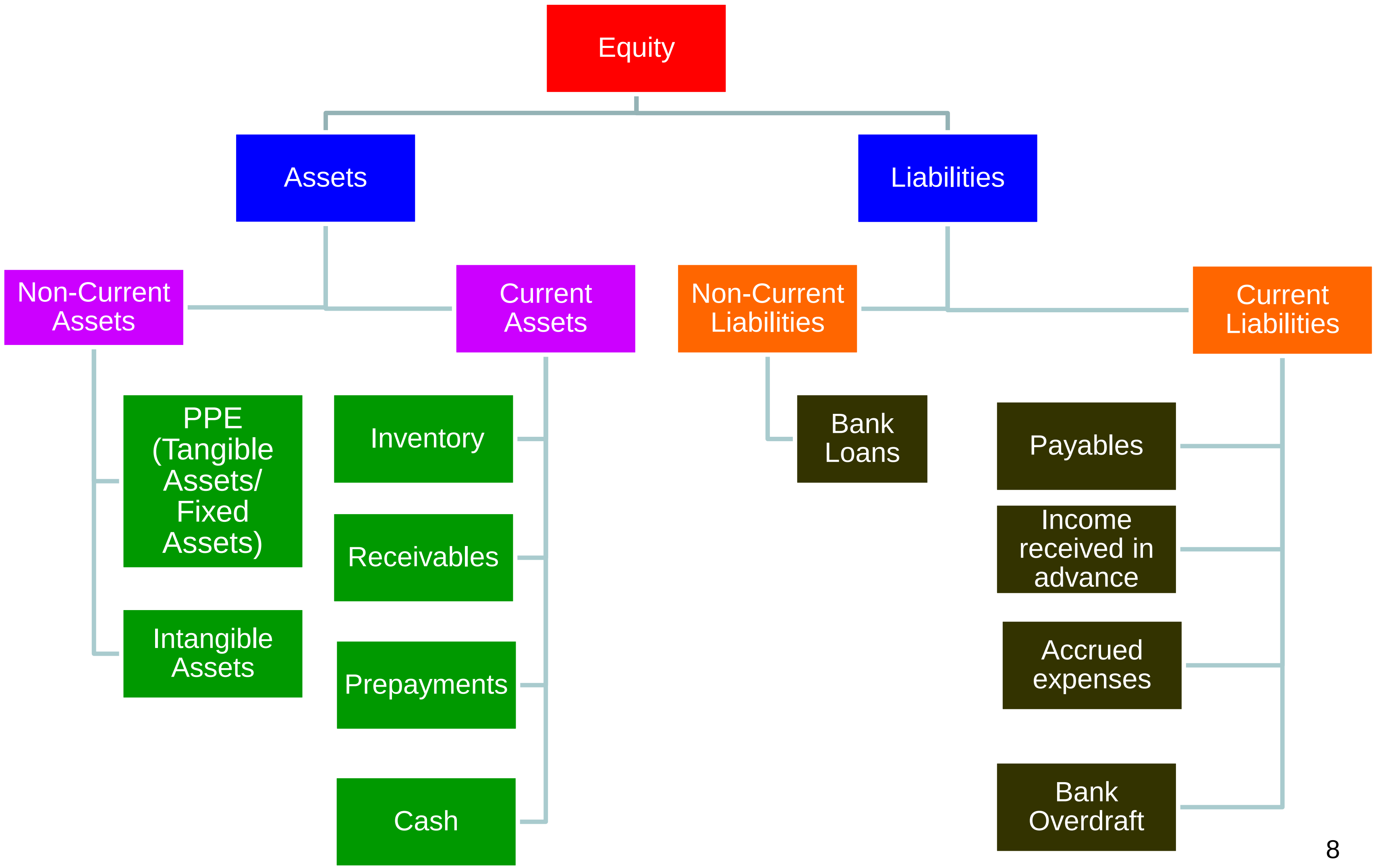
# Some basics required to ensure the right input

- **Business transactions separate from the Owners' Personal transactions**
- **Systems and Procedures**
- **Cash generation**
- **Entrepreneurial spirit**
  - **Know what you want to do?**
  - **Direction**
  - **Focus on market opportunities**
  - **High growth orientation**
- **HUNGER FOR GROWTH**

