

Financial Planning

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Lesson 11/12

1 Introduction

The lesson of today will add something to our economic background. Will be useful for an entrepreneurial point of view in order to understand the value of what we are doing if we are working on a project (a lot of companies work on a project base organization) and the budgeting (how much we are going to spend) on projects. And even more useful for people who want to build their own startup. We already saw something on the venture financing lesson, today we will see something deeper.

But, the difference is that for financial planning we have a lot of literature.

2 Financial Statement (Bilancio-Balance sheet, Stato patrimoniale)

This is useful to understand as physical persons to be able to do the declaration of incomes (the state want you to pay taxes), or if you are an employee to understand taxation on your salary. Up to a certain amount of incomes you are tax free, then at brackets you have different taxation. Everyone pay the same for the same slots.

For companies (in Italy IRES) the taxation is fixed (around 22 %). Public companies are mandatory to publish their balance sheets (how much they earned, how much they spent, and so). The balance sheet tells how rich and wealthy is the company.

Conto Economico		Bilancio Patrimoniale	
Conto Economico ABC Accounting Services Income Statement For the month ended July 31, 2008		Bilancio Patrimoniale ABC Accounting Services Balance Sheet As of July 31, 2008	
Revenue Service Revenue \$6,000	Expenses Cash \$ 700 Supplies 2,000 Equipment 500 Total Expenses 3,200 Net Income \$1,800	Assets Cash \$5,000 A/R 1,000 Equipment 2,200 Total Assets \$8,200	Liabilities Bank Loan \$3,000 A/P 1,200 Total Liabilities \$4,200 Equity Common Stock \$1,451 Ret. Income 3,200 Total Equity \$4,651 Total Liabilities and Equity \$8,200
Account Relationships † Net Income => † Equity † Revenue => † Assets (cash or accounts receivable) which † Equity † Expense => † Assets (supplies) and/or † Liabilities (accounts payable) which † Equity			

Figure 1: Income statement & Balance sheet

- Conto economico - What before we called "income statement" every line express a voice, divided in macro categories. You subtract to the incomes the costs and we have the gross margin of our product (incomes - material, bills). At a certain point you reach the net margin to bring to the taxes agency, which take 25 % of it. Then you have the final margin of the company.
- Stato patrimoniale - The balance sheet. Not just the margins, but also the possessions (Machines, Other companies stocks, Intellectual property, ...) of the company are considered.

2.1 Financial Statement Definition

" Formal record of the financial activities and position of a business, person, or other entity occurred during a certain period. Presented in a structured manner and in a form easy to understand, including:

- A balance sheet, also referred to as a statement of financial position, reports on a company's assets, liabilities, and owners equity at a given point in time.
- An income statement, also known as a statement of comprehensive income, statement of revenue & expense, profit and loss report over a period of time
- A statement of changes in equity, retained earnings, reports on the changes in equity of the company during the stated period.
- A cash flow statement reports on a company's cash flow activities, particularly its operating, investing and financing activities "

3 Cash Flow Management

We saw the cash flow of the lifetime of a startup. It tells how much money we have in our pocket at a certain time. You usually take care of your cash flow (= money in - money out) every week, month or year.

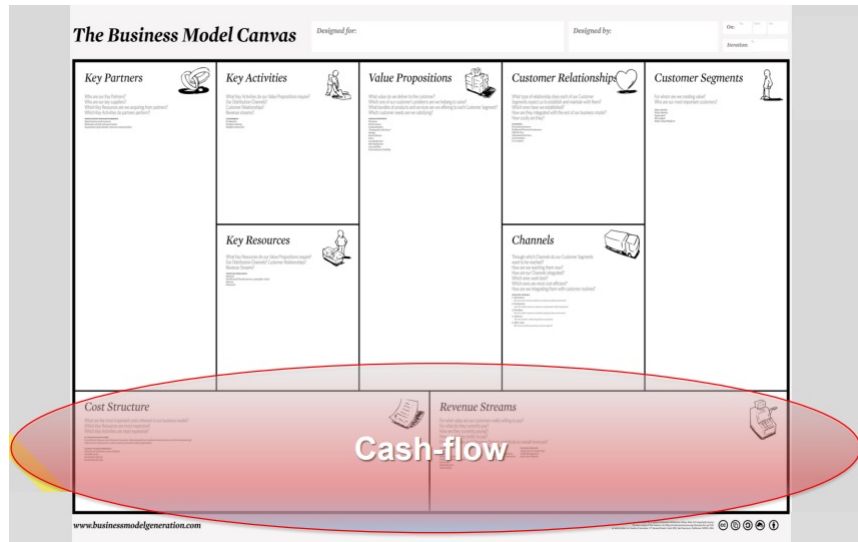


Figure 2: Location in business model Canvas

As we saw, the cash flow in business model canvas is at the bottom side (top side is about qualitative reasoning, and at bottom there are the moneys), and divided in two parts, Costs and Ravenues .

