



U.S. Small Business
Administration

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Business Model vs Economic Model

Business Model

How the business
creates and delivers
value to the customer

Economic Model

How the business
captures that value
in the form of
an economic return

Economic Model of a Business



Revenue Drivers

- How many ways does your company have to earn money?
- One source or several?
- Implications for risk?
- Is this a competitive advantage?
- Or a disadvantage?

Margins

Difference between *Price and Cost*

- What *price* do you charge for your product or service?
- How much does it *cost* you to deliver that single unit of product or service?
- Does difference between price you charge and cost of production provide adequate cash to cover fixed operating expenses and generate a profit?

Volume

The number of units of product or service you are selling or providing.

- Is generally meaningless unless you discuss it along with margin
- High volume alone is meaningless unless you keep something from each sale (margin)

Operating Leverage

Operating Leverage is the relationship between ***variable costs*** and ***fixed costs***.

- Higher fixed cost model = high operating leverage
- Higher variable cost model = low operating leverage

What is the difference between *variable* and *fixed costs*?

Implications of Operating Leverage

Higher fixed costs (higher operating leverage) means

- Greater risk
- It takes more units of service each month to breakeven
- But, once you get to breakeven, you make a lot more money

Lower fixed costs (low operating leverage) means

- Less risk
- It takes less units of a service or product each month to breakeven

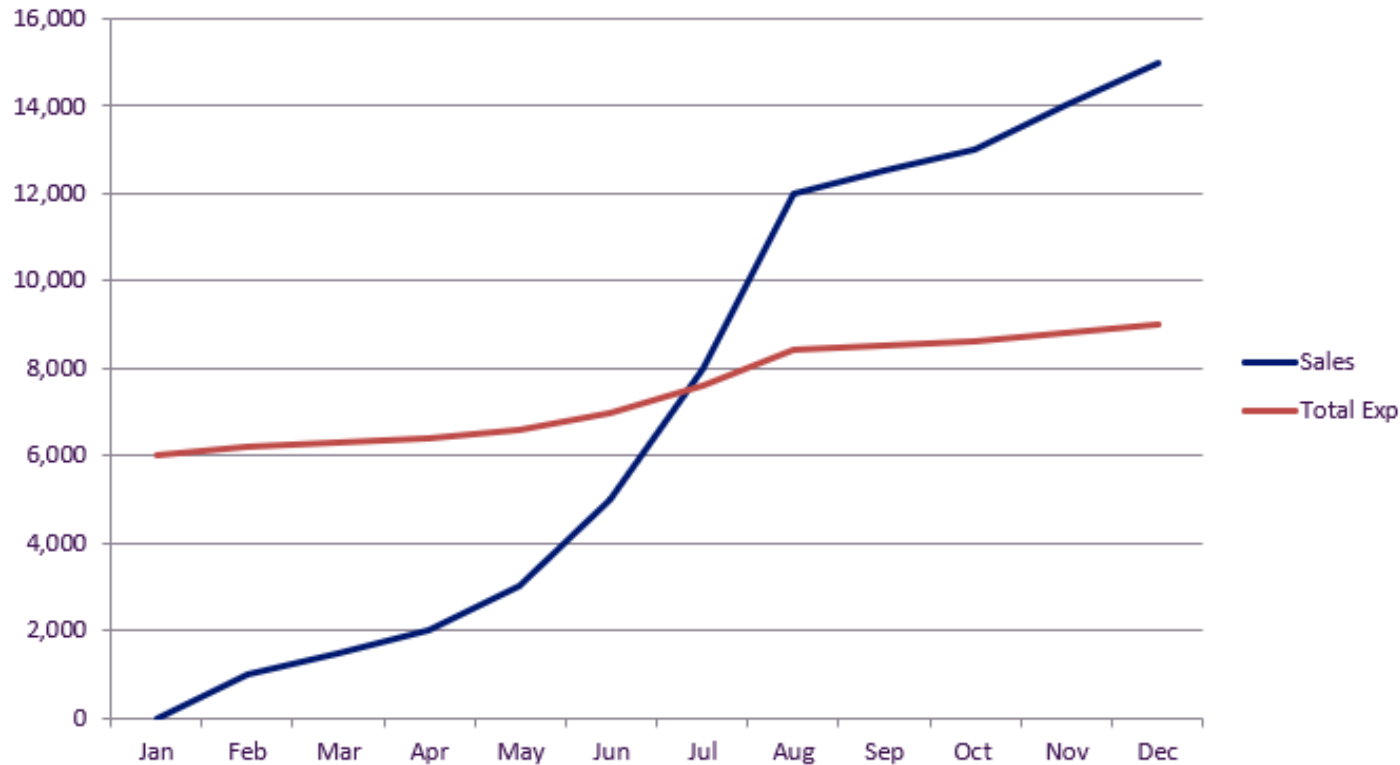
Variable Costs

- Change in direct relation to your revenue
- What does it actually cost to deliver one unit of whatever you do?
- Direct labor, payroll taxes and costs per employee (CPEs), mileage, packaging, unit transport or delivery, raw materials
- *Variable* does not = *optional*

Fixed Costs

- Expenses you have to pay no matter what sales you generate
- Remain the same over a given period of time
- Include rent, brick and mortar location, salaries (not hourly pay), advertising, insurance, write-off of equipment
- What do you think about utility bills? Variable or fixed?

Breakeven



Definition: The volume of sales revenue needed to cover all of your costs over a given period of time.

Financial Statements

BALANCE SHEET: Snap shot of a firm's assets and claims against those assets. Shows what the company owns, owes and how it is financed.