# Key Accounting Terms

- **Assets**
  - **Fixed Assets**
  - **Current Assets**
- **Liabilities**
  - **Non Current Liabilities**
  - **Current Liabilities**
- **Capital**
- **Revenue/Income/Turnover**
- **Expenses**
- **Capital Expenditure**
- **Revenue Expenditure**

# Relationship of Balance Sheet accounts



- When is Income recognized?
  - When a customer order is received
  - When goods are manufactured
  - When goods are delivered , a SALE is effected
  - When cash is received from the customer
  - Note: Income has to be **earned**

- When is an Expense recognized
  - When the benefit of a service is obtained
  - Not necessary when cash is paid
  - Note: The expense is **incurred**

- **Assets -** anything of Value owned or controlled by a business, which can be further classified into Fixed Assets and Current Assets.
- **Non Current Assets (Fixed Assets)**

Assets acquired with the long term intention of use in the business

•Tangible Assets – those that have tangibility i.e. can touch, see and feel eg: Machinery & Equipment, Vehicles etc. (commonly called Fixed Assets)

•Intangible Assets – those of value, but have no physical existence no physical existence eg: Goodwill, Patents, Software etc.

- **Current Assets**

Assets held for conversion into cash in the normal course of business Eg: Stocks, Receivables (Debtors)

- **Liabilities**

  The financial obligations of a business, which can be of a short term or long term nature.

- **Current Liabilities**

  liabilities which fall due for payment, in a relatively short period, normally less than 1 year Eg: Payables (Trade Creditors)

- **Non-Current Liabilities (Long-term)**

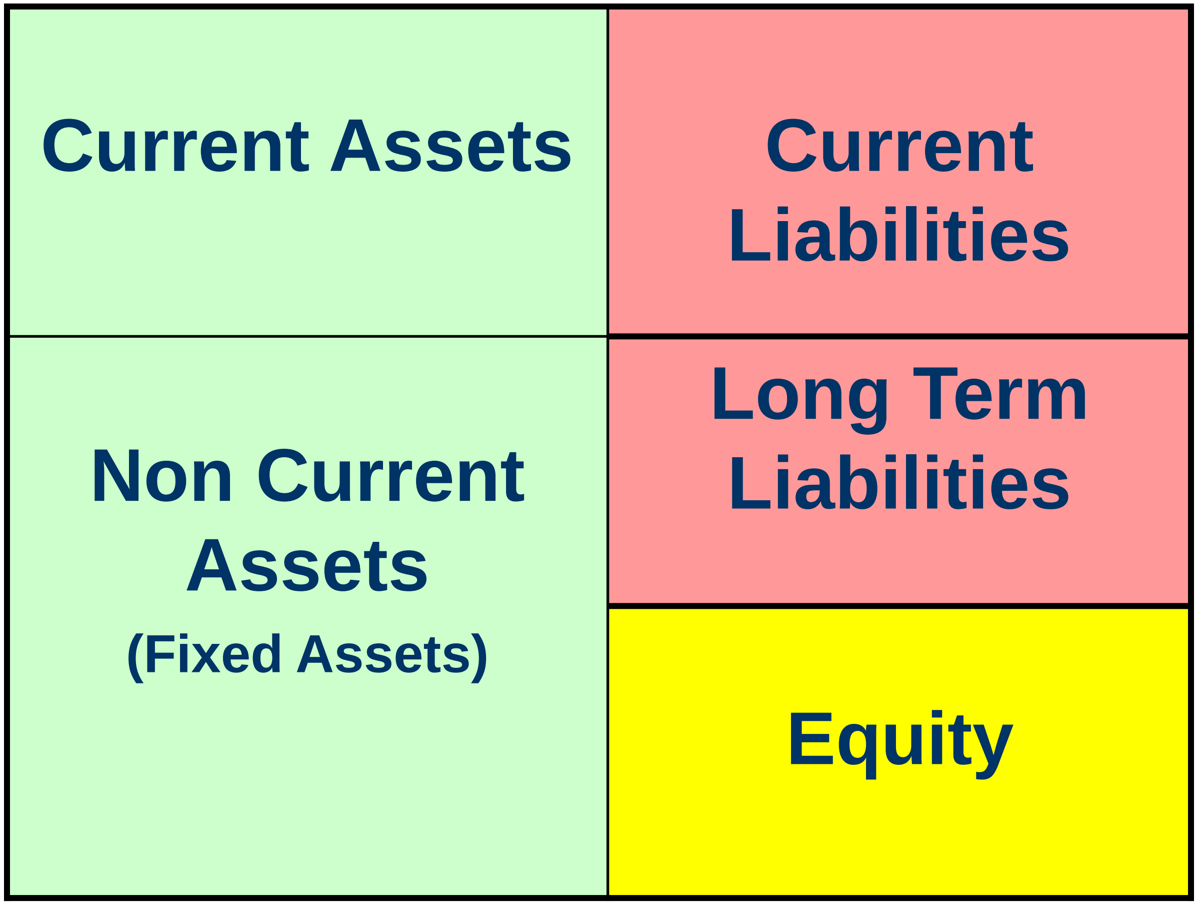
  liabilities which fall due for payment, over a relatively longer period, normally more than 1 year, Eg: Long Term Bank Loans