3.1 Example: Water in the tank!

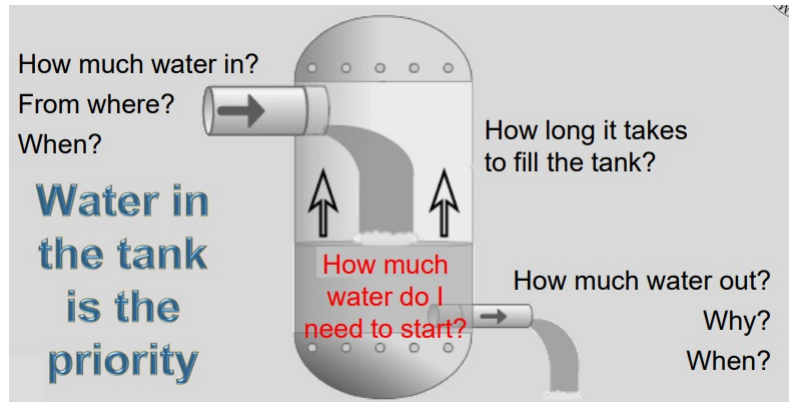


Figure 3: The Watertank example

Think about a tank, our objective is to fill it (have the most income as possible). Try to keep the water as high as possible. Some water in the tank must be always present (otherwise we are spending money we don't have!).

3.2 Why cash flow is important?

- to understand: when you can start your company (example, how much money you can get selling my app/product), what you can do with your company.
- to explain: to someone interested in your company (example. Venture Capitalists) what you can do and what happens to their money. If you can't explain in a good way your idea, no one will give you money to implement it.

3.3 Variables (related to watertank example)

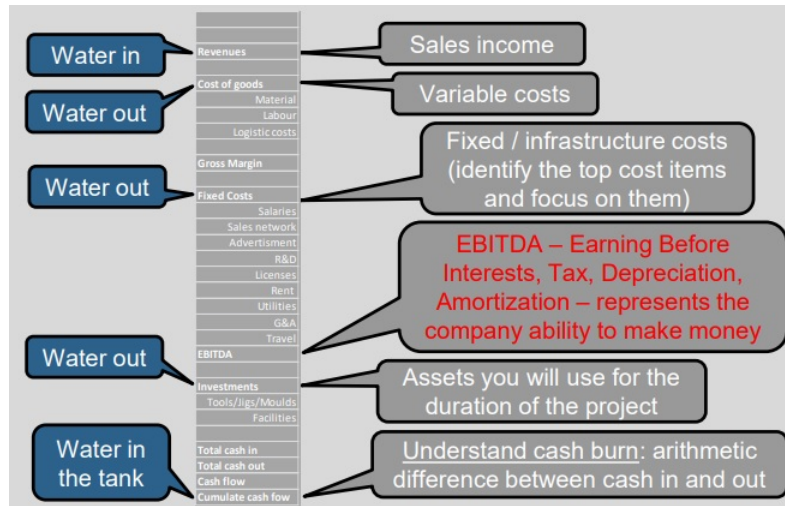


Figure 4: The Variables

We get water (money) when we sell stuff, and we lose water when we pay bills, materials, taxes, If someone want to invest in your startup they usually want to see the EBITDA, that express how much is your company wealthy. Important parameters to know.

3.4 Calculations table

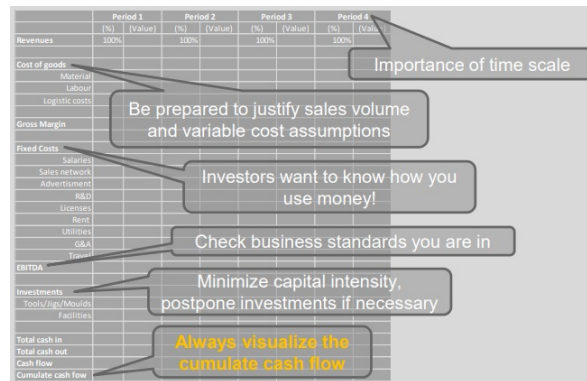


Figure 5: The Calculations

Always try to minimize capital intensity as a startup. We are lucky because IT is by nature not capital intensive.

