How to Create a Startup Budget

By

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Learning Outcomes

- By the end of this session the students should be able to:
- Identify items that appear in a start-up budget
- Prepare a Start-up budget under fidderent scenarios
- Prepare a cashflow statement

Introduction

- Starting a new business is exciting
- Did you know that 90% of startups fail?
- But why do they fail?
- It’s not because they had a bad idea. It’s also not because they didn’t pick the right market or have enough passion for their product.
- The most common reason why startups fail is that they run out of money.
- Want to avoid becoming part of that 90%?

Introduction….contd

- **A startup budget is an estimate of how much it'll cost to start and run your business.**
- A startup budget is a crucial tool for managing your finances and ensuring long-term success.
- It helps you plan for initial expenses, set financial goals, and make informed decisions.
- The budget should include where the money will come from to continue to operate the startup.
- Note that budgets aren't 100% accurate.
- They combine historical data and assumptions to predict how much money your startup will need to spend each month.
- The budget *should* start to become more accurate over time.

Introduction….contd

- Before starting Understand Your Business Model:
- Define your business model: What are you selling, and to whom?
- Identify your revenue streams: How will you make money?
- Estimate your sales and pricing strategy: What are your sales projections?

Introduction….contd

- Determine your short-term and long-term financial objectives.
- Create specific, measurable, achievable, relevant, and time-bound (SMART) goals.

Example

Short-term goal: Achieve profitability within the first year.

Long-term goal: Expand the customer base and increase revenue by 20% annually.

Step-by-step guide on how to create and forecast a startup budget.

Illustration

- Chai Kahawa (CK) is planning to open a new coffee shop in a prime location in a busy city centre under the name @Bean Haven a leading global restaurant chain.
- The business will serve coffee, tea, and light snacks.
- What will be needed to start off the business?
- What expenses will be incurred on a monthly, yearly one-off basis?
- How can CK determine the revenues?

Illustration…contd

The following are Bean Haven's projected costs & Revenues.

1. ***Startup Costs($)***

- Restaurant Partitioning & Décor 30,000
- Equipment and furniture 20,000
- Licenses and permits 5,000
- Lease drafting cost 5,000
- Marketing and branding 3,000
- Legal and accounting fees 2,000

2. Revenue Projections($)

Average monthly sales 15,000

Monthly Fixed Costs ($)

Rent 4,000

Utilities 500

Insurance 300

Loan repayments 1,500

Monthly Variable Costs ($)

Employee wages 6,000

Cost of goods sold 3,000

Marketing & promotions 1,000

Step 1: Choose a Tool to Create Your Startup's Budget

- To start, choose a tool to create your budget.
- A lot of startups prefer to use a combination of spreadsheets and a dedicated accounting software tools.
- Spreadsheets are good for getting all your expenses down on "paper" and ideating.

Step 1: Choose a Tool to Create Your Startup's Budget

- List your essential startup costs.
- Startup costs are the expenses you incur and assets you buy before launching your company.
- These are the priority purchases — the resources you absolutely need to establish your business and start selling.
- There are two kinds of startup costs.

- **Startup assets**: These are one-time purchases of assets like inventory, computers, furniture, vehicles, property, and security deposits. office space, organizing fees, trademarks, and patents.
- **Startup expenses**: These are the fixed or variable expenses that you pay before opening. Rent and payroll, for example, are considered to be startup expenses before you launch. Startup expenses are tax deductible

Step 2: Make a List of Your One-Time Expenses

- Once you have identified the tool, the next step is to list your expenses.
- Start with your one-time expenses.
- These are non-recurring expenses like:
  - ✔ Computers
  - ✔ Office furniture
  - ✔ Licenses or fees
  - ✔ One-off consultations (e.g. consulting with a lawyer)
  - ✔ One-time marketing expenses (e.g. conference booth)

What other expenses would you consider in this category?

Step 2: Make a List of Your One-Time Expenses

	Bean Haven’s Start-Up Budget		
	Initial Costs$	Monthly Costs $	Monthly Revenue $
Startup Costs			
Leasehold improvements	30,000		
Equipment and furniture	20,000		
Licenses and permits	5,000		
Initial inventory	5,000		
Marketing and branding	3,000		
Legal and accounting fees	2,000		

Step 3: Make a List of Your Fixed Costs

Fixed Costs are expenses that stay relatively the same month-to-month.

This includes expenses like:

- ❑ Rent and utilities
- ❑ Payroll and benefits
- ❑ Website hosting
- ❑ Accounting software tools
- ❑ Subscriptions

- For instance, if you have an annual subscription to Cofffee Traders Assciation, that's a fixed expense. Then you'll spread the cost over 12 months in your budget. So if you pay 9,600 for an annual subscription, you'll enter that as 800/month over a 12-month period in your startup's budget.
- Since fixed costs are more predictable, they're easier to forecast. Unless there's a drastic change to your business, your fixed costs should stay pretty consistent.

