FETC: NEW VENTURE CREATION

NQF LEVEL 4

66249

151 CREDITS

LEARNER GUIDE

MODULE 1:

Business Planning and Market Mechanism

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Key to Icons

The following icons are used throughout the study guide to indicate specific functions:

	Activity This icon indicates that you are required to complete certain activities, designed to assist you with your studies.
	**Workbook Activity** This indicates activity to be completed in the Learner Workbook for assessment purposes
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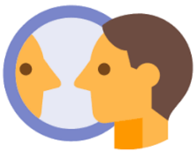	**Reflect on this** Take time to really think about this point
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ABOUT THIS GUIDE

This module belongs to you. It is designed to serve as a guide for the duration of your course and as a resource afterwards. It contains readings, activities and application aids that will assist you in developing the knowledge and skills stipulated in the specific outcomes and assessment criteria. Each section will be preceded by outcomes, criteria and critical cross field outcomes taken from the SAQA unit standards. These will describe what you must know and be able to do to successfully complete the course.

Follow along in the guide as the facilitator takes you through the material and feel free to make notes and diagrams that will help you to clarify or retain information. Jot down things that work well or ideas that come from the group. Also note any points you'd like to explore further.

How will you be assessed?

The assessment process is easy to follow. You will be guided all along by the Facilitator. Your responsibility is to complete all the activities in the workbook and submit it for assessment. At the end you will receive credits towards this unit standard upon successful assessment.

Take a moment and think about what you would like to learn from this course.

Introduction

Welcome to the Further Education and Training Certificate in New Venture Creation.
This qualification is registered on the National Qualifications Framework (NQF) at level 4 and has been specifically designed to help you learn the skills necessary to set up and run a successful small business.

Please read this section carefully as it covers some important information that you need to know before you start your training.

The New Venture Creation Qualification

This is a qualification for all members of the population. Anyone preparing to become employed, or self-employed, in any business would be the typical learner.
In fact, many newly (or not-so-newly) appointed personnel, or struggling entrepreneurs, could benefit from part or all this qualification.

The purpose of this Qualification is to develop the appropriate skills and knowledge required by a person for the establishment and development of a small to medium business venture, and address the economic, administrative and behavioural (psycho-social) barriers that contribute to success in starting and sustaining the venture.

You will be able to:

- Demonstrate an ability to identify and create a new venture.
- Demonstrate knowledge of interpersonal skills required in a business environment.
- Demonstrate an understanding of basic economics within a market economy.
- Manage a new venture by applying business principles and techniques.
- Demonstrate an understanding of the role of leadership and management.

Exit Level Outcomes of this Qualification

At the end of the programme you the learner will be competent in the following listed outcomes.

Exit Level Outcomes	Associated Assessment Criteria
ELO1. Demonstrate an ability to identify and create a new venture	1.1 An understanding is demonstrated of the importance of a paradigm shift from a job-seeking attitude to a business opportunity seeking attitude. 1.2 Business opportunities are identified and evaluated in terms of its potential viability. 1.3 Problems-solving techniques and principles are applied within a business start-up and operation context

Exit Level Outcomes	Associated Assessment Criteria
ELO2. Demonstrate knowledge of interpersonal skills required in a business environment.	2.1 An understanding is demonstrated of the concept of group dynamics. 2.2 An understanding is demonstrated of the characteristics of effective teamwork. 2.3 An understanding is demonstrated of various networking principles and techniques. 2.4 Potential personal limitations, abilities and expectations are identified for self-developmental purposes.

Exit Level Outcomes	Associated Assessment Criteria
ELO3. Demonstrate an understanding of basic economics within a market economy.	3.1 An understanding is demonstrated of new venture financing sources and opportunities. 3.2 An understanding is demonstrated of the principles of micro and macroeconomics. 3.3 Potential threats and opportunities within the economic environment are identified for future business decision making. 3.4 An understanding is demonstrated of business competitiveness.

Exit Level Outcomes	Associated Assessment Criteria
ELO4. Manage a new venture by applying business principles and techniques.	4.1 A business plan for a new venture is developed using strategic planning principles and techniques. 4.2 Guidelines for the implementation and monitoring the strategic action plan are formulated in terms of milestones and timeframes. 4.3 Financial management planning principles and techniques are applied in order manage the business in an efficient and effective manner. 4.4 Production and/or operations management is applied in a chosen business opportunity. 4.5 Sound human resources management techniques are applied to set up a productive and motivated workforce for a business. 4.6 Administrative principles and procedures are applied for sound administration and record-keeping

Exit Level Outcomes	Associated Assessment Criteria
ELO5. Demonstrate an understanding of the role of leadership and management	5.1 Knowledge is demonstrated of how management and leadership principles are applied to improve business effectiveness and efficiency. 5.2 Knowledge is demonstrated of the differences between leadership and management in terms of managing a business. 5.3 Knowledge is demonstrated of leadership and management styles in relation to their impact on business performance. 5.4 Leadership and management principles and techniques are applied to enhance business performance

Unit standards

This is a national qualification and it is made up of separate 'modules'. These 'modules' are called *unit standards.* Each unit standard has its own registration number and each one is registered on the National Qualifications Framework, along with the full qualification. Unit standards are important because they tell everyone involved what is expected of them. This is what the unit standards tell you (the learner), your teacher (facilitator) and your assessor (examiner):

You, the learner	**The unit standards tell you what you must** know and what you must be able to do **at the end of each section or at the end of the learning unit.**
Your facilitator (teacher)	The unit standards tell your facilitator (teacher) **what to teach.**
Your assessor (examiner)	The unit standards tell the assessor what kinds of **questions** to ask you in the assessment.

The unit standards can be found at the back of your learner guide in the annexures. Some things might be a bit difficult to understand so make notes so that you can ask your facilitator to explain them if you are not sure what something means.

Structure of a unit standard

Each unit standard is made up of Specific Outcomes (which are like sub-modules).

These break the unit standard up into sections that describe what you must know and be able to do. These specific outcomes can also be found in each chapter/unit of this learner guide, so that you can match the unit standards to the training material and the lessons that you attend. This will help you to prepare for your lessons and for the assessments that you are going to do throughout this qualification.

Assessment

There are two types of assessments: Formative and Summative.

Formative Assessment

In each Learner Guide, several activities are spaced within the content to assist you in understanding the material through application. Please make sure that you complete ALL activities mentioned in the Learner Workbook, whether it was done during the contact session, or not! These activities are found in a separate Formative workbook for ease of assessment. Do not complete them in the Learner Guide; use the Formative workbook to do so.

Summative Assessment

You will be required to complete a Portfolio of Evidence for summative assessment purposes. A portfolio is a collection of different types of evidence relating to the work being assessed. It can include a variety of work samples.

The Summative Workbook will assist you in identifying the portfolio and evidence requirements for final assessment purposes. You will be required to complete the assessment activities on your own time, using real life projects in your workplace environment in preparing evidence towards your portfolio.

Your assessment for this qualification will be slightly different to the assessments that you did at school. This is because the qualification will be awarded by the
Services Sector Education and Training Authority (SETA), and they do assessments slightly differently to the way that schools do it. To be awarded this qualification you will have to:

	How will you do this?	**When will this be assessed (marked)?**
Demonstrate your knowledge in the concepts presented	By completing the on-going (also called *'formative')* assessments for each chapter. These can be found in the separate workbook and are cross referenced in this learner guide.	Your assessor will mark these and give you regular feedback.
Practical application	By completing activities in your workbook that shows all your practical skills as you develop them—both in the classroom and in the workplace.	You will hand your portfolio in once it is complete. It will be assessed by registered assessors and then the Services SETA will check (moderate) the assessors (markers) before awarding you your certificate of competence.

Workplace Application	By working in a business.	This practical evidence will be part of your portfolio and will assessed at same time.

It is to stay up to date with your assessments and not fall behind. If you leave the projects/assignments until the end of the training you may find that you do not have enough time to finish them properly, which may cause you to be found “not yet competent”. This will mean that you will have to do the activity/ task again and that will take up even more time.

Second Language Usage

Fundamentals Assessment – CAT

CAT is the acronym for “*Credit Award Transfer*”, and is based in a model developed by SAQA that will be used to determine whether CAT (Credit Award Transfer) will be implemented to recognise school / FET qualifications and sector qualifications. According to the qualification requirements, 20 credits from Fundamental unit standard must be done in the learner’s second language. Therefore, half of the facilitation of the communication module, equalling 20 credits will be done in the learner’s second language. This is in conjunction with SAQA requirements of conducting communication in two languages. All qualifications require that every learner must do at least 56 credits in fundamental standards, of which 20 credits must be in a 2nd language if the qualification is al level 4 or above

It is acknowledged that many of the learners will have come from different backgrounds and with different scholastic achievements already in place – it is therefore appropriate that prior scholastic qualifications be recognised. SAQA recognises that candidates may have prior learning in literacy and numeracy that may be recognized through a process of *Credit Accumulation Transfer (CAT).*

According to the SQA Policy on FETC, Clause 5 of Executive Summary:[1]

The 20 compulsory credits in Language and Communication must be obtained in one of the eleven official languages provided for by the SA Constitution of 1996 (Act 108 of 1996) at level 4. All holders of an FETC will have achieved the same outcomes as indicated by the 20 compulsory credits but these may be achieved in any one of the eleven official languages.

To address the need to develop citizens who can participate effectively in a multi-lingual society, a further 20 credits in Language and Communication must be obtained in a second official language at a minimum of level 3. All holders of an FETC will have achieved the same outcomes as indicated by the 20 compulsory credits but these may be achieved in any one of the eleven official languages. In some learner guides, you will find content and activities that is done in a Zulu Language.

Learner materials

You will be given the following materials:

1. Learner guide (this guide) - this presents the theoretical training material that you will need to work in a business. It has been written to match the unit standards.

2. A Portfolio of Evidence (POE) workbook - this is where you will complete your assessments, projects, and other activities. Your facilitator will take these in to assess (mark) your ongoing knowledge (also called the formative assessments).

You will also need to complete projects and assignments and provide practical evidence that will be filed in this workbook. This will be taken on the agreed date and assessed.

Outcomes-Based Learning

The new learning approach in South Africa is now focused on Outcomes Based Education (OBE). This means that the focus is learner-cantered & not content-cantered. This also means that the trainer / lecturer’s focus has also changed to one of facilitation.

Outcomes based education holds the following key beliefs about learning and success:

- What and whether learners learn successfully is more important than exactly when, how and from whom they learn it.
- All learners can learn and succeed, but not on the same day in the same way.
- Successful learning promotes more successful learning, just as poor learning fosters more poor learning.

So, what does this mean exactly?

OBE means that whilst you are in the classroom you will learn through various activities, for example:

- Group work
- Pair work
- Discussions (sharing of experiences)
- Practical activities
- Role plays
- Research
- Portfolio building

This also means that your facilitator will spend less time on lecturing & more time on facilitating your learning style & pathway.

Lifelong Learning

We often think that we will be finished with learning when we finish school. However, many famous people have said that if we stop learning, we stop living. You will learn right through your life, from being in the workplace until the day that you die.

Learning Styles

Introduction

Nobody can teach a learner to study and learn without the learner making any effort on his or her part. This module is designed to help you to become a successful student. But remember, nobody can learn to do heart surgery or fly an aeroplane just by reading a book – even you cannot become an efficient student by just reading about how to do it.

With the above in mind, it needs to be said that there are no shortcuts in studying. The learner must apply him / her, and this requires certain skills, techniques and a method that suits the individual. Not every method will suit every learner as we all differ in personality and intellectual ability.

What are learning styles?

Learning styles are simply different approaches or ways of learning.

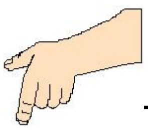
The different types of learning styles

Visual Learners: *learn through seeing*...

These learners need to see the teacher's body language and facial expression to fully understand the content of a lesson. They tend to prefer sitting at the front of the classroom to avoid visual obstructions (e.g. people's heads). They may think in pictures and learn best from visual displays including diagrams, illustrated textbooks, overhead transparencies, videos, flipcharts, and hand-outs. During a lecture or classroom discussion, visual learners often prefer to take detailed notes to absorb the information.

Auditory Learners: *learn through listening...*

They learn best through verbal lectures, discussions, talking things through and listening to what others have to say. Auditory learners interpret the underlying meanings of speech through listening to tone of voice, pitch, speed, and other nuances. Written information may have little meaning until it is heard. These learners often benefit from reading text aloud and using a tape recorder.



Tactile/Kinaesthetic Learners: *learn through moving, doing and touching...*

Tactile/Kinaesthetic persons learn best through a hands-on approach, actively exploring the physical world around them. They may find it hard to sit still for long periods and may become distracted by their need for activity and exploration.

Follow the following link or search from your browser and answer the quiz on learning styles.

http://www.educationplanner.org/students/self-assessments/learning-styles-quiz.shtml

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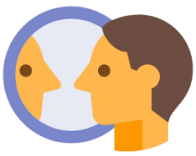	**Reflect on this** Take time to really think about this point
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Introduction to this training

The objective of this course on New Venture Creation is to give you the necessary knowledge and skills to either start your own small business or to operate within an existing business as your own unit. This is not an easy task but if you work *systematically* (step-by-step) through this learner manual and through the exercises in the workbook then you will have all the tools needed start your business.

You would get the most out of this training if you chose a product or service to sell at the beginning of the course and follow that same idea throughout the entire course.

That way everything you do (from an evaluation of the marketplace, your marketing plan, your business plans and budgets, etc.) all relate to one example.

But, if you need to change, then you can do so. It is better that the course is practical and relates to something real that you are doing rather than simply an academic exercise.

You may decide to work in small groups to start a business for this course. That is a good idea, but you must make sure that each one of you does your own work in the portfolio workbook. You cannot all have the same business plan and the same marketing plan and the same answers to the questions. You can talk about the questions and the answers but each one of you must answer each question in your own portfolio workbook in your own words. If you are found copying the SETA will not give you your certificate - and that would be a great shame after all the work, you are going to put in!

Good Luck! We hope to see you running businesses soon

LEARNING UNIT 1: Market Mechanisms

Learning Outcomes:

By the end of this unit, you will be able to:

- ✓ Explain the free market system in terms of perfect and imperfect competitive markets
- ✓ Discuss and illustrate the interaction of demand and supply in price determination
- ✓ Identify and discuss the factors that drive economic activity
- ✓ Describe the development and significance of markets with particular reference to South Africa.

1.1. INTRODUCTION

As a business owner, you will continually make decisions for your business in order to fulfill your needs and wants. These decisions are usually based on the limited resources of your business, as well as other factors, such as consumer's perceptions of your business. It is important that you understand the basics of economics, the business market and factors that drive economic activity, in order for you to make informed decisions for the ultimate success of your business. This course aims to give you a working knowledge of demand and supply and the effects of pricing, as well as competitive markets and factors that influence economic activity, such as inflation.

Economics is the study of human behaviour attempting to fulfill needs and wants. Economics assumes that humans aim to fulfill their self-interests and that they make rational decisions regarding these needs and wants. Due to this, economics can be thought of as a human behaviour study rather than a complicated form of statistics with complex tables, charts and difficult numbers. There are a few concepts of basic economics that you will need to understand before we move on to discuss economic activity and various economic markets.

Economics can be divided into two separate fields of study

(1) Micro economics
Focuses on individual sections of the economy and considers the decisions and actions of individuals, households, firms and other organisations, separate from the rest of the economy. This includes the study of demand and supply for products and services.

(2) Macro economics
Concentrates more on the economy as a whole and develops an overall view of total economic behaviour. Macro-economics explores factors such as economic growth, inflation, unemployment and production, Technology, Legislation, Culture and Politics to name a few.

As it was already mentioned in the introduction, people have needs and wants and thus make various decisions in order to fulfill these needs and wants. These decisions are made taking their limited resources into account. This is the main economic problem called scarcity, and forms the basis of economics in general. Scarcity is the conflict between limited resources and unlimited wants.

An individual's resources are time, money and skills, while a country's resources are the factors of production, such as capital, labour, technology and other resources. These are often limited and economics is the study of how these resources can be allocated more efficiently.

This chapter is based on demand and supply. This was briefly discussed in the costing and pricing module, so if you have completed that module, make sure you go back and understand it from an economic point of view.

Demand is usually graphed on a market demand curve, illustrating the amount of product or service demanded by consumers at the different prices. The relationship between price and quantity demanded is called the demand relationship. Supply shows how much the market can offer or the amount of a product or service sellers are willing to offer for sale. This is the supply relationship. Demand and supply relationships illustrate the forces and factors that affect the allocation of resources.

1.2. THE LAW OF DEMAND AND SUPPLY

The Law of Demand
If all other factors remain the same, the higher the price of the product or service the less people will demand of that product or service. More simply, the higher the price, the less the quantity demanded.

The reason for this is based on the opportunity cost of the good. Consumers will naturally avoid purchasing products and services that force them to give up another product or service they value more. For example, if you get R100 a week and usually spend R60 on food and use the other R40 on social activities, what would you decide to give up if you needed to purchase airtime for R30? Would you give up anything at all? What if you could only purchase R55 airtime because the R30 airtime was all sold out? Consumers make various decisions based on the opportunity cost of certain products and services, as well as their personal attitude towards the relationship between price and quality demanded.

Another good way to see this relationship is the concept of sales and discounts. Sometimes a lower price forces customers to purchase more of a certain product or service.

The Law of Supply
The law of supply illustrates the quantities that are offered for sale at a certain price.
It is, in essence, the opposite of the law of demand as the higher the price of the product or service, the greater the quantity supplied of that particular product or service. Producers are willing to offer or supply more products and services at a higher price as it offers greater revenues.

The Equilibrium Price and Quantity
Equilibrium price is determined when the demand and supply curves are joined and intersect at a specific point. It is at this point that the allocation of goods and services are at its most efficient. Here, the amounts of goods or services that are being demanded are the same as the amount of goods or services that are being supplied. This means that suppliers are selling all the goods or services being produced and consumers are obtaining all the products and services they are demanding.

Disequilibrium
This is a state where there is excess demand or excess supply.

Excess Supply occurs when the price is too high and not enough demand has occurred. Suppliers produce more in order to sell and increase profits; however those that consume the products or services end up consuming less due to the price increase making the product or service less attractive.
Excess Demand occurs when the price is set below the equilibrium price. This means that too many consumers demand the product or service while suppliers are not providing enough. This ends up

stabilising in the long run as the price will eventually increase due to the competition between consumers. This brings the price closer to the equilibrium.

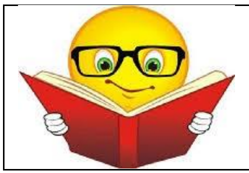
Changes in Demand and Supply
Changes in demand and supply can occur as movements or shifts occur in either the amount demanded and or supplied. Movements are changes that occur along the curve. For example, on a demand curve, a movement along the curve implies that the relationship of demand is consistent. This movement is generally due to changes in the price of the product or service affecting the price demanded. Similarly for supply where movements along the supply curve denote consistency in the supply relationship but the movement has occurred because of changes in the quantity supplied in relation to price changes. All other factors stay constant.
Shifts occur when the quantity demanded or supplied changes even though the price stays the same. This means that shifts occur due to changes in other factors, not price changes.

