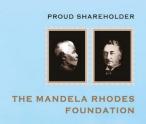
Chapter 11 Financial planning and forecasting

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Learning outcomes

- Discuss the purpose of a financial plan detail
- Define 'financial plan' and financial policy'
- Discuss the purpose of a financial policy in detail
- Name and discuss the different components of a financial policy and their influences

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Learning outcomes (cont.)

- Determine a break-even point
- Name and discuss the various types of finance
- Discuss the importance of cash flow in a small business venture
- Define 'forecasting process' and discuss this concept
- Develop the three financial statements used in the forecasting process

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Planning

Planning: thinking what and how a required outcome, result or objective

should be obtained. Planning involves:

- Identification and formulation of objectives
- Gathering all necessary data
- Analysing the data
- Drawing up the plan
- Implementation of the plan

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Financial policy

Policy: sets out guidelines or principles according to which an enterprise must act in obtaining its objectives. Components of financial policy:

- Forecasting and planning
- Major investment and financing decisions
- Coordination and control:
 - 1. Setting standards
 - 2. Compare actual results with standards
 - 3. Evaluation of deviations
 - 4. Take corrective action when necessary
- Risk management

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Financial plan

- Is concerned with:
- Investigating the choice between two or more alternatives
- For reaching a specific objective
- Determining how each specific goal is to be achieved
- Involves the effective acquisition, use and control of financial resources



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Purpose of financial plan

- Provides specific outcomes of future activities in monetary terms
- Provides the necessary figures to back the various choices made

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Purpose of financial plan (cont.)

- Factors to consider when developing a financial plan:
 - The industry and competition
 - The market
 - Current economic and political circumstances
 - Technology
 - Social environment
 - Ecological environment

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Break-even point

Quantity = <u>Fixed costs per unit</u> (Price – Variable costs)

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Limitations of break-even point analysis

- Not easy to classify all costs as either fixed or variable
- Elements of fixed and variable costs are not always constant
- Excludes qualitative factors
- Instability of monetary value not taken into account

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Financial forecasting

- Financial-planning process steps:
 - Project financial statements
 - Determine funds to support five-year plan
 - Forecast funds available for next five years
 - Establish and maintain system of controls
 - Develop procedures for adjusting basic plans

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Reasons for forecasting

- Forecasting enhances quality of planning
- Control function is made easier
- Enhances integration and coordination of various opinions and needs
- Actual performance of various departments and personnel can be measured more easily



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The forecasting process

- Information needed:
 - Operating budget
 - Projected cash budget
 - Projected statement of profit or loss and other comprehensive income
 - Projected statement of financial positions



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Pro-forma financial statements

The pro-forma statement of cash flows

- A statement of an entity's planned cash inflows (money physically coming into the business)
- Cash outflows (money physically going out of the business)
- It is used to estimate an entity's short-term cash requirements.

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The pro-forma statement of profit or loss and other comprehensive income

- A statement used to plan whether an entity will be making a profit or a loss
- During a given financial year
- Taking into account all the income that is to be received
- All the expenses that has to be paid

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The pro-forma statement of profit or loss and other comprehensive income (cont.)

- To prepare:
 - Compile sales or fee-received projection
 - Compile operating schedule
 - Determine any other expenses
 - Calculate projected profit

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The pro forma statement of financial position

A planned financial statement on a certain date
 to determine the financial position of the entity
 with respect to its capital generated and the application thereof