3.5 Visualize: Building the hockey stick

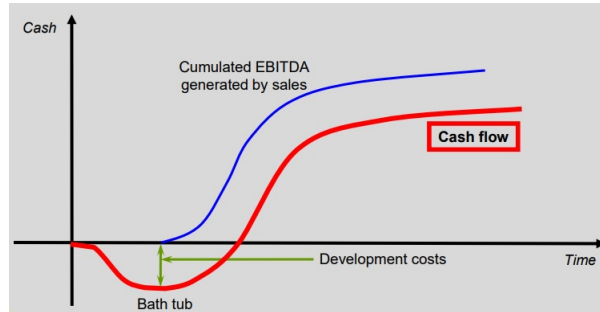


Figure 6: The Cash flow example

Cash flow related to the EBITDA. Same graph we saw in Venture Financing. Is called hockey stick due to the form of the graph.

3.6 Patient vs. aggressive investment

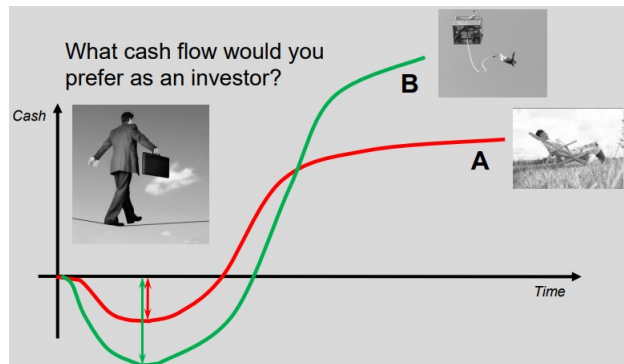


Figure 7: The Universe

One has a higher gain but need a higher investment. During time the profits increase more if we invested more as a general rule.

Usually keep track of the risk! If both paths have the same risk and is low, go for the big investment and big payoff.

3.7 Tuning

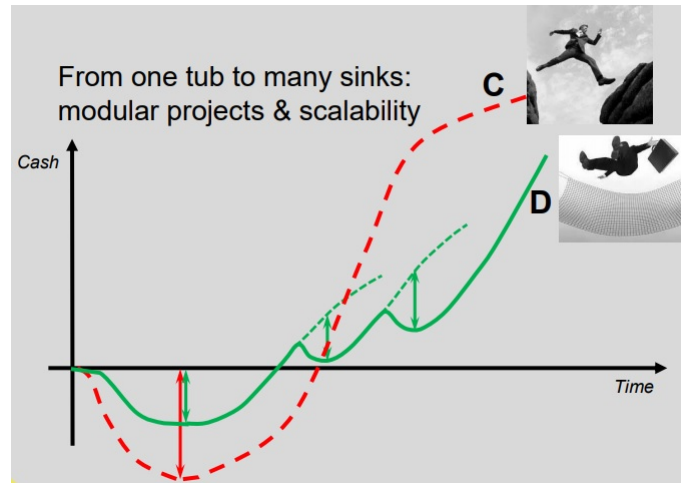


Figure 8: The Tuning

Try to divide the project in subprojects! Divide in modules. Example of a famous startup that had this approach we saw in Venture Capital: Airbnb.

3.8 Advices

- Financial planning and cash-flow management are for you
- Make assumptions and validate them in a iterative process
- It's a decision making process (short-term, long-term)
- Not all you prepare shall be exposed (hide your weak points)
- CF tuning is visible in the form of self confidence
- Investors wants to perceive you know what you talk about

3.9 Example of Cash flow

On slides. Just a visual example.

4 Business Plan

4.1 Definition

- “A written document describing the nature of the business, the sales and marketing strategy, the financial background, and containing a projected profit and loss statement” – Entrepreneur Magazine
- A business plan is essentially a roadmap for entrepreneurs, helping them collect together all the different aspects for their future venture.
- Consequently, a business plan also serves as a technical pitch for investors, banks, and other financial service providers.

4.2 Business Model vs. Business Plan

”For an improved early definition of your business idea prepare a good and sustainable Business Model. For a detailed analysis of your business once the idea is validated and all assumptions are clear prepare a sound Business Plan.”

So, the model is done even before the startup foundation, and is used also to attract investors, and the business plan is done after to describe your business.

The business model as we saw, is the model used to get value from customers.

4.3 Business planning process



Figure 9: The Business planning process

4.4 Business plan outline



Figure 10: The Business plan outline

[On the slides an example of Business plan outline]

4.5 Why do you need a business plan?

- Document your thoughts into auditable and demonstrable activity
- Show feasibility of your ideas
- Translate your planning into a roadmap that supports identifying the most successful options
- Ensure you have considered the business from all possible points of view
- Communicate your idea
- Get your startup funded

4.6 When should you do a business plan?

Never.(Unless: specifically requested, you seek funding, you want to deeply understand the functioning/potential of your company)

5 Conclusions

The arguments we discussed now are part of a tool kit that can support us when we will be part of a company or we will found a startup.