Demand curves are usually drawn on the theory that the following factors remain constant:
- ✓ Consumer's Tastes
- ✓ Consumer's Incomes
- ✓ Amount of consumer's in the market
- ✓ Prices of related products and services

If one of the above factors changed, a shift in the demand curve would result. An increase in wine consumers would increase the demand for wine, thus causing a shift.

Supply curve shifts are affected by changes in the following factors:
- ✓ Technology
- ✓ Input or Resource Prices

If a change occurred in the technology for producing wine, or the resource prices incurred in producing wine changed, there would be a change in the cost of producing wine and the supply curve would shift. These changes can either be positive changes or negative, either shifting the graph to the left or to the right.

	*Complete Activity in your Workbook*

1.3. PERFECT AND IMPERFECT COMPETITION

An economic system is "the way in which a country's economy is organised." (Le Roux, 1995, pg 8) There are many different economic systems in place around the world, and each system has different ways of solving economic problems such as the distribution of scarce resources. At one end of the economic system is the Communist Economic System, where the government takes control of economic problems. On the other end of the system is the Capitalist Economic System, where the economy is market-oriented and allows market forces to determine solutions to economic problems. These solutions are usually derived from forces of demand and supply. This is also known as a free-market system.

Communism
The idea behind communism lies in all assets belonging to the population. This system is controlled by the state and the consumer plays no role of importance in this system at all. Market mechanisms of demand and supply are virtually non-existent in this system, as the state decides what and how much should be produced.

Advantages of communism:
- ✓ Income is distributed more equally than in a free-market system.
- ✓ Due to the fact that the state controls the sharing of the economy, fluctuations are mostly eliminated.

Disadvantages of communism:
- ✓ It is difficult to obtain internal balances of supply and demand without using the pricing mechanism.
- ✓ It is difficult to implement.
- ✓ Consumer's needs are not considered.
- ✓ Freedom is restricted.
- ✓ Maximum productivity is undermined.

The Free-market System
In this system, factors of production (such as land, labour, capital and entrepreneur-ship) are owned by private individuals. The forces of demand and supply determine how resources are allocated without any government intervention.

In the market place, there are a large number of different buyers and sellers, thus creating competition that allows for changes in demand and supply. With so many varieties and substitutes, if one product becomes too expensive, a cheaper substitute can be chosen. This also allows equal ability for suppliers and consumers to influence price.

The competitive environment, in which these buyers and sellers operate, is known as the market structure. There are four types of market structure.
- ✓ Perfect Competition has a large number of buyers and sellers that make decisions and do not take the effect of their actions into account. This is due to the fact that individual economic units in perfect competition are small and are unrelated to other economic units. Their actions have no impact on other buyers and sellers.
- ✓ Monopoly is where a single organisation sells a product or service, but has no close substitutes. There is virtually no competition; however entry into this market is very difficult, almost impossible.
- ✓ Monopolistic Competition has many sellers of a differentiated product or service. Entry is easy in the long-run.
- ✓ Oligopoly has a few sellers of a differentiated product or service, or a homogenous good. Entry into this market is not very easy, but is possible.

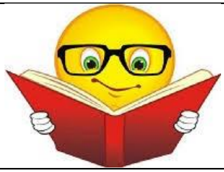
Monopoly, monopolistic competition and oligopoly are forms of **imperfect competition,** which exists due to the fact that entry into these markets is not necessarily easy. Few firms and businesses operate in these markets in order to gain maxi-mum control over the price of their goods and services. Consumers have little influence on the price of goods and services.

PERFECT COMPETITION

Perfect competition has many buyers and sellers that are too small to affect the price of a product or service. The product is usually homogenous and consumers use the price to help them decide whether to purchase. Resources are perfectly mobile and there is perfect general knowledge of the market conditions.

Perfect competition means that businesses and consumers will only exchange products and services if they both benefit from the trade. Voluntary exchange is maximized under perfect competition as output is increased until no consumers are willing to pay the opportunity cost of producing additional units of product or service. Resources are allocated efficiently to ensure that capital is being used at its highest value. For example, if the return in a competitive sector earns less than the normal rate, resources will leave the sector and be re-distributed until the remaining resources earn the normal rate of return again.

In perfect competition, production occurs at a minimum cost but this does not mean that it is more efficient than other market systems.

	*Complete Activity in your Workbook*

Why do businesses operate in competitive markets and how does this benefit consumers and the economy?

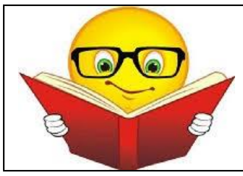
The labour government of South Africa deems competition as being beneficial for the economy as it is the main force behind productivity growth in the economy, and it encourages businesses to reduce slack and costs while providing incentives for more efficient production. Competition also helps consumers to get lower prices as well as a greater variety of products and services. Improvements to quality and customer service are also gains from market competition, as well as allowing consumers to make better informed choices. Using the knowledge you have gained on demand and supply from the previous chapter, as well as the knowledge from this chapter on competitive markets and economic system, you should be well on your way to grasping the basic concepts of economics.

Varying prices of the same product/service illustrating competition

The same product cost different amounts in different places. Take a 1 kg box of branded soap powder.

At a large chain store in the city it may cost R 20. At the cafe around the comer the same pack may cost R 23-00 while at the 24-hour convenient store it will be R 28-00, while at the spaza store down the road it may be R25-00. Oh yes, and at Makro it may cost R 17-00 a pack, but then you have to take four! Each of the shops has a unique competitive advantage, which ensures that the price asked is the most optimal for that particular market. If the above prices were the actual prevailing prices over a given period, can you think what would happen if anyone of them would double their prices?

Yes, people would buy the product at the other outlets. Relatively small (but significant) differences will be tolerated by consumers, but outside a given range they will switch to another shop. Competition ensures that prices stay within a given range.

	*Complete Activity in your Workbook*

1.4. THE ADVANTAGES AND DISADVANTAGES OF COMPETITION

The advantages are simple - it elicits the best performance from all role players. As said previously it is the mainspring for improved products leading to a higher standard of living for all. The disadvantages are that it is unforgiving - if you don't improve you lose out.

Advantages

The principle advantage is efficient allocation of resources. When many suppliers compete for the business of consumers, prices gravitate toward costs of production and scarce resources are used for those goods and services for which there is real demand. Competition thereby produces maximum economic value from given resources, and uses minimum resources to supply a given demand.

Competition helps to bring perfection. In an industry where there is intense competition, often, there is a tendency that that industry would become more and more perfect and efficient. This happens because competition shifters out the poor performing products or services and leaves only good and outstanding products for the general masses to consume. This particular advantage of competition is more likely to benefit the general population, since they would have better quality products and services for maybe cheaper prices.

A good case study is the internet marketing industry. Some years back when internet marketing was not so popular, there were lots of jerks making easy money from the internet. But today, the competition is intense... I mean so intense, and you would notice that making money in this industry has become a nightmare. You need to have an IQ above average to make money online.

Disadvantages

Competition benefits the companies that are already well established and are functioning well in a given industry. Competition is a very big barrier to entry in all industries, including the internet marketing industry. If you are already profiting from the internet, then be rest assured that someone trying to start profiting like you is having really hard times to make it. This is some kind of comfort to you since you know people would not want to come in this industry because of its competitive nature. People prefer niches where there is little of no competition so they could make easy money.

The possibilities of conducing economic and business disorder

It may lead to vicious actions such as:

- ✓ False transaction
- ✓ Business bribes
- ✓ False advertisement
- ✓ Invasion of business secrets
- ✓ Baleful goodwill denigrating behaviors.

Another disadvantage of competition can be the loss of local jobs, particularly in the manufacturing industry. As competition pushes prices of goods down firms may move offshore in search of cheaper labour in order to stay competitive. This can lead to some firms exploiting people in less developed countries and in extreme cases even child and or slave labour. Some industries do not lend themselves to competition. The main example commonly used is the supply of water to residential homes. It does not make sense to have multiple sets of pipes running to each home. In an industry such as this it is cheaper to have a monopoly firm, regulated by government to insure fair price and a minimal level of service.

1.5. ECONOMIC ACTIVITY

The business cycle
The business cycle is a model of alternating rises and declines in economic activity. These fluctuations are not of specific variables, but are taken as an aggregate of the economic activity of a country.

There are four phases in a business cycle.

- ✓ **Peak:** Is where the economy reaches a maximum in the economic activity. This is temporary.
- ✓ **Recession:** Otherwise known as a contraction, is a period of decline, brought about by decline in total output, income, employment and trade.
- ✓ **Trough:** Is a temporary minimum in economic activity
- ✓ **Recovery:** Or expansion is brought about through a period where output and employment are rising.

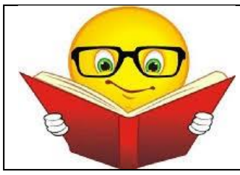
The above phases do not occur at regular fixed intervals and are not periodic. The business cycle is recurrent and persistent. In most cases, declines are followed by more declines. Similarly for growth periods, thus it is important to predict and forecast turning points in a business cycle.

Predicting movements and changes in a business cycle helps the entrepreneur to predict the spending needs of the economy. In a period of recession, the spending will be lower when compared to spending in a period of expansion. Recession periods influence the durable and capital goods more as people continue using their older goods without looking to replace them with new ones. Non-durables and services are less affected as it is often difficult to cut back on these items.

There are a few reasons for changes in business cycles.

- ✓ Firstly, innovations can cause an expansion due to the shock created in the economy. An example of this is the microchip.

- ✓ Secondly, productivity influences the economy in a similar way. If productivity expands, so too does the economy. If the productivity levels decline, this will negatively affect the level of economy.
- ✓ Thirdly, too much money causes an expansion which allows a greater amount to be spent. Too little money causes a recession.
- ✓ Lastly, total spending can change and affect the business cycle as well. If the total spending increased, the economy would expand. A decrease in total spending would contract or decrease the economy.

	*Complete Activity in your Workbook*

1.6. INFLATION

It is the persistent and appreciable increase in the general price level.

An important aspect to remember from this definition is that inflation is an increase in the general level of prices. Changes in prices of individual goods and services are not considered inflation.

Inflation is usually measured with the annual percentage increase of a CPI, otherwise known as a consumer price index. There are other methods that can be used, but this method is generally preferable.

Let us take a brief look at South Africa's inflation history as recorded by Dornbusch in his book, Macro-economics.

From 1923 to around 1939 there was no evidence of a sustained increase in the level of prices. This period was actually linked with the period of a sustained **decrease** in the general prices due to the Great Depression of 1929 till around 1933. This was labeled as a period of no inflation. A period of low inflation naturally followed between 1946 and 1972. This had positive but low rates of inflation and a tendency to decline during phases of recession in the business cycle.

Since 1973 inflation has been significantly high in South Africa, where annual rates were persistently high and stable. The inflation rate also showed little sensitivity to the changes in economic activity. Due to the current state of South Africa's inflation, a distinction needs to be made between cyclical and structural components of inflation.

There are four approaches or views on inflation.

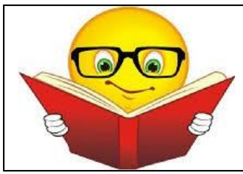
- ✓ **The Monetarist Approach** views inflation in the sense that sustained high rates of monetary growth cause high inflation and low rates of monetary growth will eventually produce low inflation.

- ✓ **The Keynesian Approach** is based on the distinction between demand-pull and cost-push inflation. Demand-pull inflation occurs when the demand curve shifts to the right due to increases in the price level as well as increases in real output. Cost-push inflation occurs when the supply curve shifts to the left due to increases in the price level as well as a decrease in the level of output.
  If this is used with the Philips model, demand-pull inflation occurs when there is an upward movement along a downward sloping Phillips curve. This in-crease in inflation is accompanied by a decrease in the unemployment rate. Cost-push occurs on the Phillips curve when it shifts to the right accompanied by an increase in the unemployment rate.

- ✓ **The Structuralist Approach** involves the distinction between three sets of factors in the inflation process.

- ✓ **The Conflict Approach** is not bothered with the details of the inflationary process but focuses on the fundamental causes of inflation.

As an entrepreneur you should learn to anticipate and consider inflation in all business activity. This will ensure you are not hurt by unanticipated inflation and the value of your money does not decrease.

	*Complete Activity in your Workbook*

1.7. FOREIGN CURRENCY & EXCHANGE RATES

Exchange rates are the price of one currency in terms of another currency, and allow comparisons of international prices of goods and services.
Foreign currency is a monetary value in another country. If you travel a lot, you should be very familiar with these terms. For example, if you travel to America from South Africa you will already know that your South African currency is Rands. Your foreign currency for America is the Dollar. You will receive a certain amount of Dollars for the amount you are willing to exchange according to the exchange rate. If you require $100 (one hundred dollars), this will be compared to the current exchange rate for dollars and rands. You will then be required to pay an amount for that $100.

This is important for entrepreneurs who are competing internationally, or who want to set a comparative price for their products or services.
The foreign exchange market is the market in which foreign currencies are exchanged. There are different mechanisms used in determining the exchange rate. These are:

- ✓ Floating rate system where the exchange rate is determined directly by market forces and will fluctuate continually due to changing market conditions
- ✓ Fixed rate system where authorities attempt to regulate the exchange rate at some appropriate level.

INTEREST RATES

This is the rate charged for the use of money and is an annual rate

It also tends to rise with inflation. Interest rates work in two ways. Firstly, if you need to purchase furniture for your new home, you may decide to take a loan. You will be required to pay back this loan over a period of months and you will be required to pay interest over these months for the money you have borrowed.

Secondly, you may invest money in a bank account. You are in actual fact allowing the bank to utilise your money until you need it. This means the bank pays you interest according to the interest rate of your savings account.

GROSS DOMESTIC PRODUCT (GDP)

This is the total value of products and services produced by a country. South Africa's GDP will be the total of products and services produced within South African borders. Products from foreign countries will not be included in the GDP for South Africa. This figure is used to calculate various economic equations and indicates how effective the country's economic efficiency is.

Balance of payments

This is in essence an accounting system for economic transactions between the government and the residents of a country. It records financial transactions between a country and the rest of the world in a period of a year. South Africa is a country that is dualistic in nature and has both first world and third world components. Some parts of the economic system are developed while other parts are not. South Africa is considered as a developed country due to its GDP, infrastructure, industrial development and technological development. However, due to unemployment, division of income, low productivity and population growth, SA is regarded as an underdeveloped country.

As an entrepreneur you will be faced with the many faces of the South African economy and business. If you grow your business and decide to trade internationally, you will need to understand your international market just as well. For now, you may want to concentrate on reading about and understanding the various in-depth aspects of the South African economy and business economics in general. There are plenty of books and publications that will provide you with this knowledge. Through reading and understanding you will research and identify areas where your business will perform well.

The socio-economic factors that underline the importance of new ventures

Poverty is a major socio-economic issue all over the world. It has various manifestations, including the following:

- ✓ lack of income and productive resources sufficient to ensure sustainable livelihoods
- ✓ hunger and malnutrition
- ✓ ill health
- ✓ limited or lack of education and other basic services
- ✓ increased morbidity and morality from illness; homelessness and inadequate housing
- ✓ unsafe environments
- ✓ social discrimination

The alleviation of poverty is one of the national and international priorities for achieving sustainable development. Among all population groups, urbanization has lead to the decline in the importance of the extended family and the emerge of the nuclear family.

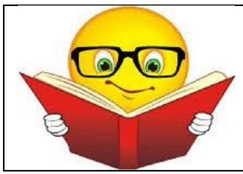
A number of South African sociological studies have investigated the existence of a great variation in family structures and the term household is usually preferred as the unit for social analysis.

A further development is the growing number of single parent families among all population groups. With a growing population, the emergence of smaller households' means that the number of households must be increasing, this in turn will increase consumption. Migrant labour is a further factor in the social and environmental pressures in South Africa. Labour for the South African mines and industries were mostly drawn from remote rural areas. Families remained in areas designated to them. Woman and children has to depend on the small income that was send "home" every month. If woman can be empowered to start their own ventures it would bring food to the table in many instances.

Growth sectors that exist in South Africa

Currently the following has been identified as growing industries in South Africa:

- ✓ Travel
- ✓ Transport
- ✓ Consulting
- ✓ Education
- ✓ Repairs and maintenance
- ✓ Technology
- ✓ Toys
- ✓ Personal Services
- ✓ Tourism
- ✓ Security
- ✓ Accommodation
- ✓ Health care
- ✓ Second Hand Trade
- ✓ On-line shopping
- ✓ Entertainment
- ✓ Mail ordering
- ✓ Information
- ✓ International Trade

	*Complete Activity in your Workbook*

LEARNING UNIT 2: Costing and Pricing

Learning Outcomes:

By the end of this unit, you will be able to:

- ✓ **Identify and apply the criteria of a price setting policy for a new venture**
- ✓ **Identify and analyse internal and external factors that impact upon pricing decisions**
- ✓ **Demonstrate an understanding of the relationship between costs, revenue and profits**

2.1. CRITERIA OF A PRICE SETTING POLICY FOR A NEW VENTURE

Pricing is an important function in any business. A price is an amount that is expected in return for a product or service. This price can change at any stage and is affected by a number of factors. These need to be taken into account, as well as costing methods, in order to arrive at a price that is fair to the consumer and to the seller.
This unit will attempt to familiarise you with terms relating to the costing and pricing methods. It will discuss various pricing methods as well as factors that influence and affect price. It will take an in-depth look at pricing strategies, as well as the steps to take in costing and pricing.

What is pricing?

Pricing is a decision, made by the entrepreneur or business owner, on the amount to be charged for a particular product or service provided by the business. This is a formal decision, which is made by analysing the costs involved in providing that particular product or service, and taking into consideration the external and internal factors.
Costing is the process of analysing the costs involved in providing the product or service, and can differ in method from business to business. Tendering is your final offer or decision made on the price of the product or service, taking into account the costing and pricing processes. Your offer, or tender of price, is either made to direct consumers, or to businesses that will use your product or service in their production cycle. The tender, or price, is regarded by these buyers, as a cost.

An example to help us understand the relationship between these concepts can be as follows:
I own a farm, on which I have fields of wheat. I decide to sell my wheat to you, the local miller. You will mill my wheat into flour and will sell this flour to a baker. I perform a costing analysis, which helps me decide on a mark-up percentage for my pricing decision. After determining my price, I offer (or tender) this price to you. You decide to accept this price and pay me when I deliver the wheat to you. After you have milled the wheat, you approach the baker to purchase this wheat from you. My tender price is regarded as a cost for you, and you take this into consideration when you perform the costing analysis to help you determine your selling price. Once you have determined your pricing method, you offer this to the baker, who accepts. The baker buys your flour and bakes it into bread. When the baker performs a costing analysis, he will consider your tender price to be a cost to him. Once he has decided on a pricing method and a cost per loaf, this is offered to the consumers, who consider his tender price, as a cost to them.

As you can see, this costing and pricing method works its way down the supply chain, and in some cases can become quite complicated. The costing and pricing strategies will be discussed in more detail, but first we will need to understand a few concepts.

Fixed costs and Variable costs
Let us take a look at the difference between fixed costs and variable costs. Fixed costs are those costs that do not change according to the production or sales levels. These costs will be incurred

each month, regardless of whether you produce any products or sell any services.