INCOME STATEMENT: Shows revenue and expenses and provides a 'bottom line' of profitability over a specified period.

CASH FLOW STATEMENT: Shows sources and uses of cash as well as net change on cash over a specified period.

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Sample Balance Sheet

ASSETS

Current Assets

Cash	\$123,000
Marketable Securities	200,000
Accounts Receivable	345,000
Inventories	100,000

Total Current Assets \$768,000

Long-Term Assets

Building (Gross)	\$350,000
- Accumulated Depreciation	<u>-50,000</u>
Net Building	\$300,000
Land	\$325,000

Total Long-Term Assets \$625,000

Total Assets \$1,393,000

LIABILITIES

Current Liabilities

Accounts Payable	\$100,000
Notes Payable	<u>150,000</u>

Total Current Liabilities \$250,000

Long-Term Note \$300,000

Total Liabilities \$550,000

Owner's Equity \$843,000

Total Claims \$1,393,000

Sample Income Statement

OPERATING ACTIVITIES, CASH FLOWS PROVIDED BY OR (USED) IN:	
Net sales	\$1,200,000
Cost of Goods Sold	850,000
Gross Profit	\$350,000
Selling, general, and admin. expenses	311,000
Income from operations	\$39,000
Interest expense	9,000
Income before taxes	\$30,000
Income taxes	12,000
Net Income	\$18,000

Sample Cash Flow Statement

OPERATING ACTIVITIES, CASH FLOWS PROVIDED BY OR (USED) IN:

Depreciation/Amortization	\$50,000
Changes in A/R	(\$345,000)
Changes in A/P	\$100,000
Changes in Inventory	(\$100,000)
Total Cash Flow from Operating Activities	(\$277,000)

INVESTING ACTIVITIES, CASH FLOWS PROVIDED BY OR (USED) IN:

Payment for acquisition of PPE	(\$350,000)
Sale of PPE	\$0
Total Cash Flow from Investing Activities	(\$350,000)

FINANCING ACTIVITIES, CASH FLOW PROVIDED BY OR (USED) IN:

Issuance of Stock	\$600,000
Dividends	
Net Borrowings	\$150,000
Total Cash Flows From Financing Activities	\$750,000
Net increase/Decrease in Cash:	\$123,000
Cash at beginning of period	\$0
Cash at end of period	\$123,000

Sample Cash Flow Projections

Cash Flow Forecast - 12 Months

Total Sales: \$ 250,000

Client name

4/5/22

Month:		Pre-Start	May-22	Jun-22	Jul-22	Aug-22	Sep-22	Oct-22	Nov-22	Dec-22	Jan-23	Feb-23	Mar-23	Apr-23
Percentage Of Total Sales			8%	8%	8%	12%	10%	9%	8%	8%	7%	6%	8%	8%
Receipts														
	100%													
Sales	Product 1	75.0%	\$ 15,000	\$ 15,000	\$ 15,000	\$ 22,500	\$ 18,750	\$ 16,875	\$ 15,000	\$ 15,000	\$ 13,125	\$ 11,250	\$ 15,000	\$ 15,000
	Product 2	23.0%	\$ 4,600	\$ 4,600	\$ 4,600	\$ 6,900	\$ 5,750	\$ 5,175	\$ 4,600	\$ 4,600	\$ 4,025	\$ 3,450	\$ 4,600	\$ 4,600
	Product 3	2.0%	\$ 400	\$ 400	\$ 400	\$ 600	\$ 500	\$ 450	\$ 400	\$ 400	\$ 350	\$ 300	\$ 400	\$ 400
	New equity inflow													
	Loans received	\$ -												
	Other													
Total Receipts		\$ -	\$ 20,000	\$ 20,000	\$ 20,000	\$ 30,000	\$ 25,000	\$ 22,500	\$ 20,000	\$ 20,000	\$ 17,500	\$ 15,000	\$ 20,000	\$ 20,000
Payments														
Cost of Goods Sold	Product 1	50.0%	\$ 7,500	\$ 7,500	\$ 7,500	\$ 11,250	\$ 9,375	\$ 8,438	\$ 7,500	\$ 7,500	\$ 6,563	\$ 5,625	\$ 7,500	\$ 7,500
	Product 2	35.0%	\$ 1,610	\$ 1,610	\$ 1,610	\$ 2,415	\$ 2,013	\$ 1,811	\$ 1,610	\$ 1,610	\$ 1,409	\$ 1,208	\$ 1,610	\$ 1,610
	Product 3	0.0%												
	Salaries and wages		\$ 1,200	\$ 1,200	\$ 1,200	\$ 1,200	\$ 1,200	\$ 1,200	\$ 1,200	\$ 1,200	\$ 1,200	\$ 1,200	\$ 1,200	\$ 1,200
	Workman's Comp.	3.5%	\$ 42	\$ 42	\$ 42	\$ 42	\$ 42	\$ 42	\$ 42	\$ 42	\$ 42	\$ 42	\$ 42	\$ 42
	Payroll taxes	15.3%	\$ 184	\$ 184	\$ 184	\$ 184	\$ 184	\$ 184	\$ 184	\$ 184	\$ 184	\$ 184	\$ 184	\$ 184
	Advertising		\$ 1,000	\$ 1,000	\$ 2,000	\$ 2,500	\$ 2,000	\$ 1,500	\$ 1,000	\$ 1,000	\$ 1,500	\$ 1,500	\$ 1,000	\$ 1,000

QUESTIONS?