DTU 42435 - F2013 9. Lecture

BUDGETTING

- **Methodology**
- **Case**

Why bother

- **Quantify scenarios** — *Get an overview of economics*
- **Quantify perspectives** — *Get people involved*
- **Determine cash requirements** — *Get your venture funded -*
- **Cash flow management by budget supervision** — *- and managed.*
- **Tuning the start-up strategy** — *- by balancing perspective against financing model*

BUDGETTING PROCEDURE
Precondition for budgetting:

Market analysis and business model finalized

1. **Market penetration scenario established -> sample**
2. **Estimate company operations as a function of 1)**
3. **Establish budgets on transactions[1] in sales and company operations**

Budget on transactions in sales and company operations

=> Your CASHFLOW BUDGET excl. investments

1) Transaction = money being moved in or out of the company's bank account

CASHFLOW BUDGET

CIMITYM

Cash Is More Important Than Your Mother (Ken Morse, MIT)

- **Input:**

  <u>ALL</u> estimated in- and outgoing payments (transactions) in a time domain

- **Output:**

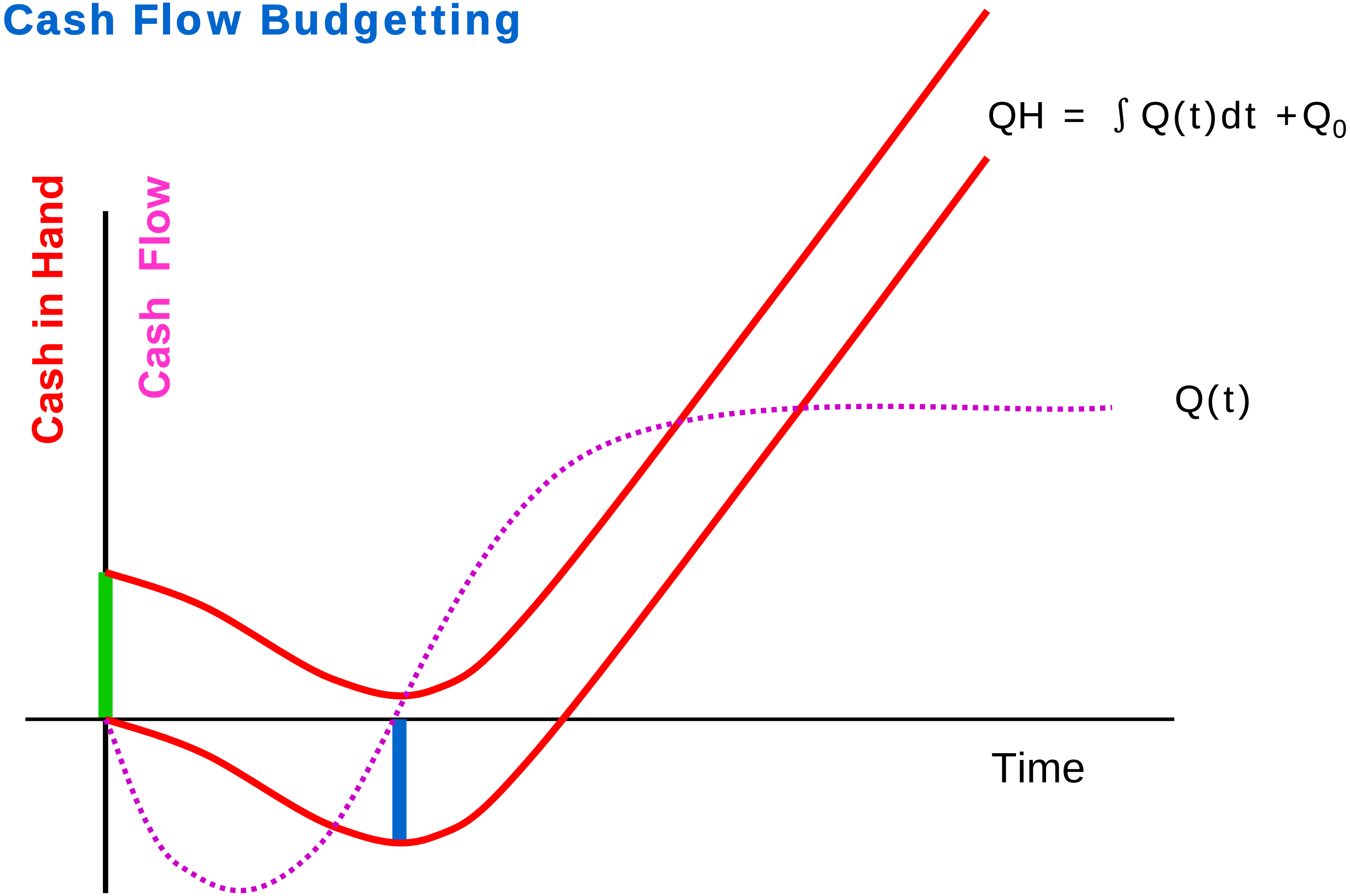
  The total amount of cash flowing in and out in the time domain =>The net amount of cash flowing in/out

Accumulated net cash flow = ***<u>Cash in Hand</u>*** *as a function of time*

Cash in Hand ***NEVER*** *negative:*
that defines your capital requirements!

Inject capital until this condition is met at any given time

Cash Flow Budgetting



Cash Flow Budgeting -> Capital Requirements

SALES and PRODUCTION

Outgoing payments to cover production and incoming payments from sales are derived from:

- Unit costs
- Sales price
- Market penetration in the time domain (market entry scenario)

MARKETING and OPERATIONS

Outgoing payments to run the company are derived from

- Sales & Marketing expenditures
- Rent, running costs, salaries
- IPR , R&D expenditures
- Capital expenditures

Add all outgoing (+) and incoming (-) payments determine cashflow (Q [DKK/month]) and cash-in-hand (QH=∑Q [DKK]).

Adjust with appropriate cash injections *(loan, equity capital)* to create a positive cash-in-hand throughout the project

Budget on Profit & Loss

Precondition: the cash flow budget

- **Covers an extended period e.g..: 1 year = Annual results**
- **Objectives: analysis, perspectives, key figures, profitability**
- **Consequences:**
  - Trim your business
  - Benchmarking against your competitors' performance
  - Benchmarking against your own previous performance
  - Sanity check – with key-figures and common sense
  - Quantify perspectives
  - Quantify returns on investments => VC case? Y/N.

Budget on Assets & Liabilities - 1

- **Assets = Values owned by the company**
- **Liabilities = How are said values financed**

- **Assets** = outstanding amounts owed to the company, cash in hand, IPR, goodwill , buildings, cars, production facilities - - - depreciated to value as per to day.
- **Liabilities** = invested capital, accumulated profit/loss, outstanding amounts owed by the company
- **Invested equity capital + cumulated profit/loss = equity capital of the company**

Budget on Assets & Liabilities is the last to complete

Budget on Assets and Liabilities - 2

Objectives:

- Determine development in company value over time
- Present financing
- Keep track of development in debtors and creditors
- Check minimum legal equity

Consequence:

- **Solvency = capacity to withstand losses is determined**
- **The development of values over time is quantified**
- **The proficiency in running a tight payment policy is demonstrated**
- In DK: legal minimum equity capital is checked