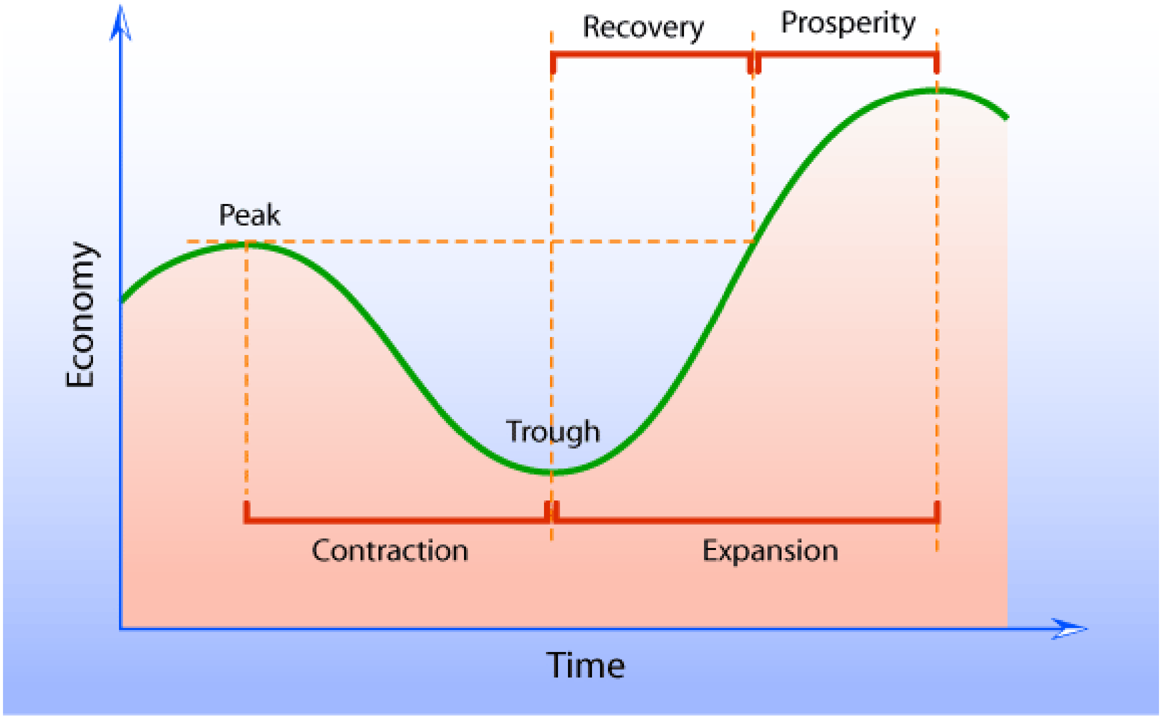
However, it is important to remember that even though fixed costs are said to remain constant, this does not mean that the amount you have planned for cannot change from year to year. Fixed costs simply will not be affected by the amount of production. These are costs such as salaries, rent and property taxes and depreciation.

Variable costs change directly with the production level or output of the business. These are costs such as raw material costs and labour, used in manufacturing. Mixed costs are a bit of both. You can expect a certain cost, regardless of the production level, however these costs will change as the productivity level changes. Examples of mixed costs are maintenance or wages of a salesperson who also receives commission. These are not extremely common, so we will concentrate on fixed and variable costs.

Total costs are the sum of fixed and variable costs and (where applicable) mixed costs. Total cost will be discussed further in the costing and pricing methods. It is important that you grasp these basic definitions.

The effect of the trading cycle

Before we move on to discuss pricing strategies in more detail, it is important for you to understand the effects of a trading cycle, otherwise known as a business cycle, on price. You may remember from your studies on economic activity and market mechanisms. A business cycle relates to the level of economic activity, which results in alternating rises and declines. This cycle is produced by fluctuations in economic activity and not fluctuations in one specific variable. This cycle is also divided into various phases, as seen in the diagram.



- ✓ A **peak** is a temporary maximum in economic activity.
- ✓ A **recession** is otherwise known as a contraction and is a period of decline in factors of economic activity, such as employment, income and trade.
- ✓ A **trough** is a period when the economy reaches a temporary minimum in economic activity.
- ✓ A **recovery** is otherwise known as an expansion and is a period where economic activity, such as output and employment, are rising.

A business owner should always take note of the phase through which the economy is moving. Each phase of the trading cycle has certain influences on the growth and continued existence of the business. Thus it is good to predict the movements in the trading cycle in order to predict how the spending habits of consumers will be affected.
During the prosperity or peak phase, the business has the opportunity to produce and market new products and services. This allows the business to explore new markets and expand its market share.

During a period of recession, consumers' disposable incomes are less and they therefore spend less. This decreases the demand for products and services and hinders the growth of a business. However, non-durables and services are not affected as much during this period as people often find it difficult to cut back on the items they believe to be necessities. The recovery phase is where economic growth will begin to take place, and businesses should prepare for this. Businesses should begin to research and develop new products and services and identify methods to increase sales and incomes levels.

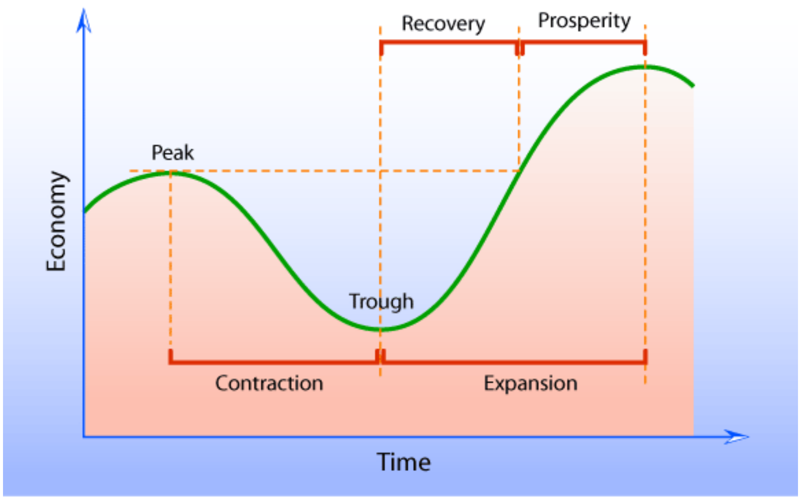
It is important to not that the patterns of trading cycles are recurrent but are not periodic. In other words, they do not occur at regular, fixed intervals. Periods of decline are often followed by further periods of decline and periods of growth are usually followed by additional periods of growth. Therefore, predicting turning points in the trading cycle are very important for economists and

business owners alike.
Business or trading cycles are caused by a number of factors.

These are:

- ✓ Innovations, which usually cause an expansion. An example of this is the microchip, which shocked the economy into an expansion.
- ✓ Increasing productivity, which expands the economy. If productivity declines, the economy and trading cycle will begin to decline.
- ✓ An increase in money, which causes an expansion. Too little money in the economy can cause a recession.
- ✓ Changes in market spending. As spending increases, the economy expands and as spending decreases, the economy will enter a period of recession.

More on this topic and other economic indicators for business owners will be discussed in the market mechanism course. It is highly beneficial to familiarise yourself with basic economics and to keep up to date with changes in the economy and the business environment.



2.2. FACTORS THAT IMPACT UPON PRICING DECISIONS

Pricing Objectives

Pricing objectives are decided upon by various members in the business. The business owner will take into consideration the pricing objectives of different departments before a final decision is made. For example, the marketing department may have a completely different pricing objective to the production department, and thus a compromise will be negotiated for the benefit of the business. This means that the pricing objective needs to correspond with the overall objectives of the business and its departments. Below are a few common pricing objectives, discussed in detail.

Survival

In this situation, the business decides to set its prices below those prices of its competitors in order to increase sales while covering costs, even if this means that the profits may decrease in the short term. Survival is often the main objective of any business. If the business is in a market with intense competitors, survival may be the chosen pricing objective. However, this is a short-run objective and the business will need to move on to a more profit-focused objective in order for it to survive in the long run.

Profit

Profit maximisation is often objective of many businesses, however if the business sets out to use this objective without considering the consumer, it may soon discover difficulties in this objective. This objective should be decided upon by estimating the demand and associated costs to produce the product or service. However it is not easy to correctly estimate these. This objective should be focused on in the long term in order to establish a solid consumer base on which the business can expand and maximize profits in the future.

Return on Investment

This objective needs to take certain aspects into account, such as the cost of producing a certain product or service as opposed to using the amount of money for an alternative use, such as investing in shares or on the stock exchange or starting another type of business. The return from these options helps the business owner to decide which option is the most viable.

Market Share

The businesses market share, which is the sales of the business compared to the industry as a whole, is an important objective. The belief in maximising market share is that higher sales volumes will lead to lower costs and higher long-term profits. This is also known as market penetration pricing. Here, a business will ask a lower price for its product or service while emphasizing the qualities of its product or service. This should win a large market share, which will decrease the costs involved for the business, which allows them to offer an even lower price in the long run.

Product Quality

This objective is based on the business striving to be the quality leader in its field. It is important to note that producing a high quality product or service goes hand-in-hand with high manufacturing costs and additional costs for research and development.

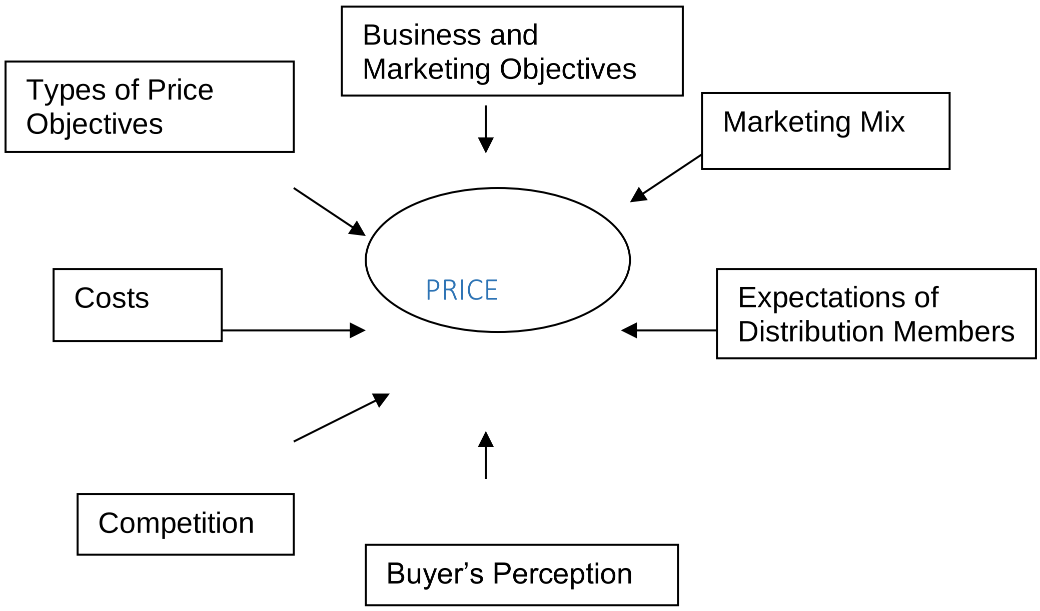
MAXIMUM MARKET SKIMMING

This objective is achieved by offering your product or service at a very high price where only a hand full of consumers can afford your product or service. Here, consumers perceive your product to be of a superior quality due to the high price, and decide that they cannot wait for the price to drop before obtaining the product or service.

As competitors introduce similar products or services and initial sales volumes drop, the price is decreased to attract other consumers. From this objective, the maximum amount of money is skimmed from the different spending segments in the market.
By using a specific pricing objective, or even taking these into account, businesses will be more successful than if they allow the market or costs determine their pricing strategy.

FACTORS INFLUENCING PRICING DECISIONS

These are various factors that influence the base price of a product or service. A base price is a price of one unit of a product at its point of production before allowance for other costs such as delivery charges or discounts. These factors are:



Business and Marketing Objectives

Business and marketing objectives, as well as other department objectives, need to be taken into account when determining a pricing objective.

Marketing Mix Variables

Price will also be affected by elements of the marketing mix. The product or service and its end user need to be taken into account. Other product elements that need to be considered are whether the product can be a hired elsewhere, or traded in. Distribution channels and middlemen will also influence the price. Promotional methods can affect price as well, for example, if a retailer takes responsibility for promoting the product, the retailer will pay a lower price for the product than if the manufacturer had to promote the product.

Expectations of Distribution Members

You will need to understand the expectations of members distributing your products. These members may provide certain services in exchange for a certain profit.

This amount of profit expected by the distribution members will influence your pricing. Other expectations could be large discounts on bulk orders and training for promoters.

Buyers Perception

Price can be more important for certain consumers than for others. This differs in the market segments and this should be taken into account when setting a price strategy.

Competition

Competitor's prices should always be taken into consideration. Prices should be adjusted according to competing products and services; however they do not need to be the same. For example, in the airline business, it is important to set prices according to competitor's prices in order to survive.

Costs

All costs need to be taken into consideration in order for the total cost of producing the product or service to be covered by the decided upon price.

Types of Pricing Objectives

Pricing objectives were discussed earlier and these definitely need to be taken into account. An example of this would be if the pricing objective is to increase market share. The business could decrease prices in the short term in order to increase market share.

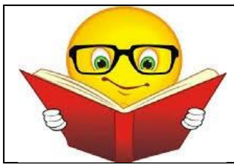
The abovementioned factors can be divided into external and internal factors that need to be considered.

Internal factors are:

- ✓ The costs
- ✓ The pricing objectives
- ✓ The business and marketing objectives

External factors are:

- ✓ The channels of distribution
- ✓ Competitors
- ✓ Customers and consumer perception
- ✓ Marketing mix factors

	*Complete Activity in your Workbook*

2.3. BASIC PRICING METHODS

We are now going to discuss how you, as a business owner, will go about setting a price for your product or service, taking the pricing objectives and costs into account. We will discuss the following methods:

1. Cost as a basis for pricing
2. Demand as a basis for pricing
3. Competition as basis for pricing
4. A combination of the above

Cost as a basis for pricing

An advantage of this method is that it almost guarantees a profit and gives clear guidelines for price fixing. A disadvantage of this method is that market conditions, competition and other factors are usually not considered. Cost-plus pricing and break-even point are taken into account. Also, it is not always possible to determine production costs.

Cost-plus pricing is where the price is based on the total cost of producing the product or service plus a percentage of profit added on to this cost.Firstly an estimate is made of the number of units needed to be supplied, and then the variable and fixed costs are calculated. A predetermined profit is added onto these costs to decide on the end price.

This is the formula used:

$$\text{PRICE} = \frac{\text{Final cost + Total Variable Cost + Estimated Profit}}{\text{Units Supplied}}$$

Break-even point is the quantity at which the sales revenue equals the total cost at a certain selling price. This means that there is a different break-even point for each different selling price. If larger quantities are sold above the break-even point, a profit will result. Sales below this point will be a loss.

Break-even will indicate the impact of your decision. Let us take a look at an example.

The fixed cost per unit manufactured remains the same regardless of the quantity produced. Let us say this fixed cost is R250.

The variable cost per unit is R30 and increases with the number of units produced.

If the business sells 5 units, and the selling price is R80, their revenue is R400.
Their costs are R400, which are Variable Costs – 5 x R30 = R150
Fixed Cost = R200

By selling these five units, the costs equal the revenue and the break-even point is attained. On a graph the break-even point is shown below.

DEMAND AS A BASIS FOR PRICING
Here, the demand for the product is taken into consideration, and this requires consumer research to determine the quantities that will be purchased at differing prices. This can be shown on a demand curve. There will be a different level of demand for each price and there is usually an inverse relationship between the price and level of demand. In other words, at higher prices, lower quantities of product or service are demanded. This is not always true, especially if the consumer interprets the higher price as a more exclusive product or service.

A disadvantage of this pricing method is that attitudes and personalities of consumers cannot always be determined and their personal income can affect demand. Also, the consumer could choose a competitor's product or service as a replacement for your product. This influence is not always taken into account.

COMPETITION AS A BASIS FOR PRICING
For this strategy, neither cost nor demands are used. Competitors pricing strategies are taken into consideration, as well as the business image, customers and other elements of the marketing mix. The decision will be made to either fix the price above, below or equal to the competitors' price.

An advantage of this method is that a comparison is made between the competitors' products and services and the businesses products and services. Any advantages can be highlighted to consumers and used as a competitive advantage. However, it is important to remember that competitors can easily adjust their prices and competing products may have features that cannot be compared to your business products.

A combination of the above
By using a combination of the above, many disadvantages will be excluded and all factors will be considered.

Price Adjustments:
Once you have decided on a price, you can still make certain adjustments. These adjustments must be determined in advance, such as discounts allowed to certain customers or whether any transportation costs for delivery of goods will be paid by the business or added on to the price. Let us take a brief overview of various price strategies and then discuss price adjustments.

One-price and Variable-price:

In a one-price strategy, all the buyers pay the same price for the product. There are no price adjustments for different buyers. A variable-price strategy is where the same product is offered at different prices to different buyers. With this strategy, the seller can adjust the price for different buyers. For example, if a regular customer is buying in bulk, a discount will be granted to lower the price and retain the customer.

Cream-skimming and Market Penetration:

Cream–skimming is where the product is introduced at a higher price into the market. Once the product has gained demand from the market that view the product as being superior due to its high price, the price is usually reduced to attract the people that were less willing to pay such a high price for the product.

Market penetration is the opposite of cream-skimming. The product or service is introduced to the market at a lower price, usually called an introductory offer.

Psychological Pricing Strategies:

These strategies are usually used to stimulate sales using small adjustments to the price. These are:

Odd Pricing

Here, the price is indicated as an odd price, such as R299.99, rather than R300. The buyer perceives the product to be in the R200 range and not in the R300 price range.

Price Lining

Retailers often use this strategy, where they select a limited number of prices at which to sell the merchandise.

The supplier however, will sell the goods to the retailer at much the same price. For example, if the supplier sold sunglasses, they would all cost the same price, but there would be different styles.

Leader Pricing

Here, retailers use leader prices which lead the customer to believe that it is a true saving. The belief here is that customers will come to the store to purchase the advertised marked-down product, but will also purchase other regularly priced goods. A disadvantage of this is that if retailers are not cautious, a particular good may obtain a low-price image. Retailers should therefore rotate the products used in this strategy.

Prestige Pricing
By fixing high prices, especially to goods such as jewellery, perfume and various cars, consumers perceive the goods to be of a superior quality and will pay these high prices for the prestige of owning the product.

Geographic Pricing
Here the transport costs involved in delivering the product to the buyer are taken into consideration. Transport costs form a large part of variable costs and there are different options to make provision for transport costs in your price.

Free-on-board Price
Here the price does not include the transportation costs, and these must be covered by the buyer. The price received by the business remains the same, but the price differs for each customer.

Uniform Delivered Pricing
With this strategy, the transportation costs are shared by both parties.

Delivered Pricing
The price quoted to the customer includes the cost of transportation.

Unit Pricing
This is often used for goods such as meat or cheese. It is often difficult to compare the prices of the same products if they are in different packaging sizes. Here, two prices appear on the label. The first is a price for the actual good, and the other is the price charged per unit, weight or volume.

Discounts and Allowances
Discounts are deductions from the price, given as a reward to buyers for loyal service or any other activities to the products advantage, such as bulk buying.

Trade Discounts
These are reductions from the price for marketing functions performed by members of the trade or distribution channels, for example a retailer. These discounts are adjusted for different channels as there are usually different services rendered.