- **Capital**

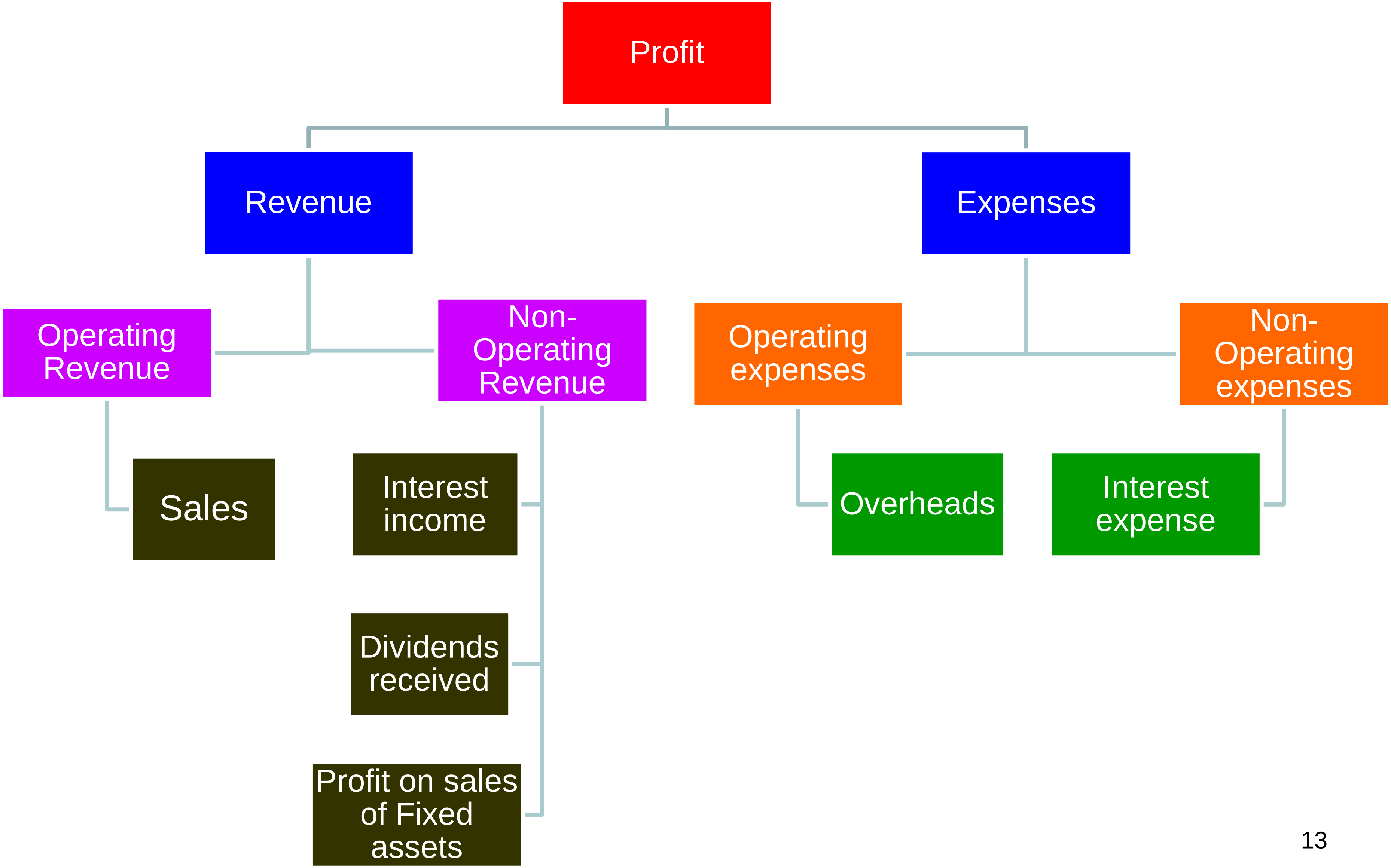
  Cash, or other Assets contributed by an individual or group of individuals as an investment into the business.