Step 4: Make a List of Your Variable Costs

- Just as the name implies, these are expenses that “vary” month-to-month depending on other factors.

- In most cases these are costs that are linked to growth. The more your business grows, the higher your variable costs tend to be, which is one of the biggest differences between variable and fixed costs.

- Some examples of variable costs are:
  - ❑ Cost of Goods Sold (COGS)
  - ❑ Rent
  - ❑ Utilities (e.g. water and electricity)
  - ❑ Bank transaction fees

Step 4: Make a List of Your Variable Costs…contd

	Bean Haven's Start-Up Budget		
	Initial Costs$	Monthly Costs $	Monthly Revenue $
Startup Items			
Leasehold improvements	30,000		
Equipment and furniture	20,000		
Licenses and permits	5,000		
Initial inventory	5,000		
Marketing and branding	3,000		
Legal and accounting fees	2,000		
Monthly Fixed Costs			
Rent		4,000	
Utilities		500	
Insurance		300	
Loan repayments		1,500	

Step 4: Make a List of Your Variable Costs…contd

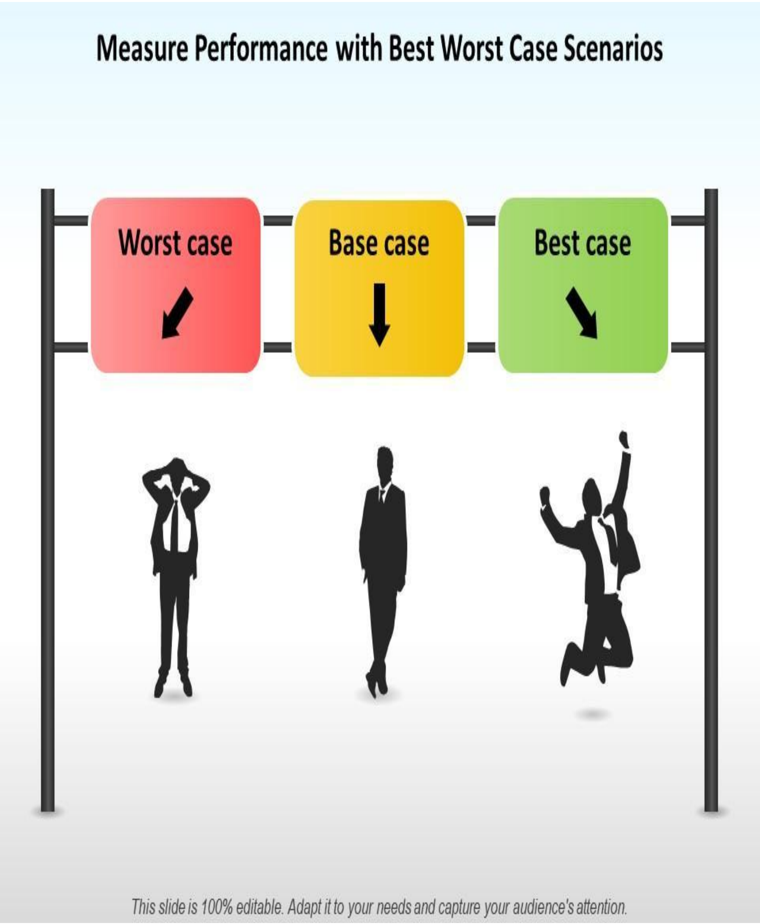
- Forecasting variable expenses for your startup budget is not easy.
- Accept that your budget forecast will not be 100% accurate.
- From our Illustration CK cannot know exactly how many customers will visit the restaurant in the next 12 months this it’s impossible to accurately forecast this budget.
- However, she must collect data and justify her assumptions about the expected sales.
- A look at her historical data can tell if the customer-base grew 10-15% per month over the past 6 months, you can use those numbers to estimate how much she will spend on coffee and cakes for the next couple of months.

Step 4: Make a List of Your Variable Costs…contd

	Bean Haven's Start-Up Budget		
	Initial Costs$	Monthly Costs $	Monthly Revenue $
Startup Costs			
Leasehold improvements	30,000		
Equipment and furniture	20,000		
Licenses and permits	5,000		
Initial inventory	5,000		
Marketing and branding	3,000		
Legal and accounting fees	2,000		
Monthly Fixed Costs			
Rent		4,000	
Utilities		500	
Insurance		300	
Loan repayments		1,500	
Monthly Variable Costs			
Employee wages		6,000	
Cost of goods sold		3,000	
Marketing and promotions		1,000	

Step 5: Forecast Your Revenue

- Where will the money come from?
- You will need to conduct a revenue forecast
- The most important thing to keep in mind here is that you need to account for your at least more than 1 scenario such as the best, normal and worst-case scenarios for how much revenue you'll generate throughout the year.
- Many startups make the mistake of building their budget based on overly-optimistic revenue forecasts. The worst-case scenario helps you to plan for contingencies.