Quantity Discounts
These are used to encourage the buyer to purchase in bulk. The discount should not exceed the cost advantage obtained through the sale of large quantities.

Cash Discounts
For clients that settle their accounts in good time, or pay in cash where they could choose another form of payment, a cash discount is usually granted to them.

Seasonal Discounts
This discount is usually used for goods or services that are demanded and bought during a particular season. Airlines make use of this during their low season. Discounts are also used to encourage the use of late-night bus rides.

Promotional Allowances
These allowances are granted for promotional services. For example, if a retailer exhibits a certain product in a prominent place in comparison to those products of competitors, the buyer receives a number of goods free of charge.

To conclude, let us take a look at the steps you will need to follow to set a price for your product or service.

STEPS IN PRICING
These steps do not all have to be followed strictly. They can be adapted to your pricing objective and pricing needs.

Step 1: Determine Pricing Objectives.

Step 2: Analyse the Target Market
Here you will need to obtain vital information on your target market. Information on their purchasing power and buying attitudes or perceptions will help you to determine the correct price to set.

Step 3: Determine the Demand.
Market research will help to give you an indication of the demand for your product or service and the quantity that can be purchased within a specified period. This will help you to determine the ratio between the price and quantities required.

Step 4: Analyse Costs.
In order for the product or service to be sold at a profit, costs need to be taken into consideration. Here the break-even point is often used as an indicator.

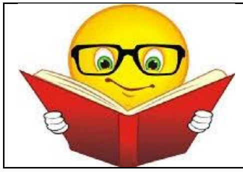
Step 5: Evaluate Competitors Prices.
If you are aware of competitor's prices, you will be in a more suitable position to set your own prices. Market research is often used to keep up-to-date with competitors' pricing strategies.

Step 6: Develop a Pricing Method
All the above information will help you to complete this step.

Step 7: Determine a Price Strategy and Adjustments.
Determine whether you will focus on a specific strategy or a combination of various strategies. Also consider how you will make pricing adjustments.

Step 8: Finalise the Price.
That's It! Be aware that once you have finalized a price, it is not set in stone.

The price may change a number of times. Just remember that your adjustments need to coincide with your pricing objectives, and all factors need to be considered. Let us move on to discuss costing and its use in pricing. We have already touched on this earlier in the chapter, but we will now look at costing in more detail.

	*Complete Activity in your Workbook*

2.4. RELATIONSHIP BETWEEN COSTS, REVENUE AND PROFITS

A distinction between types of profit
Consider the following quote by Milton Friedman regarding business firms, social responsibility and profit:

"There is one and only one social responsibility of business - to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition, without deception or fraud."

More about Profit:

Economists recognise a distinction between two levels or types of profit - normal profit and pure profit (economic rent):

Normal Profit: That return necessary to attract and maintain entrepreneurial participation in some economic activity

Pure Profit (economic rent): Return greater than normal profit

Why is a firm profitable?

Profit is a natural outcome of success in meeting the wants of someone. A firm is potentially profitable if, and only if, it produces a product or service valued by consumers. One would not expect profits for the production of broccoli-flavoured ice cream.

Costing
In a previous section we discussed pricing methods for a business. When decisions are made on pricing methods, we mentioned costing analysis taking place (STEP 4). This chapter will discuss costing analysis in more detail. Costing differs for different types of businesses, so we will discuss this analysis in a manufacturing business, a retail business and a service provider.

Factors that influence costing analysis are:

- ✓ The capacity of products or services you can produce.
- ✓ Your fixed expenses and variable expenses.
- ✓ The profit you require to make on your product or service.

Let us briefly review various kinds of costs before we discuss the costing methods.

- ✓ **Fixed Costs** are costs such as rent, wages and salaries and property taxes. These remain constant regardless of the units produced. Even if there is no production at all, these costs will continue, however these costs can change slightly in the long run, such as an increase in rent.
- ✓ **Total Fixed Costs** are the sum of all the fixed costs.
- ✓ **Average Fixed Costs** can be calculated by dividing the total fixed costs by the number of units produced.
- ✓ **Variable Costs** such as labour and raw materials can be directly related to the production level. These can be controlled by changing the level of production. If there is no production, the variable costs are zero.
- ✓ **Total Variable Costs** are the sum of all variable costs.
- ✓ **Average Variable Costs** can be calculated by dividing the total variable costs by the number of units produced. Usually, the average variable costs are high for the initial units produced, but these decrease as production increases. This is due to the businesses receiving discounts on larger quantities of raw materials and a higher, more efficient use of labour. However, if this production level continues to increase, it can reach a turning point where average variable costs begin to increase. This is due to factors such as overtime payments and a less efficient use of production facilities.
- ✓ **Total Cost** is calculated by adding the total fixed costs amount to the total variable cost amount.
- ✓ **Average Total Cost** takes the total cost amount and divides it by the number of units produced.
- ✓ **Marginal Cost** is the cost of producing and selling one more unit.

COST ANALYSIS FOR A MANUFACTURING BUSINESS.

There are various steps you will need to follow to analyse the costs of a manufacturing business. Firstly you will need to determine your fixed costs and fixed expenses. These should not change much from month to month, but may change slightly such as an increase in rent or light and water payments. These payments have to be paid each month regardless of the amount your business produces or sells.

A brief list of these expenses could look similar to this:

- ✓ Electricity and Water
- ✓ Telephone
- ✓ Office Stationery
- ✓ Insurance
- ✓ Salaries
- ✓ Repairs and Maintenance
- ✓ Rent

If your business has not yet started producing products, and you are only starting out, you will need to try and estimate these fixed costs as accurately as possible. From this calculation you will need to calculate the average fixed expenses per product you produce.

After this calculation you will move on to calculate your variable expenses, which are the actual costs to produce the product. These costs can be the labour and raw material used to produce the product, or a more indirect cost such as transportation.

Using the above calculations, you will now need to determine the minimum amount you could sell your product at. As you are obviously in the business to make a profit, you will have to add on a mark-up to determine your offer or selling price. Your mark-up will be determined by an analysis of you break-even point, the competitiveness in your industry and your pricing decisions on factors such as whether your product is a luxury or a necessity.

To calculate your break-even point you will need to divide your total fixed costs by the selling price less average variable expenses. In other words,

$$\text{Break-even Point} = \frac{\text{Total Fixed Costs}}{\text{Selling Price} - \text{Average Variable Costs}}$$

This point indicates the number of units needed to be produced and sold in order to cover the total monthly expenses. As mentioned before, when the volume of production increases; the cost to produce the units decreases. This can be seen in the graph.

From here you will make a pricing decision using an analysis of your break-even point and cost analysis.

Cost analysis for a retail business

Your first step here is to calculate the cost of sales of the product you would like to resell. This is usually the price you pay to the manufacturer or supplier for the product in question. After this calculation, you will need to determine the variable expenses percentage and the fixed expenses percentage. The following are the formula's to be used for this calculation.

(Variable Expenses) ÷ (Cost of Sales) x 100 = Variable Expenses %
(Fixed Expenses) ÷ (Cost of Sales) x 100 = Fixed Expenses %

These percentages can be used to calculate the true cost of a product for a retailer. Let us take a look at a brief example.

John opens a retail store selling couches and other lounge furniture. John would like to calculate the minimum amount he can sell a lounge suite and has taken the following into consideration:

- ✓ John pays a 10% commission to his employees for every lounge suite sold.
- ✓ John expects to have a total sales of R100 000 per month.

- ✓ His cost of sales has been calculated to be R50 000 and his fixed expenses are expected to be R20 000 per month.

John asked you to perform your costing calculations on a lounge couch he has purchased for R1000 and intends to sell for R2000.

(Variable Expenses) ÷ (Cost of Sales) x 100 = Variable Expenses %
R10 000 ÷ R50 000 x 100 = 20%

(Fixed Expenses) ÷ (Cost of Sales) x 100 = Fixed Expenses %

R20 000 ÷ R50 000 x 100 = 40%

To use these percentages, you take the cost of the lounge couch, which is R1000 and perform the following:

Cost of the Couch	R1000
Commission	R200 (R2000 x 10%)
Fixed Expenses	R400 (R1000 x 40%)
TOTAL COST	R1600.00

This can be used to determine whether R2000 is a fair enough price to ask for the couch. Remember, you may end up giving a discount to a few customers, so your mark-up should be enough so that you can still make a profit on the goods you sell with a discount.

Cost analysis for a service provider
Your first step in this situation is to determine the number of hours you intend to work and charge for each month. If you are training consultant and have decided that you can only work for 5 hours per day and 20 days a month, multiply these together to obtain the number of hours you intend to work per month. That is 100 hours per month taking public holidays into consideration etc.

Next you will need to determine your total expenses including a salary for yourself. Your expense list could be as follows:

- ✓ Rental R1000
- ✓ Accounting Fees R400
- ✓ Stationery R350
- ✓ Other Expenses R2000
- ✓ TOTAL R7750.00

Using this total, you can determine a minimum hourly rate for you to charge.

Minimum Hourly Charge = Total Expenses ÷ Number of Charge Hours

R7750.00 ÷ 100 Hours

R77.50

To calculate your selling price, you will need to perform market research to determine the acceptable range of charges your competitors are using. You will need to perform price comparisons before you can determine or settle on your selling price.

Your mark-up percentage can be calculated using the following formula:

(Selling Price – Cost Price) ÷ (Cost Price) x 100

Your gross profit percentage can be calculated as follows:

(Selling Price – Cost Price) ÷ (Selling Price) x 100

If your training costs you R77.50 an hour and you charge R200 an hour…

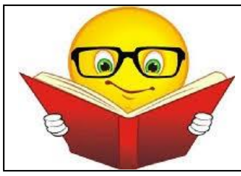
Your mark-up % = (R200 – R77.50) ÷ (R77.50) x 100 = **158%**

Gross Profit % = (R200 – R77.50) ÷ (R200) x 100 = **61%**

Now that you have analysed and calculated a few costing ratios, you should have a better understanding in costing. This can now be used in your pricing methods. It may be beneficial for you to go back to chapter 1 and review what you learnt from this chapter. It may make a bit more sense. When you are analysing competitors' costs, keep in mind you should have already analysed competitors' products and services as well as costs in your business plan. Take a look through your business plan and keep an eye open for any information you can use in your costing and pricing calculations.

Also be on the lookout for opportunities where you can develop your product or service further. This will either put you in a different competing bracket, or in a total new niche market, which will also have an effect on your pricing strategy. Instead of you pricing simply to survive, if you enter a niche market, you may find yourself adopting a different pricing strategy, possibly even one where you can charge high prices but consumers perceive your product to be superior to those of your competitors.

The assessment of your environment will allow you to gain greater insight into your competitors, suppliers and customers, which will give you an added advantage when determining pricing strategies.

	*Complete Activity in your Workbook*

2.5. BANKING

Today it is extremely dangerous to walk around with piles of cash. Also the old saying of keeping money under the mattress really isn't practical at all.

When you have an established client base and your business is of such a type that doesn't only accept cash from clients, there are new technologies that are much more convenient for customers to pay accounts or do electronic purchases. These technologies are internet, telephone and cellphone banking. Without a bank account none of your customers will be able to make these transactions.

Types of accounts

There are accounts for personal, business, corporate and merchant use

- ✓ **Savings Account**: Savings Accounts offer a variety of saving strategies with different features and benefits designed to accommodate client requirements.
- ✓ **Cheque Account:** The Cheque Account range offers a variety of products and services that cater to the requirements of a variety of Absa customers.
- ✓ **Credit Card:** The credit card is a credit based transacting tool for individual, corporate or business clients.

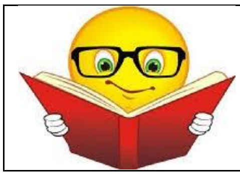
Interest Rates

- ✓ The type of account you choose will determine how much interest you will receive on your positive bank balance.
- ✓ Credit card and cheque accounts provide better interest on positive bank accounts.
- ✓ We all know that our interest rates in South Africa and the entire world changes in a continuous basis.
- ✓ The type of account and products you choose will determine how profitable your business will be. You should choose a financial product that will allow you the most flexible and profitable charges on the financial transactions.

Bank Statements

A **bank statement** is a transactional statement that shows what money came into the account and what money left the account. It also shows items such as credit interest, banking charges, current balances, debit orders and the account details.

Bank statements can be obtained from the nearest branch or online. It is very important to understand a bank statement to ensure that no unplanned transactions were made or any fraud committed.

	*Complete Activity in your Workbook*

LEARNING UNIT 3: Business Plan

Learning Outcomes:

By the end of this unit, you will be able to:

- ✓ **Identify, gather and analyse the relevant information needed to compile a business plan.**
- ✓ **Formulate an ethical framework for the operational plans of a new venture.**
- ✓ **Establish and prioritise business, financial and / or operational goals and objectives for a new venture.**
- ✓ **Design and present business, financial and / or marketing plans based on a budget for a new venture.**

3.1. INTRODUCTION

Business plans are utilised for a number of different reasons. Firstly, a business plan can be drawn up to assess the viability of your business idea. You will find a business plan helpful in this sense as you will need to assess the market for your product or service, as well as your competitors and other important information. Assessing the viability of your ideas is covered in our manual on viability of business opportunities and ideas. This manual will concentrate on helping you to formulate a business plan.

Secondly, a business plan can also be drawn up if the business is applying for funding, especially at banks. Here, the bank manager will want to discuss your business plan in-depth in order to assess the viability of your business being successful. Business plans can also be formulated as a tool for moving the business into the future. If the business is already running, and certain strategies, such as marketing and advertising strategies have changed, these need to be communicated in the business plan.

Let us take a more in-depth look at the importance of a business plan, and its components.

	Should the primary purpose of the Business Plan be for the raising of finance? Each financial institution has a guideline as to their minimum requirements which need to be included in the Business Plan. Please consult each targeted financial institution before commencing the development of your Business Plan to ensure that you meet their minimum requirements.

3.2. INFORMATION NEEDED TO COMPILE A PLAN

THE PURPOSE AND IMPORTANCE OF A BUSINESS PLAN

The main objective of a business plan is to explain to a reader what the nature of the enterprise is and what its business strategy for the following three or more years will be. The main reason for a business plan is to do systematic planning for your enterprise and then put it into writing.

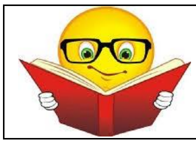
Who needs a business plan?

Every business needs one!! By having a business plan you can have the maximum insurance that your business are going to work that you won't loose a cent of your own money or need any more than you had anticipated the business planning give you the chance to make your mistakes on paper before you are tempted to make them for real. Planning will enable you to identify all the resources you will need to successfully complete your plan. It will ensure you identify at the beginning how much cash you will need; how big a production/service facility will be required; how many people will be needed. Too often theses areas are neglected. Preparing a business plan will get you into a new way of looking at your business. Planning is a continuous process that will ensure that your business is best suit to the changing business environment about it.

Planning makes you more confident about the future – It ensures that you are better prepared for some of the uncertainties ahead of you because you have thought about them in advance. Planning helps you give an invaluable tool to monitor and control the business by – if it is not in the plan then you should question why you are doing it. Is the progress as good as planned? If it is not, ask yourself why not? And what are you going to do about it?

Planning can help you to obtain finance. It often happens that the entrepreneur does not have enough money to run an enterprise. He then looks for additional finance. Financiers will pay attention to specific matters in the business plan; they will want to see what return they will earn in their investment.

A business plan is developed once a feasibility study has been done. The business plan is the entrepreneurs planning document and it serves as an instrument to arouse the interest of potential investors. It is valuable in defining and forecasting potential risks and problems, and the possible results of the opportunity. The plan is not only supposed to spell out the opportunity which is to be exploited, but also the strategy which will be followed to exploit the opportunity. It is an indication that the entrepreneur has the ability to execute the plan. It is the road map to a successful business.

	*Complete Activity in your Workbook*

3.3. THE DIFFERENT ELEMENTS OF A SUCCESSFUL BUSINESS PLAN

The business plan must indicate exactly:

- ✓ which activities the enterprise is currently involved in
- ✓ what the mission, objectives, goals of the enterprise are
- ✓ what strategy must be followed the attain these goals: and
- ✓ what control measures have been taken if the goals are not attained

According to the ABSA website, a successful business plan should have:

- ✓ Description of the business
- ✓ A description of the market
- ✓ Competition
- ✓ Management
- ✓ Support
- ✓ Swot analysis

- ✓ Financial information

Description of the business

The objective of this section is to explain:

- ✓ What the business is all about
- ✓ If this business is part of a franchise, provide us with the background
- ✓ How do you plan to run it
- ✓ Why you think the business will be successful

If it is a new business, the description should also contain responses to the following:

- ✓ Why will you be successful in this business?
- ✓ What is your experience in this business?
- ✓ What will be special about this business?
- ✓ Have you spoken to other people (fellow business people or franchisees) in this kind of business and what was their response?
- ✓ Have you spoken with objective trade suppliers to find out what managerial and/or technical help they will provide?
- ✓ Have you asked about trade credit?
- ✓ If you will be doing any contract work, what are the terms? Mention any firm contract or letter of intent and include it as supporting documentation.
- ✓ Will you offer credit to your customers?

The Market

The basic marketing considerations:

- ✓ Who is your market?
- ✓ What is the present size of the market?
- ✓ What % of the market will you have?
- ✓ What is the market's growth potential?
- ✓ As the market grows, will your share increase or decrease?

4 P'S OF MARKETING

Product / Service

- ✓ What product/services will be sold by your business?
- ✓ Why would a customer make use of your product/service?
- ✓ What are the different product/service features that make your product/service so unique?
- ✓ Can competitors copy your product/service easily? If not, why not?

Place / Distribution

- ✓ Physical business address?
- ✓ What are the physical features of your building?
- ✓ Is the building leased or owned? Provide details.

- ✓ If renovations are needed, what are they? What is the projected cost? Get quotes in writing from more than one contractor. Include quotes as support documents.
- ✓ What is the neighbourhood like? Does the zoning permit your kind of business?
- ✓ What kind of businesses is in the area?
- ✓ Have you considered other areas? Why is this one the most desirable site for your business?
- ✓ Why is this, the right building and location for your business?
- ✓ How does the location affect your operating costs?
- ✓ If you are not performing as predicted, due to a bad location, will you be able to move your business?
- ✓ How much will it cost you to relocate? If this is a franchise operation, will the Franchisor be able to contribute any funds for relocating?

Price

- ✓ How are you going to price your service, product or merchandise to make a fair profit and, at the same time, be competitive?
- ✓ How will you attract and keep this market?
- ✓ How can you expand your market?
- ✓ What price do you intend getting for your product/service?
- ✓ Is this price competitive?
- ✓ Why will someone pay your price?
- ✓ How did you arrive at the price? Is it profitable?
- ✓ What special advantages do you offer that may justify a higher price (you don't necessarily have to engage in direct price competition)?
- ✓ What price are the competitors charging?
- ✓ Why is it more expensive or cheaper than your service/product?

Promotion

- ✓ Do you think it is necessary to advertise in your business? If so, explain why?
- ✓ What type of advertising will you make use of?
- ✓ Why would you say this type of advertising will be effective?
- ✓ As a % of turnover, how much will you spend on advertising?
- ✓ If this is a franchise operation, what is the advertising fee payable to the Franchisor?
- ✓ How are these funds administered?
- ✓ Will you as a franchisee be able to provide input on spending these funds?