**Capital + Retained Profits = Equity**

# Structure of Balance Sheet



# Relationship of Income & Expenditure accounts



## Revenue (Income)

Amounts already earned (either received or which is due), as a result of the exchange of goods or services

Eg: Sale of goods, Income earned from Services offered

- Revenue earned and cash received is <u>Cash sales</u>
- Revenue earned but cash not received is <u>Debtors</u>
- Cash received and Revenue not earned is <u>Receipts in advance</u>

## Expenses

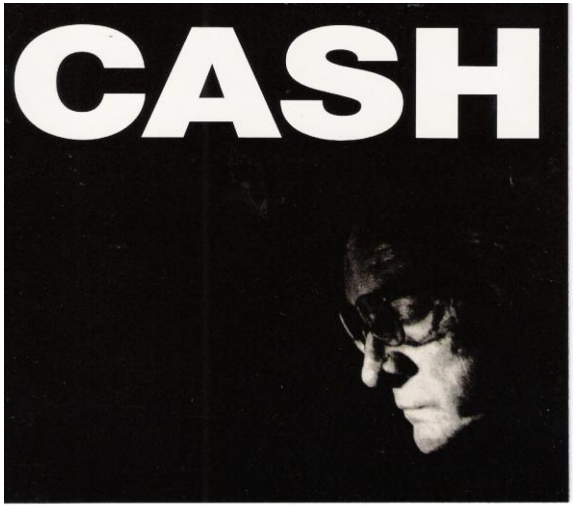
Payment made or due to be made, for a benefit or service which has been availed of <u>eg:</u> Rent, Salaries, Electricity

- Expenses incurred and paid for is <u>Cash paid</u>
- Expenses incurred and not paid for is <u>Accrued expenses</u>
- Expenses paid and not incurred is <u>Prepaid expenses</u>