Step 5: Forecast Your Revenue

- The base scenario assumes average growth; best-case scenario assumes faster growth while the worst-case scenario assumes slow or even declining growth

- As an example, let's say your Bean Haven has grown its revenue 15% month-over-month for the past six months.

- The revenue assumptions for your three scenarios might look something like this:
    - ❑ Base scenario: 15% revenue growth
    - ❑ Best scenario: 25% revenue growth
    - ❑ Worse scenario: 12% revenue growth

Step 5: Forecast Your Revenue….contd

- All assumptions about the revenue forecast should be based on data and not just wishful thinking.

- In the example above if CK needs a plan on how to achieve a 25% revenue growth rate when historically she achieved 15%.

- What strategies can be taken?
  - ❑ Allocate more of our budget to advertising?
  - ❑ Have happy hours?
  - ❑ Add to the menu list?
- What other strategies can be adopted?

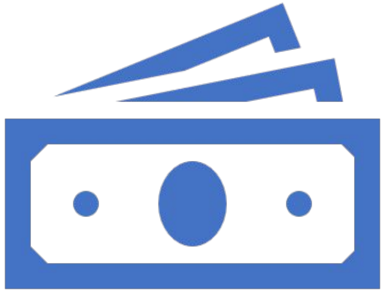
Step 5: Forecast Your Revenue….contd

	Initial Costs$	Monthly Costs $	Monthly Revenue $
Startup Costs			
Leasehold improvements	30,000		
Equipment and furniture	20,000		
Licenses and permits	5,000		
Initial inventory	5,000		
Marketing and branding	3,000		
Legal and accounting fees	2,000		
Monthly Fixed Costs			
Rent		4,000	
Utilities		500	
Insurance		300	
Loan repayments		1,500	
Monthly Variable Costs			
Employee wages		6,000	
Cost of goods sold		3,000	
Marketing and promotions		1,000	
		10,000	
Revenue Projections			
Average monthly sales			15,000.00
Total	**65,000**	**16,300**	**15,000.00**

Net Income

- Calculate your net income (revenue - expenses) for each month.

Step 6: Create a Cash Flow Projection



Now that you have your revenue and expenses, the final step is to create a cash flow projection.

A cash flow projection is simply a forecast of how much money will move in and out of your startup each month.

Step 6: Create a Cash Flow Projection

Steps:

- ❑ Find your opening cash balance: How much money does your startup have in the bank at the beginning of the month?
- ❑ Calculate your receivables (revenue): How much money is your startup going to receive this month?
- ❑ Calculate your payables (expense): How much money is your startup going to pay out this month?
- ❑ Use the cash flow formula: Receivables – Payables
- ❑ Add your opening balance: Add your opening balance to the number you calculated in step #4 to find your closing balance for the month

- Note: If you use a financial planning tool like Finmark, all of this is done for you and made into a chart that looks much better than a spreadsheet. Just sayin…

Step 6: Create a Cash Flow Projection

	Jan	Feb	Mar	Apr	May	Jun	Total
CASH INFLOWS							
Investment	10,000						10,000
Credit sales	2,500	10,000	10,000	10,000	10,000	10,000	52,500
Total inflows	**12,500**	**10,000**	**10,000**	**10,000**	**10,000**	**10,000**	**62,500**
CASH OUTFLOWS							
Project materials		3,000	3,000	3,000	3,000	3,000	15,000
Sub-contract labour	4,000	4,000	4,000	4,000	4,000	4,000	24,000
Marketing	500	500	500	500	500	500	3,000
Legal and accounting	1,250	0	0	0	0	0	1,250
Equipment	2,500	0	0	2,500	0	0	5,000
Sophie & Jack salaries	1,000	1,000	1,000	1,000	1,000	1,000	6,000
Other costs	500	500	500	500	500	500	3,000
Total outflows	**9,750**	**9,000**	**9,000**	**11,500**	**9,000**	**9,000**	**57,250**
NET CASH FLOW	**2,750**	**1,000**	**1,000**	**-1,500**	**1,000**	**1,000**	**5,250**
Opening balance	0	2,750	3,750	4,750	3,250	4,250	
Closing balance	2,750	3,750	4,750	3,250	4,250	5,250	

Tips

Seek Professional Advice:

- ❑ Consider consulting with an accountant or financial advisor to ensure your budget is comprehensive and realistic.
- ❑ They can also offer tax advice and financial planning insights.

Be Realistic and Conservative:

- ❑ When estimating expenses, it's better to overestimate to ensure you have a financial buffer.
- ❑ Stay conservative with revenue projections to avoid disappointment.

Monitor and Adjust:

- ❑ Regularly review your budget against your actual income and expenses.
- ❑ Make adjustments as necessary to stay on track.
- ❑ Consider different scenarios (best-case, worst-case) to be prepared for fluctuations.

Thank you for listening