Competition

If you have decided that your market is large enough to be profitable and promises reasonable expansion possibilities, check your competition, both direct (similar operations) and indirect. Consider these questions:

- ✓ Who are your five closest competitors?
- ✓ Why would you consider these operations to be competitors?
- ✓ How will your operation be better than theirs?
- ✓ How are their businesses: Steady? Growing? Dwindling? Why?
- ✓ How are their operations similar or dissimilar to yours?
- ✓ What are their strengths and/or weaknesses?
- ✓ What have you learned from watching their operations?

Management

Include and describe the following on all members / shareholders / directors:

- ✓ Staff organogram / Family Tree
- ✓ Personal history (include CV)
- ✓ Qualifications (formal and informal)
- ✓ Related work experience
- ✓ Duties and responsibilities
- ✓ Salary
- ✓ Strengths and weaknesses
- ✓ Business background
- ✓ Management experience
- ✓ Age, special interests, reasons for going into a business
- ✓ Health
- ✓ Why are you going to be successful in this business taking your background into consideration?
- ✓ Staff

The following will describe your staff needs:

- ✓ Will the members / shareholders / directors be directly involved in the business?
- ✓ What is your staff's needs now? In the near future? In five years?
- ✓ What skills should they have?
- ✓ Are the people you need available?
- ✓ Full or part-time?
- ✓ Salaries or hourly wages?
- ✓ Fringe benefits?
- ✓ Overtime?
- ✓ Will you have to train people? If so, how and at what cost?
- ✓ Will the worker/s be unionised?

Support

- ✓ Who will be the major role-players be in supporting your business?
- ✓ What type of support will these role-players provide in your business?
- ✓ If the current "supporters" fall away, will you be able to survive?
- ✓ If this is a franchise operation, describe the whole support function from the side of the Franchisors.

Swot Analysis

Inside your business:

- ✓ Strengths
- ✓ Weaknesses

Outside your business:

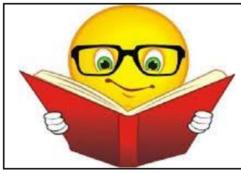
- ✓ Opportunities
- ✓ Threats

Financial Information

- ✓ Set-up Cost
  Provide a detailed breakdown of the set-up cost:
    - o Shop fitting
    - o Equipment
    - o Signage
    - o Stock
    - o Working capital, goodwill, etc.
    - o Other
    - o NOTE: Remember to include VAT
- ✓ How much will your own contribution be?
- ✓ Where did you get your own contribution from?
- ✓ What will be paid for with this contribution?
- ✓ If the property is leased, will the landlord be able to contribute any funds in terms of shop fitting etc.
- ✓ Who will the suppliers of your equipment be?
- ✓ Should one of your machines break, will the suppliers be able to provide the necessary support?
- ✓ Did you compare prices of various suppliers?
- ✓ Remember to include deposits, e.g. rent, water and lights, telephone, etc. in the initial set-up cost.
- ✓ If this is a franchise operation, what is the initial franchisee fee and the royalty fee payable on a monthly basis to the Franchisor?
- ✓ How much will the owner's remuneration be (monthly)?
- ✓ If this is a franchise business, will you be able to buy your equipment from any supplier or be compelled to buy it from a selected supplier nominated by the Franchisor.
- ✓ If this is an existing business, provide audited financials or at least the latest management accounts on the business.
- ✓ Financial Projections
    - o Cash-flow projections
    - o Income statement
    - o Balance sheet

Financial projections must include the following:

- ✓ Turnover
- ✓ Cost of sales
- ✓ Gross profit (turnover minus cost of sales)
- ✓ All expenses payable (remember your own salary)
- ✓ Royalty payments
- ✓ Bank repayment
- ✓ Net profit after loan repayment
- ✓ Do projections for a 3-year period, considering the escalation on rent and turnover growth and inflation.
- ✓ Show the break-even point
- ✓ Briefly describe how turnover figures were calculated



Complete Activity in your Workbook

3.4. INFORMATION ON THE RESOURCES NEEDED

Contents of the Business Plan

✓ Description of the enterprise ✓ Primary activities ✓ History of the enterprise ✓ The enterprise's position in the market ✓ Market analysis ✓ Competition ✓ Manufacturing plan	✓ Staff ✓ The goal and strategy of the enterprise ✓ Mission. objectives and goals ✓ Strategy for achieving goals and opportunities ✓ Management summary - A short and concise presentation of your business plan.

Aspects that should be addressed in the business plan

The business plan must be clearly presented. If it is not clearly presented, it can indicate that the necessary management skills are lacking. The business plan must contain a management summary and a list of contents, after which all elements of the business plan must be dealt with systematically. It must not be a theoretical document without action plans.

Conciseness is a prerequisite for a business plan. It must contain enough information without becoming verbose. Keep it simple and come straight to the point. Detailed information can be attached as supplements.

The business plan must be a user friendly document. It must be easy to read and the pages bound together in some way. There must be no loose sheets of paper. However, it must not be unnecessarily decorative. A neat, businesslike document is what is needed.

Number the paragraphs

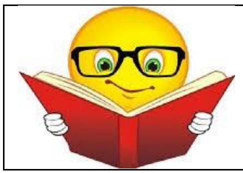
The first paragraph of the business plan must be a management summary. Its purpose is to focus the attention of the interested persons on the business idea. The rest of the business plan is used to illustrate the information in the first paragraph. The first paragraph must contain the following:

- ✓ the mission of the enterprise
- ✓ who the management of the enterprise is or will be
- ✓ who the target market is and how large the potential market is, what the expected market share is and how the target market will be reached
- ✓ what product or service will be provided

- ✓ Funds that will be needed (exact amounts), how the money will be applied and how it will be repaid. Also mention how much money the owner has invested in the enterprise (what the owner's interest is)
- ✓ The position of the enterprise within the market must be clearly indicated. The size of the market must be conveyed, and how it has been calculated. You must indicate how you set about determining the size.
- ✓ The business plan must indicate clearly what the mission of your enterprise is and that you know exactly which needs your product will satisfy.
- ✓ Indicate your expected sales and how you have calculated them. Also give your cost of sales per unit.
- ✓ You must discuss your competitors and your relationship with your competitors very thoroughly.
- ✓ Also discuss the weaknesses (risk) openly and indicate how you will manage them.

There are therefore three requirements that a business plan must meet:

- ✓ The proof that there is really a demand for the product or service
- ✓ That the management team is experienced and balanced in its composition
- ✓ That the business plan shows a profitable enterprise for all parties and the risk involved not too great.

	*Complete Activity in your Workbook*

3.5. INDUSTRY SPECIFIC AND LEGAL REQUIREMENTS FOR OWN VENTURE

Legal requirements for an own venture

It is easy to start some businesses, but others need to go through many legal formalities before being registered as a business.

- ✓ The owner of the one-person business is fully liable for the debts of that business. In other types of ownership the liabilities for the owner are limited.
- ✓ There are many one–person businesses because it is easy to start your business this way. e.g. Stall owners, tourist guides, taxis and cafes.
- ✓ Except for stall owners others do not need to register (Tourism 4 p175: Leon Smit, T.C Vivian) all owners of this type of business must register at their local authority.
- ✓ Contact your local authority to find out if you need a licence, but most one-person businesses do not need a licence, except for those working with food, liquor, transport of persons and other types where other persons might be at risk as a result of your business activities or its products.
- ✓ You only need to register for VAT if your turnover is more than R300 000.00 per year. If you plan to have a flea-market stall on private property, you must obtain permission from the owner to do so.

- ✓ Some businesses need a trading licence to run a business legally. Contact your local municipality to find out if your business needs a licence.

Licensing requirements depend on:

- ✓ Your type of business
- ✓ If you run your business from home or from an office
- ✓ The province or metro where your business is located

Look at different types of businesses in document for additional reading to address the legal formalities of each type of business. E.g. the close corporation and company possess their own legal personality, while the sole proprietor and partnership do not.

This means that the person in the sole proprietorship and the partnership are usually responsible for the tax and debt obligations / commitments of the business. They therefore have unlimited liability for commitments of the business.

The shareholders of companies and members of close corporations have limited liability in respect of commitments of the particular business form. The person can therefore be held responsible to a limited extend for the commitments of the company or close corporation.

Legislation that will impact on your business will be the legislation that is set up for the types of business forms e.g. Closed Corporation, Private Company, Public Company or Sole Proprietary.

DRAWING UP A CODE OF ETHICS FOR THE BUSINESS

When registering a business, one is provided with information on what statutory council is applicable to that business sector. They have certain regulations such as minimum wages and working conditions.

Evaluating Codes of conduct used by similar organisations in the sector for inclusion in an ethical framework for the business

A corporate **Code of Conduct**, sometimes also referred to as Code of Ethics, helps a company to show to all involved parties, internal and external, the standards that govern its conduct, thereby conveying its commitment to responsible practice wherever it operates.

As you know, there have been many legal and paralegal initiatives to promote or require good conduct by corporations. Because there are now so many of these guidelines, it is not simple to get an overview, so that you're able to quickly assess if your firm's Code of Conduct is 'world-class'. There are things that should be considered in any Corporate Code of Conduct.

It is suggested that there are 8 governing ethical principles which taken together **to create or evaluate a Code of Conduct** and their most important aspects are:

1. The Fiduciary Principle (Diligence, Loyalty).
2. The Property Principle (Protection, Theft).
3. The Reliability Principle (Contracts Premises, Commitments).
4. The Transparency Principle (Truthfulness, Deception, Disclosure, Candor, Objectivity).
5. The Dignity Principle (Respect for the Individual, Health and Safety, Privacy and Confidentiality, Use of Force, Association & Expression, Learning & Development, Employment Security).
6. The Fairness Principle (Fair Dealing, Fair Treatment, Fair Competition, Fair Process).
7. The Citizenship Principle (Law & Regulation, Public Goods, Cooperation with Authorities, Political Non-involvement, Civic Contribution).
8. The Responsiveness Principle (Addressing Concerns, Public Involvement).

SOCIAL AND ETHNIC CONSIDERATIONS

Ethic responsibilities

The business environment is the place where “right” or “wrong” issues become even more confusing The reasons are countless but it eventually comes down to one reason, namely money. The saying that “the business of business is business, whatever it takes” Partly explains it. Some businesses are making millions of Rands by means of dubious activities.

Ethics refer to moral principles or a set of values held by an individual or a group. Decisions are taken in accordance with these principles of conduct. Such decisions are then considered to be correct. People differ, cultures differ, societies differ and what is regarded as right or wrong also differs.

One can however do an easy “ethics check” by asking the following 3 questions:

- ✓ Is it legal? – Will I be violating the law?
- ✓ Is it balanced? – Is it fair to everybody?
- ✓ How will it make me feel about myself? – Will it make me and my community proud?

There is no right way to do a wrong thing!!

Social responsibilities

Social responsibilities refers to an obligation that a person or business has towards other individuals or communities.

Although starting your own business is your right, it does not give you the right to interfere with other people’s rights. You have a social responsibility towards:

Employees: If a business is serious about its own long-term future, it should make additional investments in its labour force.

Customers: Good customer care is quickly recognised by customers and word of mouth is still one of the most powerful advertising methods.

Environment: Our heritage is threatened by uncontrolled pursuit of economic goals by businesses. Resources are scarce and we may make use of them but we have no right to abuse them.

Community: A contribution to the community might create an environment, which is more conductive to good business. This means more jobs and a better standard of living and by implication more customers and better profits.

Ten Commandments of business social responsibility:

- ✓ You should take corrective action before it is required.
- ✓ You should work with affected people to resolve mutual problems
- ✓ You should work with affected industry standards and self-regulation.
- ✓ You should publicly admit thou mistakes.
- ✓ You should get involved in appropriate social programmes.
- ✓ You should help correct environmental problems.
- ✓ You should monitor the changing social environment.
- ✓ You should establish and enforce business code of conduct.
- ✓ You should take needed public stands on social issues.
- ✓ You should strive to make profits on an ongoing basis.

PERSONAL VALUES FOR MODIFYING AN ETHICAL FRAMEWORK

Each individual has a core of underlying values that contribute to our system of beliefs, ideas and/or opinions. Integrity in the application of a "value" ensures its continuity and this continuity separates a value from beliefs, opinion and ideas.

In this context a value (e.g. Truth or Equality or Greed) is the core from which we operate or react from. Societies have values that are shared among many of the participants in that culture.

These beliefs can be grouped into four categories:

- ✓ Ethics (good, bad, moral, immoral, amoral, right, wrong, permissible, impermissible)
- ✓ Aesthetics (beautiful, ugly, unbalanced, pleasing)
- ✓ Doctrine (political, ideological, religious or social beliefs and values)
- ✓ Inborn

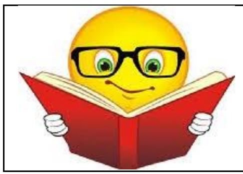
Here are examples of values:

acceptance	enthusiasm	justice	respect
accountability	equality	kindness	responsibility
adventure	fairness	learning	restraint
appreciation	fantasy	love	self-awareness
balance	fidelity	loyalty	self-discipline
caring	focus	magnanimity	self-reliance
chastity	foresight	mercy	self-esteem
compassion	friendship	moderation	self-respect
confidence	generosity	modesty	sensitivity
cooperation	gentleness	nurturing	sharing
courage	giving	obedience	sincerity
courtesy	helping	optimism	tenacity
creativity	honesty	patience	thoughtfulness
curiosity	hope	peace	tolerance
dependability	humour	perfection	trust
determination	imagination	perseverance	truth
effort	innocence	potential	understanding
endurance	integrity	purpose	unpretentious
			unselfishness

DRAWING AN ETHICAL FRAMEWORK AND CODES OF ETHICS AND CONDUCT

A code of ethics should include the following:

- ✓ Fundamental honesty and adherence to the law.
- ✓ Product safety and quality.
- ✓ Health and safety in the workplace.
- ✓ Employment practices.
- ✓ Selling and marketing practices.
- ✓ Security and privacy.
- ✓ Political activities.
- ✓ Financial reporting.
- ✓ Supplier relationships
- ✓ Protecting the environment.

	*Complete Activity in your Workbook*

3.6. ALIGN PERSONAL OBJECTIVES TO THE BUSINESS GOALS

Assessing your personal and business objectives

1. First consider your personal objectives: Think through the following questions and write your answer after each. Be as specific as you can – and as honest with yourself as you can!

a. Why did you originally make the decision to go into this business?

b. What do you hope to obtain from it? Be specific!

c. Are you getting out of the business what you originally hoped for?

d. How hard do you want to be working:

- ✓ Next year?
- ✓ Five years from now?
- ✓ Ten years from now?

e. When will you be willing to get out of the business?

f. How interested are you in rendering real service to your community?

g. How much pride do you take in the quality of your product or in the service you render?

h. List your strongest personal abilities, which you should be capitalizing on.

i. Do you have any knowledge and/or interest in any kind of business other than the one you are in now?

j. List the other areas that represent potential for diversification.

k. Do you have the capability to manage more than one area of endeavour?

l. If not, how can you acquire the capabilities?

m. List your principal personal deficiencies, which might handicap you in future growth.

2. Second, prepare to draft a statement of your business objectives. It will be helpful if you will first answer each of the following questions:

a. What will be your primary source of business for the next five to ten year?

b. Do you anticipate diversifying into other fields in this period of time? If so, what?

c. How are you going to go about entering another field?

- ✓ Do you have anyone on your present staff that knows something about this area? If not, where can you find someone who does?
- ✓ Do you know people in the other area(s) that will give you advice? Who?

d. Do you have enough capital to start up a new and strange endeavour?

e. If not, where will you find it?

- ✓ Can you joint venture with someone? Who?
- ✓ Who are the major investors in your area?

- ✓ How can you get to know them better?

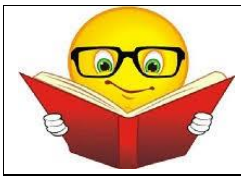
f. Do you have factual evidence that there are real opportunities in this other area, or do you just think the other fields are greener?

h. What are the risks of this other area? Are the potential rewards great enough to justify the risk?

i. What do you want your business to stand for in the eyes of others – the community, your customers, your employees, etc.?

k. How long do you plan for the business to survive?

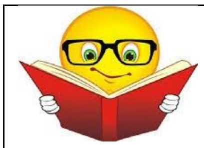
l. What will happen to it if you are no longer directly involved in managing it for one reason or another?

	*Complete Activity in your Workbook*

VISION STATEMENT OF A NEW VENTURE IS COMPILED

What Is a Vision Statement?
A vision statement is your ticket to success. A photograph in words of your company's future, it provides the inspiration for both your daily operations and your strategic decisions. Without a vision statement, effective business planning would be impossible; it's the vision statement that provides the destination for the journey, and without a destination, how can you plan the route?

What Is a Mission Statement?
A mission statement defines what a company currently does – products or services, key business drivers (e.g. highest quality and on-time delivery), how the company competes in the marketplace, and perhaps even some corporate values (e.g. being a good neighbour in the community). It may involve some "stretch" or challenge, but a mission mainly looks from the present out only one or two years. The "stretch" should start the company moving in the direction of the mission.

	*Complete Activity in your Workbook*

3.7. SHORT AND LONG TERM GOALS

3 Rules for Setting Business Goals

Like setting personal goals, setting business goals provides us with direction and motivation. But only if we set the right goals, goals that will keep our business on track rather than derail it. How do we know that we're setting the right business goals? The right business goals follow three goal setting rules.

1) Business goals need to be relevant.

Business owners sometimes make the mistake of choosing business goals that are pointless. For instance, one person I know once set a business goal to hand out one hundred business cards a month. Well he did, but so what? If his intention in setting this business goal was to bring in more business, we all know that the way to do that is to establish relationships with people, and you don't accomplish that by just handing someone a card. The whole exercise was just a waste of time. To be relevant, a business goal has to be profitable in some fashion. That's not to say that every business goal has to be measurable in Rands and cents, but it does have to possess a clear advantage or benefit to your business.

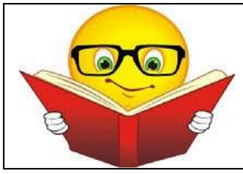
2) Business goals need to be actionable.

An even more common mistake when setting business goals is to choose business goals that are too vague or abstract. Business goals such as "Andy's Antiques will improve our customer service" sound nice - but if Andy's Antiques is your business, how are you going to do that? When you're setting business goals, be sure that you have developed them from general statements, such as in the example above, to specific actions that can be performed and evaluated. Goals without action plans are just pretty words.

3) Business goals need to be achievable stretches.

The purpose of business goals is to move our businesses forward and to motivate us. So we have to position the bar very carefully when we're setting business goals. If the bar is set too high, we set ourselves up for failure and disappointment and many of us, recognizing this in advance, will just stop trying. On the other hand, if the bar is set too low, and all we have to do is step over it, we might not bother to do it as we won't get enough satisfaction or recognition from the accomplishment. A goal has to stretch us to be worth doing. Recognize that a business goal has to 'feel' worthwhile and set business goals that will accomplish the dual purpose.

Follow these three rules when you're setting business goals and you'll find that you're automatically achieving more because you'll no longer be wasting time setting goals that defeat the purpose of the exercise.