# GENERAL STRUCTURE

## Financial Statements

## Template used for monthly information

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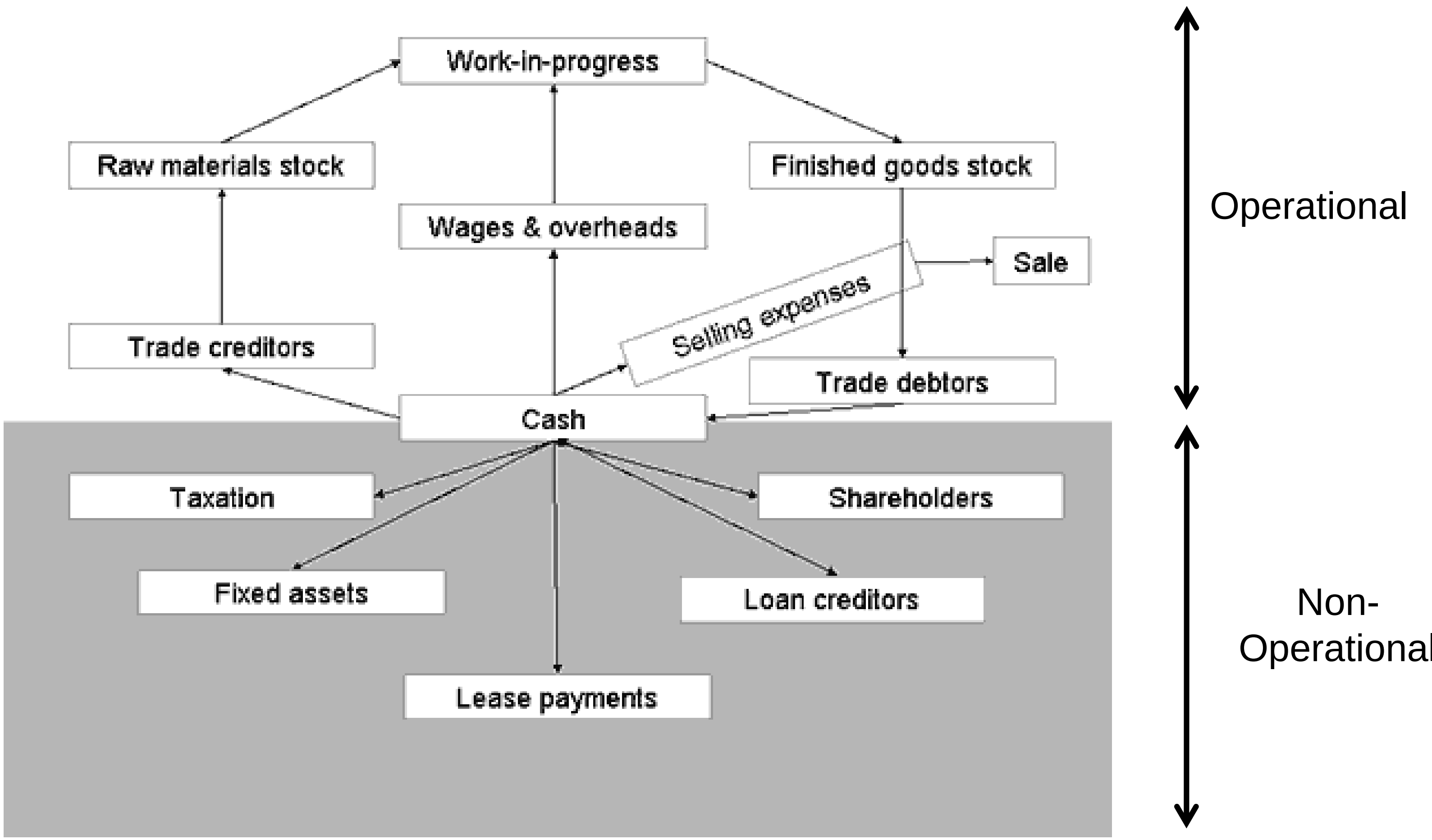
CASH before you Crash!

# Simple Cash flow

| Cash flow statement | figures in Rs. 000's | | |
|---|---|---|---|
| | **July** | **Aug** | **Sept.** |
| **Cash inflows/Receipts** | | | |
| Cash sales | 220 | 150 | 170 |
| Collections from Debtors | 320 | 280 | 230 |
| | | | |
| Equity Capital | 1,700 | | |
| | **2,240** | **430** | **400** |
| | | | |
| **Cash Outflows/Payments** | | | |
| Raw materials | | | |
| - Payments to Suppliers | 170 | 140 | 150 |
| Rent | 50 | 50 | 50 |
| Wages | 90 | 80 | 80 |
| Electricity | 45 | 60 | 60 |
| Staff salaries | 120 | 150 | 140 |
| Other Administrative expenses | 75 | 80 | 70 |
| Selling & Distribution expenses | 25 | 30 | 30 |
| Capital expenditure payments | 1,500 | | |
| | **2,075** | **590** | **580** |
| | | | |
| **Net Cash flow** | **165** | **(160)** | **(180)** |
| Balance b/f | 100 | 265 | 105 |
| **Balance c/f** | **265** | **105** | **(75)** |

# The Business Cycle



# Projected Financial statements

- Income statement
- Cash flow

# Forecasting methods

- Incremental forecasts

- Objective method of estimating demand
  - Sales
  - Expenses
    - Raw materials
    - Overhead and other expenses

# BEST PRACTICES

Effective Governance procedures

# The Burn Rate

The rate at which a company spends cash to cover overhead costs without generating a positive cash flow is called the **burn rate**.

