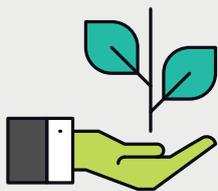


Thinking of starting a small business?

Do your planning first

Has COVID made you reconsider your working future? Did you come up with that one-in-a-million great idea for a home business over lockdown? Are you thinking about making the leap from the salary line to being a small business owner? Keryn Jarvis, Senior Manager in our Tauranga office gives you a few must-consider-firsts before you make that life-changing leap.



Starting up or buying into a small business has so much allure - the idea of "being your own boss" appeals to many of us. Imagine the flexible hours! Not having to fill in a timesheet! In reality, what we've found from our work with our clients is that there are five key "must have" personal attributes all small business owners have:

- A commitment to hard work and personal sacrifice;
- Enthusiasm, tenacity, and the appropriate level of self confidence;
- A product, skill, or service which is marketable;
- Managerial, administration and marketing skills;
- Adequate personal financial resources.

Now, for tomorrow

Dream Big: the reality of risk & reward

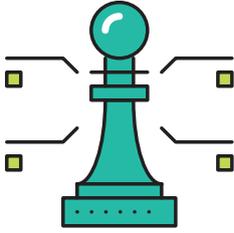
The dream of owning a successful small business usually involves setting your own goals, having lots of personal accountability and decision making power. However the reality can be more like "buying a job".

For all the rewards of being your own boss, many things we take for granted as an employee disappear when you are a business owner. Say goodbye to job security, set hours of work, guaranteed regular income, holiday and sick pay, and long service leave.

Owning your own business also means there is a risk that you could lose your investment if the business fails. By going into business for yourself you will be facing risks not associated with paid employment. These are many and varied and the riskier the business, the more it will need to generate by way of return to justify taking those risks. For example, a fixed deposit account at 1% - 2% with a major bank is considered a risk-free return. Another alternative could be a commercial building at 4%-6% return.

As the risk of any venture increases, so will the required rate of return on that investment. A business owner should therefore review the risk versus return of the business regularly.





Plan to fail or fail to plan?

Business start up statistics in New Zealand are also worth considering. According to a survey performed by Ministry of Business, Innovation and Employment (MBIE) in 2017, 63% of Kiwi businesses started in 2010 (with no employees) ceased to exist by 2016. Businesses with up to 5 employees were slightly better at 48%. Unfortunately, this shows a large percentage of start-ups don't move beyond the start-up phase.

While the reasons for business failure are varied, the most common appear to be:

- Poor management
- Poor record keeping
- Insufficient working capital
- Failure to plan
- Misuse of time
- Neglecting marketing

Excuses for business failure are too often levelled at "business climate", finance costs and difficulties, demand slumps, and regulations – not at the five "must haves" we talked about at the beginning of this piece.

We find that well managed businesses will generally:

- Weather economic and business storms
- Have proper financial information
- Have a written business plan with future development and expansion guidelines
- Have an adequate product mix
- Do not rely too heavily on one, or a limited group of customers or clients
- Know their operating environment

What to look out for once you're started

There are many checkpoints on the road to failure and if these are addressed along the way then survival is more likely. Some issues to consider are:



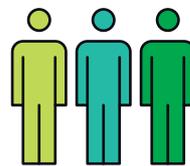
Insufficient Working Capital

Many small businesses suffer from this problem, especially during the "start up" phase or during expansion or growth periods. Insufficient working capital often makes it difficult to purchase stock efficiently and at the best prices, with lack of stock often resulting in lost sales.

Borrowing excessively means a greater portion of gross profit is directed towards finance costs and cash flow is also drained by repayments. Invariably the business struggles to meet its commitments as they fall due, increasing stress on the business owner.

Partnership Problems

Partners should be selected in the same way as employees are selected – that is, on the basis of their ability to work with you and contribute effectively to the business and help achieve its goals. Too often a partner is selected simply because he/she is a relative or friend or is willing to contribute an amount of capital.



Lack of Management Expertise

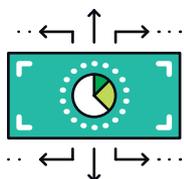
A business plan is essential, not only for the purpose of raising capital but to act as a blueprint for your business's future growth. Make sure you have the necessary expertise in your chosen business field; don't think you can get away with "learning on the job".

Incorrect Pricing Policies

Too often prices are set to market determinants rather than to cost recovery and profitability generation. Efficient client service or added value may be more important than price alone. Unless you can make an adequate margin or profit, the business is doomed to fail.

Marketing

Many small businesses go broke simply because they don't sell enough product or they fail to keep abreast of market, operating and technological changes. In most businesses, nothing is constant. You must continually update your product or service to stay in tune with market demands and competition.



Cash flow

A business that fails to forecast or track its cash flow appropriately is headed for trouble. Without proper and accurate cash flow projections and tracking, management is unable to identify future cash requirements and hence lacks vital information about the financial direction of the business.

However, "cash flowing" alone is not enough, the business must be returning a profit. The long term trend of both must be positive in order to survive and prosper. Ideally each business should have a budget showing expected future income and expense levels and the minimum return required by the business owner.

It is important for the business owner to know the point at which the business will break-even.

That is, the point at which the gross profit (revenue less direct costs) equals total fixed costs. Any additional turnover will result in a profit equal to the gross profit on this turnover, and any reduction in turnover will result in a loss, as all fixed costs are not being met.

Knowing these revenue levels and monitoring them regularly will allow the business owner to know from month to month how their business is performing. Low profit months will generally impact on cash flow in the current and following periods. Therefore the ups and downs in turnover will usually be mirrored in cash flow projections. Hence the importance of the interaction between profitability and cash flow projections.

Ready to make the leap?

Buying or starting up your own business can be both an exciting and stressful time. The key to increasing your chances of survival is being prepared and equipped with the right information and specialist advice, and having access to real time reporting on an ongoing basis so you can monitor how things are tracking and make decisions in a timely manner.

Your accountant or business advisor is a key partner in this process. Ideally you should run your business plan past them first, before even approaching the bank for funding. You'll get a much better idea of viability, as well as an alternate perspective. Even though you think your idea is the "best thing since sliced bread", your advisor may have tried many more types of bread than you and have a different view!

Starting a new business can be the life change you need: just make sure you look before you leap.

About Baker Tilly Staples Rodway.

Baker Tilly Staples Rodway is proud to be a member of Baker Tilly International, a top ten global network of independent accounting and business advisory firms, whose member firms share our dedication to exceptional client service.

www.bakertillysr.nz