	*Complete Activity in your Workbook*

POSSIBLE CONTRIBUTION TO COMMUNITY AND REGIONAL GROWTH OBJECTIVES

What is meant by social responsibility?

Your goal must not only be to make money, but also to invest in social responsibility.

That means that you must give back to the community.

The enterprise also needs to take an interest in how their activities impact on society and basically comes down to the idea of acting as a responsible citizen.

Why is it important to act in socially responsible way?

Because the more you give the more you get back as people support your business and remain loyal.

What do these responsibilities include?

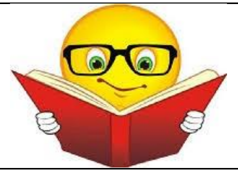
Social responsibilities include:

- ✓ Commitment of the business to behave in an ethical manner
- ✓ Contribute to social development
- ✓ Improve the quality of life of the workforce as well the local community and society at large.

Contribute to social development

- ✓ A successful entrepreneur not only benefits himself but also the community, region and country as a whole.
- ✓ The development of entrepreneurial qualities can cause significant changes especially in the rural communities through income generation and economic growth.
- ✓ That means potential entrepreneurs play a major role in job and wealth creation. This obligation is seen to extend beyond just obeying the laws. An organisation must take further steps to improve the quality of life for employees and their families as well as the local community and society at large.
- ✓ This process of communities equipping themselves with the knowledge, skills and resources they need in order to change and improve the quality of their own lives and their community is called empowerment**.**
- ✓ When businesses invest in their own communities though job and local wealth creation it will to a certain extent prevent people leaving the security of their families and local communities in search for a better life elsewhere such as in cities. This means that it significantly reduces the migration of labour and urbanization**.**
- ✓ Urbanization is the process in which the number of people living in cities increases compared with the number of people living in rural areas.

- ✓ Rapid urbanization brings with it many problems as it places huge demands on land, water, housing, transport and employment.

	*Complete Activity in your Workbook*

CULTURAL VALUES AND BELIEFS OF PROSPECTIVE EMPLOYEES

Defining your Values System

What are Values?

They refer to:

- ✓ Principles
- ✓ fundamental convictions
- ✓ ideals, standards or life stances

which act as general guides to behaviour or as points of reference in decision-making or evaluation of beliefs or action and which are closely connected to personal integrity and personal identity. (Halstead, 1996)

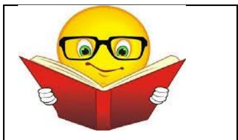
Values are:
The priorities individuals and society attach to certain beliefs, experiences and objects in deciding how they shall live and what they shall treasure. (Hill, 2004)

They are said to be:

principles and fundamental convictions which act as general guides to behaviour, the standards by which particular actions are judged as good or desirable. (Halstead, Taylor and Taylor, 2000)

A value system refers to *how* an individual or **a** group of individuals organise their ethical or ideological values. A well-defined value system is a moral code.

Your values determine the actions you take, as well as the goals you set

	*Complete Activity in your Workbook*

3.8. RESEARCH AND ANALYSIS OF COMPETITORS

Researching the Competition

Competition comes from many sources. Some of your competition will be direct competitors such as other food processors selling the same product or indirect competition selling a different food product. You must pay attention to both direct and indirect competition if you are to market effectively.

In doing research on your competition, you must learn who and what you are competing against. Some of the factors you will want to look at are:

- ✓ Products - what do they sell? What is their niche?
- ✓ Prices
- ✓ Customers - who are they?
- ✓ Image / reputation
- ✓ Longevity - does it have staying power?
- ✓ Type of promotion - is it effective?
- ✓ Strengths and weaknesses

Your competitive Advantage

Once you have researched and studied your competition, you will want to think of different ways to compete. You will want to look for your competitive advantage by asking yourself:

- ✓ What can you do better than your competition?
- ✓ What can you do differently than your competition?
- ✓ What will make your business stand out from your competition?

3.9. STRUCTURE AND LAYOUT OF THE BUSINESS PLAN

Your business plan should at least consist of the following parts:

- ✓ Cover page.
- ✓ Design a smart looking, professional cover page with the second page giving the contents of your business plan. It is important for your cover page and your whole business plan to show how serious you are about starting your own business.

Your cover page must give:

- ✓ the name of the business
- ✓ the entrepreneurs name
- ✓ the entrepreneurs addresses and contact telephone numbers
- ✓ the logo of your business

Summarize your business idea

Your summary should make the reader want to continue to read the rest of the document. Although the summary is requested on the third page of your business plan workbook, you should only write it after all the other parts of your plan has been written. You need to do this so that you can first get a complete picture of the business plan before making a summary of it.

Describing your business

- ✓ The marketing plan of your business
- ✓ The management plan of your business
- ✓ The financial plan of your business

MARKETING AND PROMOTION OF THE OWN VENTURE

The marketing plan of your business should include the following:

- ✓ A description of your target market
- ✓ What percentage of the target market you will succeed in getting
- ✓ sales forecasts for the first year of your business
- ✓ description of your main customers
- ✓ description of your potential competitors, their marketing strategies and how they can influence the success of your business
- ✓ a description of your promotions- marketing of your products, pricing – how pricing will be done, place – where customers can get your product or service, products – what products and services you can offer your customers.

Advertising

An essential aspect of the marketing campaign is effective advertising. Any advertisement should cause the following responses in the reader:

A I D A

- ✓ **Attract (Attention):** The advertisement should make use of colour, bold script and illustrations to attract attention
- ✓ **Interest:** The advert should arouse the reader's interest with questions or promises.
- ✓ **Desire:** The advert should fill the reader with immediate desire to buy the product or service. Use urgency words like "NOW" or "before it's too late".
- ✓ **Action:** The advert should inspire the reader to action. "Go for it! You deserve it!"

Hint: Where you advertise is very important. Contact the local newspapers and find out what it costs to advertise. You may save money and reach more people by doing a mail drop (for a fee the Post Office will do this for you). Remember that these costs must be added to your product price.

FINANCE REQUIREMENTS FOR THE BUSINESS

The financial plan of your business is important and needs a lot of attention. Many new ventures experience a lot of financial difficulties in the beginning and sometimes fail because they didn't do proper financial planning.

Your financial plan should at least include the

- ✓ Start up costs
- ✓ A calculation of break-even point
- ✓ A cash–flow statement showing how much cash you can expect to have available each month.
- ✓ A detailed income and expenditure statement.
- ✓ Financing needs from banks and other financial institutions.
- ✓ Security you can offer to lending organisations

Points to Remember: The Financing section must show that you are as committed to your business venture as you expect those reading your business plan to be. Show the amount of personal funds you are contributing and their source. Also include the amount of capital you need and your plan to repay this debt. Include all pertinent financial worksheets in this section: annual income projections, a break-even worksheet, projected cash flow statements and a balance sheet.

THE PROJECTED INCOME AND EXPENSE

Projected income and expenses of the new venture must be covered under the financial plan section of your business plan.

THE OPERATIONS PLAN

This section is covered under the SWOT analysis and Marketing plan in your business plan

SWOT ANALYSIS

- ✓ Discuss definite and possible strengths, weaknesses, opportunities and threats
- ✓ Give an honest assessment of the risks faced by the business, entrepreneurs and investors in relation to the potential for growth, profitability, and capital appreciation
- ✓ Discuss strategies that can be implemented to address the risk factors highlighted

Points to remember: An honest and critical evaluation of the strengths, weaknesses, opportunities and threats will help you capitalise on your strengths, overcome your weaknesses, exploit opportunities and avoid threats (or turn threats into opportunities).

Relevant documentation is compiled to support the business plan

The following supporting documentation should be included where applicable:

- ✓ Newspaper clippings, promotional literature, product brochures, market research, trade and industry publications
- ✓ partnership, association or shareholders' agreements
- ✓ offers to purchase, purchase and sale agreements

- ✓ contracts, orders, letters of intent
- ✓ memoranda of understanding, lease, franchise, agency or distribution agreements
- ✓ documentation relating to licences, copyrights, trademarks and patents
- ✓ quotations or pro-forma invoices for capital items to be purchased
- ✓ detailed personal balance sheets of the entrepreneurs
- ✓ copies of identity documents and marriage certificates of the entrepreneurs
- ✓ schedules of life insurance and endowment policies of the entrepreneurs
- ✓ copies of company or close corporation certificates and registration documents
- ✓ drawings, work flow charts, plans, factory layouts, maps, etc.
- ✓ a list of persons to whom reference can be made regarding creditworthiness, product and service quality, and the skills, abilities and integrity of the entrepreneur

3.10. BUSINESS PLAN INFORMATION IS PRESENTED IN RELEVANT AND CLEAR FORMAT

Uses of a business plan

A business plan is a valuable management tool. It has very many uses, which include the following:

Setting goals and objectives

A business owner should use the business plan as a tool for setting the direction of a business over the next few years. The plan should also include the action steps and processes to guide the business through this period.

Of course, a business plan is not a guarantee that problems will not arise, but with a well thought out plan, you can better anticipate a crisis situation and deal with it before it becomes too serious. Furthermore, a well-constructed plan could help the business avoid certain problems altogether. Business planning is probably more important to the survival of a small and growing business than it is to a larger, more mature one.

Six steps in preparing your business plan

Identify your objectives

Before you can write a successful business plan, you must determine the following:

- ✓ Who will read the plan?
- ✓ What do they already know about your business?
- ✓ What do they want to know about your business?
- ✓ How do they intend to use the information they will find in the plan?

Find a balance between what the members of your target audience want to know and what you want them to know. You are now ready to begin preparing a useful business plan.

Outline your business plan

Once you have identified the objectives for your business plan, and you know the areas that you want to emphasise, you should prepare an outline based on these requirements. It can be as general or as detailed as you wish.

Review your outline

Review your outline to identify the areas that, bearing in mind your readers and objectives, should be presented in detail or in summary form in your business plan.

Writing your plan

Assuming that the bank manager is the target audience for your business plan, ask yourself if he or she will be able to answer the following questions based on the information you are providing:

- ✓ Who are you?
- ✓ Why is the business viable?
- ✓ Exactly how much money do you need and why?
- ✓ Where will this money go?
- ✓ What will you contribute to the business?
- ✓ When and how will the loan be repaid?
- ✓ What if the business fails?
- ✓ Can this business afford its owner(s)?

Have your plan reviewed

Ask someone familiar with business management and the planning process to review your business plan for completeness. This person should check it for objectivity, logic, presentation and effectiveness. Next, incorporate the feedback and comments you receive.

Update you plan

Business plans are 'living' documents and must be periodically updated or they become useless. As your environment and objectives change, update the plan to reflect these changes. Refer to this booklet each time you update your plan to ensure that all areas are properly covered.

The basic business plan outline

1. Executive summary and table of contents

The executive summary is a very important part of your business plan, as the reader will consult it first to get a 'feel' for the document. It should be less than three pages in length and provide the reader with a brief but complete overview of the entire business plan. Do not merely list the topics contained in the business plan. Emphasise the key issues presented and focus on the factors that will make the business successful in a competitive market. The executive summary should be the last section of the business plan that you write.

The table of contents follows on the executive summary and should help your reader to locate specific sections of information in the plan. Do not give detailed descriptions of the contents; merely list the headings and corresponding page numbers.

2. Personal information

Personal details

This section should be completed individually by each of the owners of the business.

- ✓ First name(s) and surname
- ✓ Date of birth
- ✓ Identity number
- ✓ Business and home telephone numbers
- ✓ Full residential address
- ✓ Nationality
- ✓ If not a South African, whether you are a permanent or temporary resident
- ✓ How long have you been resident at your present address?
- ✓ Whether your residential property is owned or rented
- ✓ If resident at the present address for less than three years, state your previous address
- ✓ Whether your previous residence was owned or rented

Marital status

- ✓ Married, single or divorced
- ✓ Married by ANC or COP
- ✓ Whether your status has changed since 1984 (If so, attach a copy of the contract.)
- ✓ If married by ANC, attach a copy of the contract
- ✓ If divorced, the date on which it was final (Attach a copy of the final decree of divorce.)
- ✓ Number of dependants, including spouse
- ✓ Number of children and their ages

Spouse's details

- ✓ First name(s) and surname
- ✓ Date of birth
- ✓ Identity number
- ✓ Employer, current position at work and work address
- ✓ Business and home telephone numbers
- ✓ Annual income

Personal references

- ✓ Names, addresses and contact telephone numbers of at least three people to whom reference can be made

Employment history

- ✓ Highest educational qualification obtained and when achieved
- ✓ Formal apprenticeships or pupilage and when completed
- ✓ Career history details: employer, employment period, type of work, last position held, annual income
- ✓ Capacity you will be employed in this business

Financial Affairs

- ✓ Do you have or have you had an interest in another business? Give details.
- ✓ The monthly income you will earn from the business
- ✓ The rand value of other financial benefits that you will receive from the business
- ✓ If you have been sequestrated, when were you rehabilitated?
- ✓ Give details if you were found guilty of criminal offences.
- ✓ Give details of judgements for debt against you

Details of personal assets

- ✓ **Fixed property**
    - o Stand number, street address, name in which registered, market value, municipal value
    - o Details of these properties sold under Deed of Sale
- ✓ **Machinery, vehicles and equipment, etc**
    - o Registered owner, description, year model, date purchased, registration number, leased or owned
- ✓ **Furniture and fittings**
    - o Estimated market value
    - o Ownership vested in yourself and/or your spouse?
- ✓ **Jewellery, cameras, etc**
    - o Estimated market value
    - o Ownership vested in yourself and/or your spouse?

Other Assets

- ✓ **Life insurance:** Life insured, insurance company, policy number, annual premiums, death value, date taken out, type of policy, surrender value, beneficiary
- ✓ **Banking accounts:** Account in the name of, name of bank, branch name, type of account, account number, current balance
- ✓ **Investments, fixed deposits, etc:** Investment in the name of, where invested, type of investment, amount invested, interest rate, expiry date
- ✓ **Share investments in listed companies:** Investment in the name of, name of company, number of shares, present market value
- ✓ **Share investments in private companies:** Investment in the name of, name of company, number of shares, present market value, copy of the latest financial accounts

- ✓ **Membership of close corporation:** Name of member, name of close corporation, percentage membership, amount contributed, copy of the latest financial accounts

Details of personal liabilities

- ✓ **Fixed properties:** Stand number, bonded to, rand value of bond registered, outstanding balance, monthly repayments
- ✓ **Machinery, vehicles and equipment:** Registered owner, registration number, financed by, outstanding balance, monthly repayments
- ✓ **Furniture and fittings:** Items not yet fully paid for, outstanding balance(s), monthly Repayments
- ✓ **Jewellery, cameras, etc:** Items not yet fully paid for, outstanding balance(s), monthly repayments
- ✓ **Life insurance policies ceded to a third party:** Policy number, ceded to, why ceded
- ✓ **Credit cards:** Name of cardholder, name of bank, present balance, expiry date, ordinary limit, budget limit
- ✓ **Banking accounts:** On which account number(s) do you or your spouse use overdraft facilities? What are the limits? What are the expiry dates? What are the present balances? Provide details of security held by the bank.
- ✓ **Short- and long-term personal liabilities, excluding normal trade creditors:** Owing by, owing to, outstanding balance(s), how or when payable, monthly repayments

Suretyships:

- ✓ In favour of who have you signed sureties?
- ✓ State amount of the sureties, purpose of suretyships.

Notarial bonds:

- ✓ Over which of your assets have notarial bonds been registered?
- ✓ In favour of whom?
- ✓ For what amount?
- ✓ For what purpose?

Income: The gross monthly income of your spouse

3. **Business description**

- ✓ Is the application in respect of
- ✓ A new business?
- ✓ An existing business?
- ✓ A franchise? (If a franchise, enclose the franchise agreement.)
- ✓ A newly acquired business?
- ✓ Name of the business
- ✓ Telephone and facsimile numbers
- ✓ Trading name of business

If a company or close corporation, state the full registered name and enclose Form CK1 or CK2 where applicable.

- ✓ Street address from which business will be/is operating
- ✓ Postal address of business

If a company or close corporation, state the address of the registered office.

- ✓ Registration number
- ✓ Date registered

Owners of the business:

- ✓ Name(s)
- ✓ Director, partner, member or shareholder
- ✓ Percentage holding
- ✓ Financial contribution
- ✓ If buying an existing business: Why the current owner wishes to sell the business, details of the current owner and selling price of the business
- ✓ Describe the present or proposed activities of the business.
- ✓ If the business is part of a group of companies, provide details in the form of an organogram.

For a company

- ✓ Authorised share capital (number of shares)
- ✓ Issued share capital (number of shares)
- ✓ Give details of owners listed above who have an interest/interests in other businesses.
- ✓ How long has the business been in operation?
- ✓ For how long has the business been owned by the owners listed above?
- ✓ Provide details if the business or any of the listed owners have ever entered into a compromise with their creditors.

4. Market analysis

This section is of critical importance. It must clearly identify your understanding of the market, its characteristics, and your position within it.

You should identify customers and potential customers, and explain factors such as customer needs and decision factors. The absolute size of your market should be outlined, or estimated by reference to competitor information. Include your current and forecast market share.

5. Market and sales activities

- ✓ What percentage market share are you aiming to capture and how will you achieve this?
- ✓ Why is the market for the products/services of the business growing or declining?
- ✓ State the main competitors of your business - name of each business, location, and distance from your business, how these businesses will react to your business.

6. Products and services

This section should explain your principal products and services, their applications, and distinguishing features. The main purpose of explaining the product is for the reader to understand the market, any unique selling points and, consequently, the business opportunity.

7. Operations

Premises

- ✓ The location of the business (e.g. central business district, near freeway etc), the size of premises. Are the premises adequate for the short to medium term?
- ✓ If the premises are leased - attach a copy of the lease agreement, state the term of the lease, the date that the lease expires, whether the lease is subject to annual increases, percentage increase per annum, the monthly rental
- ✓ If the premises are owned - the present market value, when purchased, the purchase price, amount for which the premises are insured, date that the insurance expires
- ✓ If the property is bonded - to whom, value of the bond, outstanding balance of the bond

Machinery, vehicles, equipment furniture, fixtures, and fittings

- ✓ Provide a list of items presently owned by the business - type, serial/reg. no., market value, present condition, contributed by, paid for or not
- ✓ Provide a list of items that the business must still purchase - type, cost excluding VAT, new or second-hand, supplier(s)
- ✓ How will budget output be achieved?
- ✓ What maximum budget output will be achieved?
- ✓ At what stage will the additional items be required?
- ✓ How will assets be depreciated (vehicles, machinery, furniture, fixed property, other) - straight line, reducing line, per annum?

Personnel

- ✓ How many people are currently employed by the business?
- ✓ How many additional people will be required?
- ✓ Provide an organogram of the present/proposed staff structure.

Accounting

- ✓ Name of accountant/bookkeeper, plus address and contact telephone number(s)
- ✓ Name of auditor(s) - plus address and contact telephone number(s)
- ✓ Will monthly accounts be made available?
- ✓ How often will a full stock-take be done - monthly, quarterly, annually?
- ✓ How will stock be valued?