Use the burn rate to calculate how long a company can go without revenue.

Cash on Hand ÷ Burn Rate = Number of Months before Cash Runs Out

# Burn rate - explained

- Speed at which your cash balance is going down

- If you had Rs.1 million in cash on January 1st, and now it is October 1st and you have Rs.250,000 left, your burn rate is Rs.750,000/-, or Rs.83,333/month.
  - Rs.750,000 is the amount of cash that has been spent (Rs.1million minus Rs.250,000)
  - and 9 is the number of months that have transpired (January through end September)

- Being October 1st and you have Rs.250,000 left and your burn rate is Rs.83,333/month. How many months of cash do you have left? The amount of cash you have left divided by your burn rate (250,000/83,333) and you get **three months**. Ie: at year end, you will be out of money.

A more sophisticated way to calculate the Burn rate.

1. Add up all your monthly expenses on the income statement.

2. Then add up any outlays of cash for capital expenditures or other regular uses of cash on the balance sheet and cash flow statement.

3. This is "gross burn rate".

4. Now look at the cash receipts from sales. Include all incoming cash you are certain you can count on every month. This is the 'build rate'.

   Subtract this from gross burn and you get "net burn rate".

5. This should be the amount of cash that your business is burning in any given month.

# Burn rate

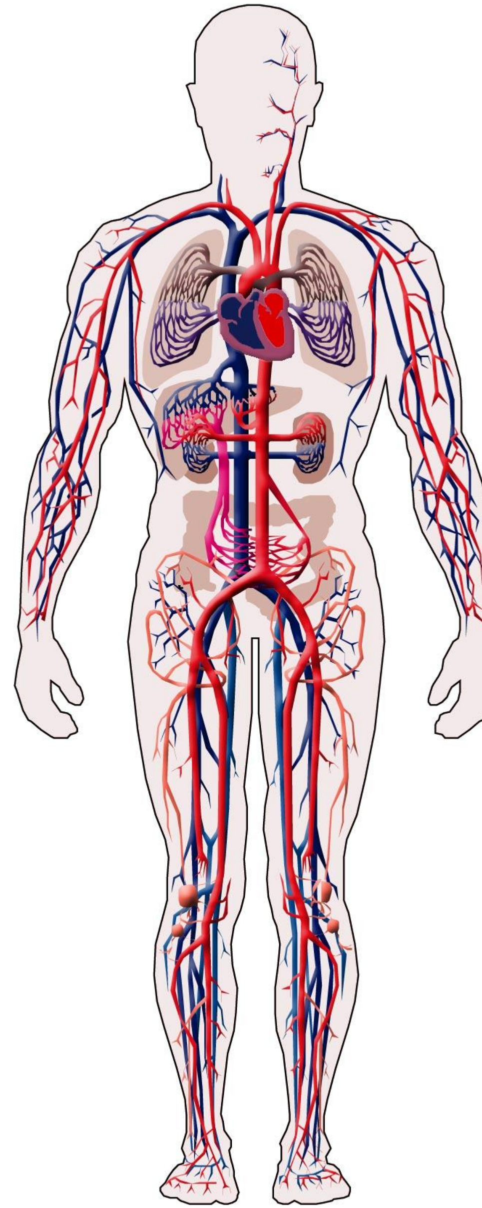
1. Find the amount of money lost (net cash) by subtracting the expenses from the total income, and a negative number indicates a loss.
   – Eg: Company A had Rs.200,000 in sales over six months, but its expenditures over the six months equaled Rs.320,000. The net cash: Rs.200,000 – Rs.320,000 = -Rs.120,000

2. Divide the total amount of money lost by the time period of measurement in months.
   – If company A netted Rs.120,000 loss over six months, its burn rate would be Rs.120,000/6 = Rs.20,000 per month.

3. Divide the amount of cash reserves the business has by the burn rate to find the number of months left before the company runs out of cash.
   – If company A only has Rs.100,000 in cash reserves: 100,000/20,000 = **five months** before the company is out of cash.

**Entrepreneur** **&** **Finance**


# Our Learning?


0777 727170

hussaintmoosajee@gmail.com

***Hussain Moosajee***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