Sales

For an existing business

- ✓ The total outstanding debtors
- ✓ Normal debtor terms

Suppliers

- ✓ Main supplier(s) and their details - names, telephone numbers, terms, goods to be supplied
- ✓ Alternative suppliers - how their prices compare, terms, quality, etc
- ✓ The mark-up that you will place on products
- ✓ Average gross profit you will aim for
- ✓ Will the business be registered for VAT?
- ✓ If sales are subject to seasonal fluctuations, provide details.

Source and application of funding

Source

- ✓ Cash contributed by owner(s)
- ✓ Cash in bank (existing businesses)
- ✓ Assets contributed by owner(s) and their value - machinery (R value), vehicles (R value), equipment (R value), furniture, etc (R value)
- ✓ Fixed property (R value)
- ✓ Amount owing to creditors - existing businesses - (R value), age analysis
- ✓ Other finance granted (R value)
- ✓ Bank overdraft facilities (R value)

Application

Buildings (R value)

- ✓ Alterations to buildings (R value)
- ✓ Amounts owing on machinery (R value), vehicles (R value), equipment (R value), furniture, etc (R value)
- ✓ Work in progress (existing businesses) (R value)
- ✓ Debtors (R value) - age analysis

Banking details

- ✓ Has a bank account been opened?
- ✓ At which bank? Which branch and account number?
- ✓ If an overdraft was granted, the limit?
- ✓ What security does the bank hold?

Outside (other) finance

- ✓ Approved facilities - what other finance is the business making use of?
- ✓ Borrowed from, balance outstanding, terms, interest rate, monthly repayments, security given
- ✓ Facilities not yet approved - If application was made for additional finance, provide details.

Funding requirements (from bank):

- ✓ Overdraft
- ✓ Medium-term loan
- ✓ Letter of credit
- ✓ Guarantee
- ✓ Lease (quotation of equipment to be financed)
- ✓ Other

9. Financial data

Historical financial data (past three to five years, if applicable)

- ✓ Annual financial statements
- ✓ Income statement
- ✓ Balance sheet
- ✓ Cash flow statement
- ✓ Have the above results been audited?

Prospective financial data (next two years)

- ✓ Cash flow
- ✓ Projected income statement and balance sheet

The following initial cash flow items must be considered when compiling a cash flow statement

- ✓ Registration fees of company or close corporation
- ✓ Attorney's fees, e.g. partnership agreement, lease agreements, etc
- ✓ Trading and other licences
- ✓ Rental in advance
- ✓ Telephone installation and deposit
- ✓ Water and lights deposit
- ✓ Post Office box deposit
- ✓ Deposits for capital goods or double lease payments
- ✓ Cost of initial stationery
- ✓ Cost of initial or start-up stock
- ✓ Other deposits
- ✓ Advertising or opening promotion

The following monthly expenses must be considered:

✓ Wages ✓ Other manufacturing costs ✓ Salaries ✓ Owners' and/or directors' salaries ✓ Other salary-related expenses (pension fund contributions, UIF, etc) ✓ Rent ✓ Rates ✓ Insurance ✓ Repairs and maintenance	✓ Printing and stationery ✓ Vehicle running expenses ✓ Entertainment and travel ✓ Advertising ✓ Interest ✓ Carriage and packaging ✓ Bank charges ✓ Telephone and facsimile charges ✓ Commissions ✓ The effect of value-added tax

✓ Electricity and water ✓ Hire and leasing charges	✓ Auditors' fees ✓ Franchise royalties

10. Appendices or exhibits

Detailed or confidential information that is not appropriate for distribution to everyone receiving the body of the plan can be represented here.

Appendices and exhibits should be bound separately from the other sections of the plan and provided to readers only if required.

✓ Curriculum vitae of each key manager ✓ Pictures of products ✓ Professional references ✓ Marketing studies ✓ Pertinent published information ✓ Magazines ✓ References to books ✓ Patents ✓ Significant contracts ✓ Leases ✓ Sales contracts ✓ Purchase contracts ✓ Partnership/Ownership agreements ✓ Share-option agreements ✓ Employment/Compensation agreements ✓ Insurance	✓ Franchise agreement ✓ Copy of first page of ID document ✓ Marriage certificate, final decree of divorce order or antenuptial contracts ✓ Quotation for equipment to be financed ✓ Audited financial statements ✓ Monthly management accounts ✓ Offer to Purchase or Agreement of Sale ✓ Founding statement and amendments if a close corporation ✓ Memorandum and articles of association, shareholders' agreement, company resolutions if a company ✓ Life assurance policy or policies ✓ Any other relevant information ✓ Other expenses

11. Administrative considerations

Copies of the business plan should be controlled, and a distribution record kept. This will allow you to update your distributed plans as needed and help to ensure that your plan is not more widely distributed than you intend it to be. Remember too that an appropriate private placement disclaimer should be included if the plan is being used to raise capital.

12. **Information to add to your basic business plan**

Competition

- ✓ Identification (by product line or service and market segment)
- ✓ Existing competitors
- ✓ Market share
- ✓ Potential (How long will your 'window of opportunity' be open before your initial success breeds new competition? Who are your new competitors likely to be?)
- ✓ Direct and indirect competition
- ✓ Strengths (competitive advantages)
- ✓ Weaknesses (competitive disadvantages)

- ✓ Importance of your target market to your competition
- ✓ Barriers to entry into the market, e.g. brand loyalty, existing relationships

Market analysis

- ✓ Description of your primary industry
- ✓ Size of the industry – historically, currently, in five years and in ten years
- ✓ Industry characteristics and trends (where is it in its life cycle?)
- ✓ Major customer groups - businesses, governments and consumers

Market test results

Potential customers contacted

- ✓ Information/Demonstrations given to potential customers
- ✓ Reaction of potential customers
- ✓ Importance of satisfaction of targeted needs
- ✓ Test group's willingness to purchase products/services at various price levels

Product or service research and development

- ✓ Major milestones, ongoing efforts
- ✓ Lead times (time between placing of order by customer and execution of the order)
- ✓ Initial orders
- ✓ Reorders

Regulatory restrictions

- ✓ Customer or government regulatory requirements and their impact
- ✓ Anticipated changes in regulatory requirements and their impact

The information on marketing and sales activities can be expanded upon by adding the following details:

- ✓ Overall marketing strategy
- ✓ Marketing penetration strategy
- ✓ Growth strategy
- ✓ Internal campaigns
- ✓ Retention
- ✓ Expansion
- ✓ Acquisition
- ✓ Franchise
- ✓ Horizontal (providing similar products to different users)
- ✓ Vertical (providing the products at different levels of the distribution chain)
- ✓ Distribution channels (include discount/profitability levels at each stage) -internal sales force, distributors and retailers
- ✓ Communication - promotion, advertising, public relations, personal selling, printed materials (catalogues, brochures, etc)

Sales strategies

- ✓ Sales force - size, recruitment and training, compensation and sales activities
- ✓ Internal vs. independent representatives (advantages and disadvantages of your strategy)

The information on products and services can be expanded upon by adding the following details:

Detailed product/service description (from the user's perspective)

- ✓ Specific benefits of product/service
- ✓ Ability to meet needs
- ✓ Competitive advantages
- ✓ Present stage (idea, prototype, small production runs, etc)

Product life cycle

- ✓ Description of the product/service
- ✓ Factors that might change the anticipated life cycle (i.e. lengthen or shorten)

Copyrights, patents and trade secrets

- ✓ Existing or pending copyrights or patents
- ✓ Anticipated copyright and patent filings
- ✓ Key aspects of your products or services that cannot be patented or copyrighted
- ✓ Key aspects of your products or services that qualify as trade secrets

Research and development activities

- ✓ Active in process
- ✓ Future activities (include milestones)
- ✓ Anticipated results of future research and development activities
- ✓ Research and development activities of others in your industry

Production and service delivery procedures

Internal

- ✓ External inputs (subcontractors)
- ✓ Production and service delivery capacity

Internal and external

- ✓ Anticipated increases in capacity
- ✓ Investment
- ✓ New cost factors (direct and indirect)
- ✓ Timing

Operating competitive advantage

- ✓ Techniques, experience, economies of scale and lower direct costs

3.11. PROCEDURES TO PRESENT THE BUSINESS PLAN TO A FINANCIER

One of the institutions that offer finance to businesses is Khula Enterprise. The Khula Credit Indemnity Scheme was established to give access to finance to people who wish to start or expand small to medium sized businesses but do not have sufficient collateral / security to support facilities provided by participating banks. The scheme covers facilities from R10 000 to R3 million. The funding application to them follows the procedure outlined below:

Step 1: Approach any participating bank of your choice and submit your business plan to a business development officer for a facility application.

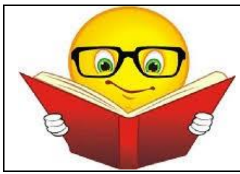
Step 2: If you do not have enough collateral, inform the bank and request them to approach Khula for an indemnity on your behalf.

Step 3: The bank will assess the business plan and your application in terms of the bank's own lending criteria and decide if the business will be able to cover the business expenses and the monthly instalments and remain sustainable**.**

Step 4: If the bank believes that the business will succeed, the facility is then approved and a facility proposal is submitted to Khula for an indemnity application**.**

Step 5: Khula considers the proposal and assesses the need for assisting the business with indemnity. The indemnity can only be used when the SME cannot provide enough collateral or security themselves. The bank manages the loan and collects your instalments for the duration of the loan.

For more information visit Khula and Landbank’s presentations or any other bank representatives in your area

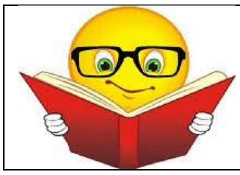
	*Complete Activity in your Workbook*

3.12. MONITORING AND REVISING IMPLEMENTATION PLANS

Developing an effective plan is only "half the battle." Getting it implemented is the other, and generally the tougher, half. And an important part of the plan implementation is monitoring – taking a periodic look at "how it's going."

Monitoring the implementation of your plan is important for a number of reasons.

- ✓ First, it helps to assure that your efforts conform to the plan. That you're actually performing the action steps you intended. That you're "on track."
- ✓ Second, you've got to be sure the results you achieve align with your quantified objectives.. That you're accomplishing what you intended to accomplish. Monitoring helps here too.
- ✓ Also, monitoring allows for corrective action. For making the necessary changes along the way. To "fine tune," not only your strategies, but your planning process as well.
- ✓ And since monitoring is part of a control process, it encourages improved performance. Knowing they'll be measured stimulates employees to do a better job.
- ✓ Finally, and most importantly, monitoring provides the essential link between the written plan and the day-to-day operation of your business. It demonstrates to all that "you really are managing the business according to your plan".

	*Complete Activity in your Workbook*

LEARNING UNIT 4: Tendering

Learning Outcomes:

By the end of this unit, you will be able to:

- ✓ **Identify information sources of available business and new markets that can be accessed.**
- ✓ **Analyse tender documents for viability in the new venture context.**
- ✓ **Calculate costs, revenue and profits of a specific tender.**
- ✓ **Complete tender documentation**

4.1. INTRODUCTION

A tender is an offer to do work or supply goods at a fixed price. Getting goods or services is also known as 'procurement'. Since January 2004, government began referring to tenders as 'bids'. When government 'puts out a tender' or 'invites bids' this means government asks the public for price offers to supply work or goods to the government. The government then assesses who to choose based on the prices offered and the nature of the person or company making the tender.

The tender or bid process is designed to ensure that the work to be done for government is given out in a fair way. There are a number of policies (known as 'procurement policies'), which guide government on how to make decisions on which tender to accept. Although price is very important in the decision on which tender or bid to accept, it is not the only factor taken into account.

Once government accepts a tender, it is binding on both parties. This means that the person or company that won the tender has to provide the goods or services in the manner agreed to and at the price offered, and government must pay the agreed price at the agreed time. In other words, once accepted, a tender is a binding contract.

WHO RUNS TENDERS OR BIDS?
Previously, all national government procurement (the obtaining of goods and services) had to be done through the State Tender Board. The State Tender Board is in the process of being dismantled and the provision of the Public Finance Management Act (PFMA) No.1 of 1999, which repeals the State Tender Board Act, is likely to become law in 2004.

The regulations to the State Tender Board Act of 1968 were amended in December 2003 so that the accounting officers of national departments can procure goods and services in terms of the PFMA. Procurement can be done in both the old and the new way until the State Tender Board Act is actually repealed.

Provincial Treasuries are in the process of carrying out similar processes, which will lead to the dismantling of Provincial Tender Boards, and the empowering of accounting officers in provincial departments. This whole process is called "the implementation of supply chain management". The National Treasury has issued 'Practice Notes' which national departments must follow to ensure uniformity in the procurement process. Provincial Treasuries are empowered to issue additional practice notes, which must not conflict with the national practice notes, for their provinces. It is during this process that government began referring to tenders as 'bids'.

4.2. WHAT IS DEFINED IN A TENDER PROCESS?

The tender process defines the following:

- ✓ Who is permitted to submit a tender
- ✓ What the tender is for
- ✓ What the conditions of the tender are that need to be fulfilled
- ✓ Legal terms and conditions

The conditions that need to be fulfilled will be in terms of:

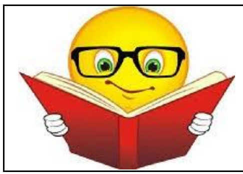
- ✓ The product or service
- ✓ The price
- ✓ The delivery terms and project plan

- ✓ Contract duration
- ✓ Financial viability

Tenders can be open or closed tenders. A closed tender only allows selected or invited companies to respond to the tender. An open tender allows response from any individual or company.

A TYPICAL TENDER PROCESS

Step	Process
Defining the tender strategy	The organisation defines its aims, decides what is needed, prepares the proposal and decides how the tender exercise will be carried out.
Inviting tenders	An invitation is made to suppliers to put in an offer or tender. This is usually in response to an advert. Sometimes a questionnaire needs to be completed before tendering, supplying information on financial status, experience and references. This enables suppliers to pre-qualify and help to narrow down the tenders.
Evaluating the tenders	The tenders are then evaluated against set standards. This process is where the tender is clarified before acceptance
Awarding the tender contract	The contract is accepted and awarded to the supplier whose bid offers the best value for money
Managing the contract	Both parties involved work together according to the specifications in the contract
Review and testing	The supplier's performance is checked and monitored by the organisation. The need for a repeat of the contract will be reviewed, and may be advertised again.



Complete Activity in your Workbook

4.3. HOW DO YOU IDENTIFY TENDER OPPORTUNITIES?

As a supplier, your first step is to identify tenders that are appropriate to the goods or services that your business can offer and provide. Some people feel that is it difficult to find tenders and work for their business, however businesses that require goods or services want you to find their tenders and they want you to respond. Thus, tenders can usually be found in obvious places such as newspapers and trade publications or magazines. Websites are a good place to start. If you have a list of businesses that may need your services, log on to their websites to see is there is any further information available. If they do not have any tenders available, they may very well have place for you to leave your details in order for them to contact you when tenders become available.

Most major businesses have web pages dedicated to tenders and business opportunities. Daily newspapers are also well worth the look. There are usually a few tender applications advertised and you may come across a few related to your business industry. Typically, you may need to download the relevant information and documents from the business web page or contact the relevant person in order to arrange for them to be e-mailed or posted to you. These documents are very important and the tender process cannot go ahead without them as they contain very important information. Sometimes you will need to register your intent to apply to the tender, either by submitting a letter of intent or by attending a compulsory information session where you will register

4.4. ANALYSING THE TENDER DOCUMENTS

Only a very few of the tenders will be suited to your business. It would be a waste of your time and effort to respond to every tender that you come across. Responding to tenders can be time consuming and expensive. In order to make sure you do not waste your time and money, you will need to analyse the tender to find out if it is a viable tender opportunity.

When assessing the viability of the tender, focus on your target market and core competencies. Many businesses have an outline with criteria that they assess in order to decide whether to bid or not to bid. Meetings are usually held at regular intervals to evaluate the viability of the business to deliver the tender on a technical level, on a commercial level, on a legal level and on a logistical level. If, during these meetings, it is evident that the business cannot deliver or realistically meet the requirements, the decision is either made to withdraw from the process or to continue but to partially comply with the requirements.

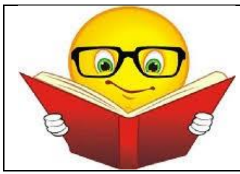
Essentially, in analysing the viability of the tender, you are examining the requirements of the tender against the products or services you can supply.

When you evaluate the tender, you should short-list the essential ‘killer criteria’. Killer criteria are used to dispose of tender applications that do not meet certain pre-defined criteria so that the bulk of the responses are immediately eliminated.

South Africa’s killer criteria usually include items such as:

- ✓ Black Economic Empowerment
- ✓ Technical aspects of the client’s requirements that are considered non-negotiable requirements.
- ✓ Acceptance of legal terms and conditions.

If you intend to respond to a tender, you should consider any killer criteria that may be evaluated and make sure that your tender more than meets the requirements.

	*Complete Activity in your Workbook*

4.5. THE COST, REVENUE AND PROFIT OF A TENDER

This is where the real work begins. You will discover that the tender evaluation team's sole purpose will be to get as much from you for as little as possible. Your purpose is often the opposite. If you provide a pure commodity, your price is the only differentiator. For any other goods or services, your task will be to convince the client of the value of your solution at the price offered.

When a business issues a tender, they have a good idea what revenue should be generated through the new goods and services. They also have an idea of what profit they would like to achieve. PROFIT = REVENUE – COSTS.

To you, the price of the product or service you are tendering is revenue. From your client's perspective, your price represents a cost to them. You will be trying to maximise your revenue while they are trying to minimise their costs. You ultimately control the final price, as no business can force you to accept a price, however being inflexible may cause you to lose the business.

The total cost of ownership or the life cycle costs are other terms often used in tenders and for all practical purposes they mean the same thing. If a customer was deciding to purchase some equipment, they will generate a profit and loss analysis to understand implications of the purchase. Similarly for the tender evaluation team. If they do not make the necessary calculations, they may make a serious error in judgement and damage their business through this error. This may cost them their jobs.

As a supplier, you also have input costs and fixed and variable costs. All businesses strive to make a profit. When you price your tender, you will need to understand your profit margin and how much can be added or subtracted without impacting your profitability negatively.

How will the client pay if you are awarded the contract? This can impact heavily on your business. Options could be:

- ✓ To pay in full, up front.
- ✓ To deposit deferred payments.
- ✓ To lease.

The breakeven point outlines the price below which your company will begin to lose money. Profitability is what business is all about. However, some businesses choose to sell below their breakeven point in order to get the business for the first time. This is dangerous because the next time the tender is available, another business may tender below your price and you will lose out on all the profit. You should not accept a price below your breakeven point so that you make sure you do not lose money.

Before submitting your response to the tender, you should check all your pricing and costing. It is even suggested to get someone else to check it for you. Also check that all the requirements called for in the tender, are met in your proposal.

INTERNAL FACTORS IMPACTING UPON PRICING DECISIONS

The internal factors that impact upon price are:

- ✓ Product
- ✓ Promotion
- ✓ Distribution
- ✓ Cost

Product

- ✓ Level of quality
- ✓ Differentiating product lines within organisation
- ✓ Stage of the product life cycle
- ✓ Product design

Promotion

- ✓ Coupons, rebates, discounts, etc
- ✓ Advertising
- ✓ Sales & negotiation

Distribution

- ✓ Distribution channels involved
- ✓ Traditional channels vs. direct via Internet

Cost

- ✓ What does it cost to produce, promote, and distribute the product?
- ✓ Break-even analysis
- ✓ Total Cost (TC) = Fixed Costs (FC) + Variable Costs (VC)
- ✓ Total Revenue (TR) = Price x Quantity Sold
- ✓ Break-even point is where TC = TR
- ✓ Additional sales beyond this point will result in profit (TR-TC)
- ✓ Break-even analysis example - Manufacturing tennis shoes
- ✓ FC = equipment, facility lease (R100,000)
- ✓ VC = wages, leather (R20 per shoe)
- ✓ 5,000 pairs of shoes produced and sold
- ✓ TC=100000 + (5000 x 20) = R200,000
- ✓ Price to break even at 5,000 shoes sold = R200,000 / 5,000 = R40 per pair
- ✓ What would the break-even price be for 10,000 pairs of shoes?
- ✓ Cost-plus pricing
- ✓ Building upon the break-even analysis, we can add a desired profit to the cost side of the equation
- ✓ TC=FC +VC +desired profit

- ✓ Flat amount vs. percentage of costs
- ✓ Cost-minus pricing?

Organizational objectives

- ✓ Income = achieving maximum profits
- ✓ Sales = maintaining or enhancing market share
- ✓ Competitive = meet, avoid, or undercut competitors
- ✓ Social concern

EXTERNAL FACTORS IMPACTING UPON PRICING DECISIONS

In the tendering environment, it is the components which influence price sensitivity that should be considered

Competition Effect

You competitor's actions have a huge influence on your pricing decisions. Competitors will also react to your pricing decisions. It is important to monitor both your competitor's price levels and their reactions to your pricing moves. A competitor might lower his prices to respond to you cutting your prices. The competition can also launch a product that is similar to yours at a better price. This method can be reversed, when you use the competitor's prices as a guide for your pricing. It is very important that you constantly collect information on your competitor's prices. Try to meet or beat your competition.

Cost Effect

The cost of raw material is often beyond your control, yet it is a factor that affects all business.

The end benefit effect

How price sensitive are buyers? Will he/she cancel the tender if the price is above the limits? How important is the product for the buyer.

The total expenditure effect

How significant are buyer's expenditures in the product both in Rand terms and as a share of their total budgets?

The price/quality effect

Is a prestige/neutrality/expertise image an important attribute of the product? Is the product enhanced in value when its price excludes/includes some customers?

The sunk investment effect

Has the buyer of the products made complementary expenditures in anticipation of its continued use? For how long are buyers locked in by those expenditures?

The unique value effect

Does the product have any unique attributes that differentiate it from competing products? How much do buyers value those unique differentiating attributes?

The substitute awareness effect

What alternatives do buyers have (considering both competing brands and competing products)? Are the buyers aware of the alternative suppliers or substitute products?

The difficult comparison effect

How difficult is it for buyers to compare the offers of different suppliers? Can the attributes of a product be determined by observation, or must the product be purchased and consumed to learn what if offers? Are the prices of different suppliers easily comparable or are they stated for different sizes and combinations that make comparisons difficult?

REVIEW COSTING AND PRICING METHODS

Cost-orientated pricing

Many small businesses determine their basic price based on their costs. The idea is to set your price high enough to cover your costs and still make a profit (Van der Walt *et al.*, 1995)

Cost-plus pricing

Many small businesses use this method. Here you determine the cost of the product and then add a set percentage to the cost for the profit margin. This method is popular and easy to use.

Assume you are the manufacturer of steel fences. Your financial analysis showed the following:

Variable costs: R60

Fixed costs: R15 000

Expected sales 5000 fences

The unit cost for each fence is:

$$\text{Unit cost} = \text{Variable cost} + \frac{\text{Fixed cost}}{\text{Current sales}}$$

$$= R60 + \frac{15\,000}{5\,000}$$

$$= R63$$

Assume you want a profit margin of 40% (also called a mark-up)

Cost plus price = unit cost

(profit margin) = R63

40

= R105

You will charge customers R105 for each fence and make a profit of R42 per unit (R105-63 = R42)

Rate of return pricing

This method is similar to the previous one but brings another aspect into the calculation, namely the cost of investing your money into the business. The idea is to set a price that gives you a certain rate of return on your total investment. This differs from the cost-plus method, which gives you a certain profit margin per item sold.

To use this method you need:

- ✓ an estimate of the units that you will sell
- ✓ what each unit costs
- ✓ the total amount of money invested in making and selling the product
- ✓ the target rate of return that you want on your money

Target return price =unit cost + target rate of return x total money invested: estimated sales.

Customer orientated pricing

It is setting a price that is perceived by customers to be of value relative to what they get for the price (Van Der Walt *et al*., 1995:490)

Backward pricing

Estimation of the price that customers will be willing to pay

Prestige pricing

This method shows the quality or prestige of a product.

Odd-number pricing

Using prices ending in odd numbers or under a round figure e.g. R2.99 instead of R3.00.

Price lines

Use only a few prices for each of your product lines. E.g. economy line, value line, high quality line

Skimming and penetration pricing

When introducing a new product to the market you can use the skimming approach – price your product or service fairly high to recover your investment quickly or the penetration approach – Price your product relatively low. You will do this to break into new markets.

Bundle pricing

To combine two or more products at the same price; It is also a good way to introduce new products.

Leader pricing

This is when the business owner lowers the price on a popular product to attract more customers to the store. Although the business earns lower profit margins on the products, customers might buy other products that will improve the profits.

4.6. EXPENSES AND REVENUES

Expenses	Revenue
• Direct labour • Materials • Rent • Electricity • Travel • Entertainment • Office supplies • Salaries	• Income from Rentals • Royalties • Miscellaneous sources • Revenue from sales of products/services

Expenses accrued refers to expenses that relate to the financial year under review but which are not yet recorded in the general ledger because the invoices have not been received by the last day of the financial year.

Expenses are decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity participants.

Expenses prepaid refer to expenses paid in the current financial year, of which a portion relates to the current year and the balance to the next financial year(s).

Assess suppliers and new products in terms of potential contribution to profit and securing the tender

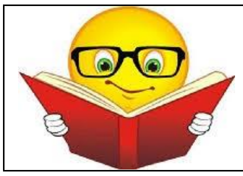
Activity	In your groups, referring to a tender document, make a list of your suppliers and their new products. Assess these suppliers and products to see if they will make a contribution to profit and securing the tender. Identify the one's that will make the biggest contribution to your profit and market share. Motivate why you would give preference to that particular supplier.

Suppliers	Products	Assessments

Motivation

Identify competing products/services considered in the tendering process

In the same groups, compare available products/services to each other and make a list of the products/services that you will consider in your tender.



Complete Activity in your Workbook

4.7. COMPLETE TENDER DOCUMENTS ACCURATELY

One of the conditions spelt out clearly in the "special conditions of tendering" is that it is the responsibility of the tenderer to ensure that all the documents are included in the package. Should documents be missing, please ask the issuer.

Before submitting tender documents see to the following:

- ✓ Your tender is a professionally presented document. It gives the impression that you are professional, reliable and efficient.
- ✓ Ensure documents are in the correct format.
- ✓ Allow sufficient time to complete the documents and submit on time.
- ✓ Remember that no fax/telex/electronic mail tender submissions will be allowed.
- ✓ Ensure that the place where the tenders must be submitted is known well in advance.

Carry out checks and balances on the costing and the input into the documents

As in all areas of your business, attention to detail is the key to success. Tendering carries a particularly heavy paper component, involving official forms and many other documents, depending of the nature of the tender.

Try to stick to the order and format adopted on the tender specification form. This will make your tender document easier to read than if you attach reams of information, which the adjudicator will struggle to find.

Ensure the following:

- ✓ All costs must be taken into account.
- ✓ All prices must be VAT inclusive.
- ✓ The tender price must include a profit.
- ✓ It is important that tender prices are calculated properly as any changes to the Tender price after the closing date, will result in the Tender being disqualified or the Tender incurring losses.
- ✓ Fill in and sign all forms in ink.
- ✓ Ensure that you address the documents correctly as stipulated in the tender documents.
- ✓ Supply the correct address for correspondence.
- ✓ State clearly, where requested, that you are authorised to offer the tender, and give proof of such authority.

- ✓ Seal the package/envelope and ensure that you clearly mark the tender number and the closing date and time on the outside.

Adhere to dates and times of submitting tenders

- ✓ It is important to have a clear understanding of the following concerning dates and times.
- ✓ Closing time: Means the date and the hour specified in the tender documents for the receipt of tenders.
- ✓ Timeliness: With respect to supplies, timeliness means delivering the requisitioned supplies to the end user in the quantity and at the time necessary for the end user's purposes. With respect to services, timeliness means performance at the time necessary for the end user's purposes.
- ✓ It is very important to adhere to dates and times, if it they are not adhered to it will lead to disqualification of the tender.
- ✓ Example of dates and times specified in a tender document: factors regarding dates and times are underlined.

Rules of engagement in the Tender process

The rules of engagement in the Tender process, as stipulated below must be adhered to at all times. Failure to do so will result in *disqualification* from the Tender process.

The following rules of engagement will apply:

The completed Tender documentation must be returned to SARS by no later than 11h00 on 19/11/2009

The Tender documentation must be sealed in an envelope on which the following information is clearly indicated:

The name and address of the tenderer;

Tender number; and

Closing date

The Tender documentation may be posted to SARS (for attention of Mr. M Buthelezi, Block D) or be placed in the tender box at the main gate entrance, LeHae La SARS, 299 Bronkhorst Street, Nieu Muckleneuk, Pretoria <u>before the closing time.</u>

No extensions for return of the response and submissions will be granted.

Questions for clarification of issues must be directed in writing to the SARS Procurement Centre: Ms N.Dlambewu Tel 012 422 4057

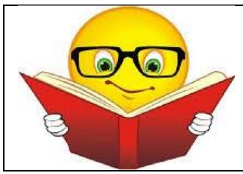
Any attempt to gain information in a manner deemed to be unfair or disadvantageous to other respondents or any attempt to influence the outcome of the response evaluation will result in immediate disqualification from the Tender process. Failure to comply with the completion regulations listed in section 5.1 will result in *disqualification* from the selection process.

The front page of this document must be completed and attached to the Response Sheet and the submissions.

4.8. WHAT IF YOU ARE UNSUCCESSFUL?

If you are unsuccessful you may ask for feedback from the tender evaluation team or business. They have to provide you with feedback if you have requested this within 15 days. The request will have to be in writing.

If you are unsuccessful with one tender, do not be disheartened. This does not mean that you will be unsuccessful on other tenders. Use the feedback to help you with future bids.

	*Complete Activity in your Workbook*

4.9. PRICE NEGOTIATION

In negotiation, there are many tactics that you may meet or use. They can be fair, foul or something in between, depending on the competitive or collaborative style of the people involved and the seriousness of the outcomes. Outlined below are few price negotiation techniques that can be used.

1. Better Offer

When the other person makes an offer, say that you have already received a better offer from somebody else. If they ask what that offer is; then you may or may not choose to tell them. If you do, then you have the opportunity to set a lower limit that the other person knows that they cannot go below.

Example:

Sorry, I've already had a better offer that.
I was offered twice that price only last week.

A better offer from elsewhere is a walk-away alternative that you can deploy at any time. The other person does not know whether you actually do have a better offer or whether you are bluffing. The problem for them is that if they call your bluff then you might actually have such an offer. If you actually do have a better offer, you are indeed in a stronger position if you do need to conclude the deal. As a part of developing your walk-away, you would have also better understood the overall situation and built your own confidence -- which alone is worth the effort of looking elsewhere beforehand

2. Better than that

When the other person makes an offer, say 'You'll have to do better than that!'.
You can accompany this with a saddened, shocked or disgusted look.
Then be quiet and wait for the "to do better".
Example:
A person buying a car asks for the price. The sales person says it. The buyer raises an eyebrow and mutters 'You'll have to do better than that.' and looks, appraisingly at the sales person.
Oh, come one. I'm not a fool. You'll have to do better than that.

When you say 'You'll have to do better than that', you are actually implying that you know that the other person is trying to deceive you, for example with an exorbitantly high price. Having been 'found out' (although you actually may not know what a fair price is), this puts them under social pressure to conform to norms of decency and fair pricing.

3. Cards on the table

Tell the other side exactly what you want or give them information that they did not know before.
Explain why you are doing this, for example is because you trust them or because you are in a hurry.
Example:
Look, I'll put my cards on the table. What I really want is...
I think I can trust you. The full story of why I need the ticket is that...
Sorry, the truth of the matter is that Mike says I have to do this.

In card games, putting your cards on the table is showing others exactly what you have. When a person 'puts their cards on the table' they are asking the other person to believe them. By using such a gesture and also talking about why they are doing it, they are asking the other person to accept that they are being trustworthy. Which they may not be, of course

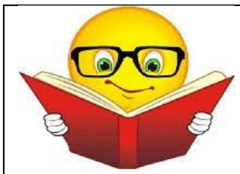
4. Deadlines

Set a deadline by which the other person has to decide or act. Make it clear that this is an absolute time by which they must do what you want them to do.
As the deadline approaches, increase the emotional atmosphere, talking more about what will happen if the deadline is missed. This may be specific and threatening actions or vague and disturbing hints. Use things which cannot be challenged, such as contract completion dates, demands made by senior people and so on.
Example:
I must have your answer before we leave today.
I am talking to Steve later. He will want to know what we have agreed.
The product will be released at the end of the week. If you can't deliver by Thursday, it will be too late.

A deadline creates tension in the scarcity of time that it gives and the imagined consequences of not reaching the deadline. Hurrying people up reduce the time they have for reflection and considered thought. If you can occupy them with worries about what may happen if the deadline is not met, then they will spend less time thinking of objections and counter-arguments to your suggestions. Deadlines can easily be challenged, but it is surprising how often they are not questioned.

5. Expanding the pie
Change the frame of the negotiation from a zero-sum, win-lose game to a win-win scenario where both sides can benefit more by working together on mutual benefits.
Example:
Two business competitors on an industry standards committee agree to settle differences and promote the standard as this will help increase the number of total customers, thereby giving each a greater market value.
A husband and wife who are negotiating about holidays and the ability to take time off work reframe the situation as 'getting away together' and end up with a decision that when one goes away on business the other will go along too.

In many negotiations there is an assumption that it is win-lose, and with every gain that one person makes the other person will lose an equal amount. In a worst-case scenario (which is surprisingly common), it becomes personal and the sense of fair play (or even getting what I need) goes out of the window as each player seeks to harm the other before they get harmed themselves.
This is a limiting perception and it is often possible for both people to gain, especially if they collaborate. 'Expanding the Pie' comes from the metaphor where people are negotiating about a single pie, such that where one person gets more of the pie it is clear that the other person gets less. If both parties work together to get a bigger pie, then both can have more.

	*Complete Activity in your Workbook*

DIRECT COSTS

Direct costs can be traced directly to a cost object such as a product or a department. In other words, direct costs do not have to be allocated to a product, department, or other cost object.

For example, if a company produces artisan furniture, the cost of the wood and the cost of the craftsperson are direct costs—they are clearly traceable to the production department and to each item produced—no allocation was needed. On the other hand, the rent of the building that houses the production area, warehouse, and office is not a direct cost of either the production department or the items produced. The rent is an indirect cost—an indirect cost of operating the production department and an indirect cost of crafting the product.

To calculate the total cost of the production department or to calculate each product's total cost, it is necessary to allocate some of the rent (and other indirect costs) to the department and to the product.

INDIRECT COSTS

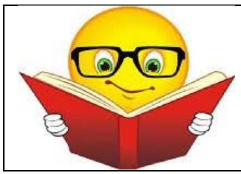
Indirect costs are business expenses that are not directly related to a particular product or function within the general operation. Costs of this type tend to have an impact on the overall operation of the business, making it very difficult to charge the costs to a specific department or associate them with one function. Costs of this type are sometimes referred to as overhead, a term that helps to describe the broad application of these costs.

There are many examples of indirect costs that occur in both small and large businesses. General supplies for the administration of the business are one example. Items such as paper, pens, and other essentials that are utilized in the record keeping and general clerical functions of each department are often classified as an indirect cost. In like manner, services such as auditing the accounting books or the preparation of legal documents are expenses that impact the entire operation and are usually considered indirect in nature.

Several of the expenses related to the upkeep and maintenance of business facilities are considered indirect costs. Utilities such as electricity, water, and Internet access are expenses that benefit the business in general and thus are classified as overhead expenses. In like manner, the cost of renting or leasing business space is also part of the overhead, making it an indirect cost.

There are examples of what may appear to be an indirect cost actually being a direct cost. One example has to do with employee salaries. When the employees are performing their usual functions, they are benefiting the business as a whole; their wages and salaries are considered indirect costs. However, if those same employees are assigned to a specific project that is the sole focus of their workday for a period of several days or weeks, their wages or salaries can be considered a direct cost, with that cost directly applied to that project.

Companies in different parts of the world handle the documentation of indirect cost allocation differently. Some choose to create a general line item that accounts for all indirect costs. Others choose to create a line item in the budgets of each department and divide the overhead among them equally. Because the revenue arms of many national governments provide specific instructions on how to classify an expense as direct or indirect, companies operating within a specific jurisdiction will adjust their classification of direct and indirect costs to comply with those instructions

	*Complete Activity in your Workbook*

	ANNEXURE 1: GROWTH ACTION PLAN

The personal development plan will enable you address any areas of weakness that you identify during the course and stimulate your desire for personal growth.

Growth Action Plan			
I have identified the following as areas in which I need to improve in order to become competent. List in order of priority.			
Actions to be taken	Resources	Completion date	Evidence

Learner Name:______________________________Signature:____________________

Facilitator Name: ___________________________Signature:____________________

ANNEXURE 2: WORDS THAT ARE NEW TO ME

Compile a list of words that is new to you and discuss the meaning of the words with your facilitator

Term	Description
e.g. characteristic	Trait, feature, quality, attribute, etc

Learner Name:______________________ Signature:____________________

Facilitator Name: ____________________Signature:____________________

ANNEXURE 3: TRAINING EVALUATION

Training Programme	
Facilitator Name	
Date	

Ratings:

1	Poor
2	Areas for Improvement
3	Meet the standard requirements
4	Very Good
5	Excellent

Tick where appropriate

Did the training relate to your job e.g. skills, knowledge?	1	2	3	4	5
Comments:					
To what extent will your performance improve as a result of attending this training	1	2	3	4	5
Comments:					
To what extent would you recommend this course to others?	1	2	3	4	5
Comments:					
Did this training meet your desired needs?	1	2	3	4	5
Comments:					
Was the training material user friendly / easy to understand?	1	2	3	4	5

ANNEXURE 4: EVALUATION OF FACILITATOR

Ratings:

1	Poor
2	Areas for Improvement
3	Meet the standard requirements
4	Very Good
5	Excellent

Tick where appropriate	1	2	3	4	5
Preparation for the training					
Knowledge of subject					
Handling of questions					
Interaction with participants					
Voice clarity					
Use of training aids (flip charts, handouts, etc)					
Facilitator made training exciting					
Recommendation of facilitator for future training					

Other comments on facilitator’s delivery of this training:

ANNEXURE 5: RESOURCES

We gratefully acknowledge various sources of information which have been used in the development of this material, and apologize for unacknowledged sources.

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