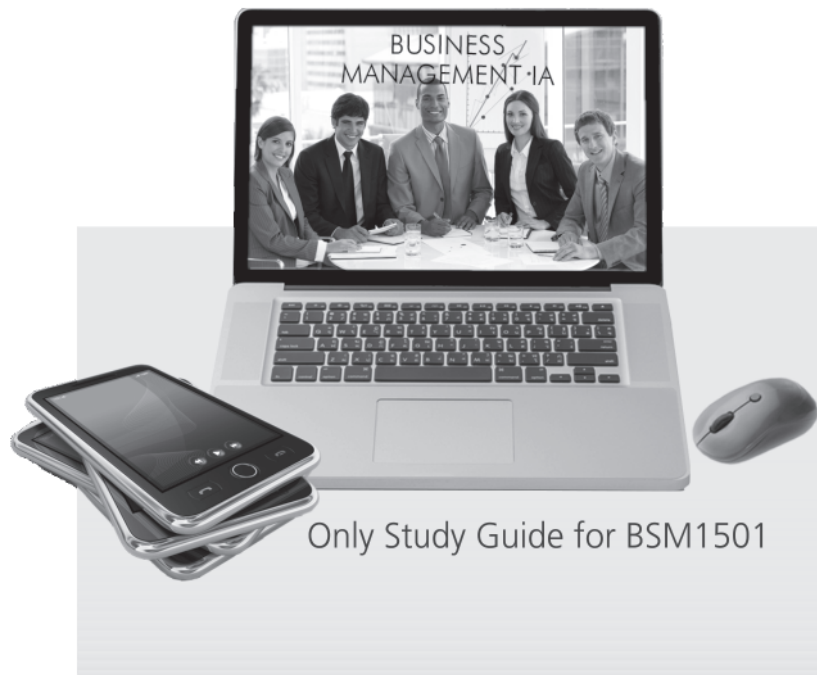


BUSINESS MANAGEMENT 1A

ENTREPRENEURSHIP

and how to establish your own business



DEPARTMENT OF BUSINESS MANAGEMENT
PRETORIA

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INTRODUCTION

Welcome

It is a great pleasure to welcome you to this module. We hope that you will enjoy this course. This study guide is merely a summary of the contents in your prescribed textbook.

PURPOSE OF THE MODULE

The purpose of the module *Entrepreneurship and how to establish your own business* is for you to acquire foundational concepts in business management. This module will develop your understanding of entrepreneurship and it will teach you how to become an entrepreneur and introduce you to the route that you have to follow to start your own business. It provides a foundation for all later modules in this subject.

LINK TO OTHER MODULES

This module does not stand alone. It is an integral part of Business Management I. The purpose and the learning outcomes of this module are therefore aimed at developing your expertise and abilities in the field of entrepreneurship.

MODULE OUTCOMES

Module outcomes

After completing this module, you should have the competence to identify and start a small business with the necessary assistance and support, and to develop business plans that comply with appropriate laws and that reflect an ethical approach to management.

The intended outcomes can be distinguished as follows:

SPECIFIC OUTCOMES	ASSESSMENT CRITERIA
1. Compile a business plan with assistance	1.1 Apply market research techniques and the SWOT analysis to identify and evaluate opportunities, sketch customer profiles and identify competitive advantages. 1.2 Apply financial and marketing knowledge and planning and information technology skills to generate a business plan.

2. Implement a business plan with assistance	2.1 Apply knowledge of the business world and communication and networking skills in obtaining a support base. 2.2 Use knowledge of legal requirements to register an enterprise and ensure compliance. 2.3 Apply knowledge of business practice to obtain the necessary resources. 2.4 Identify entrepreneurial skills to start an enterprise according to the business plan.
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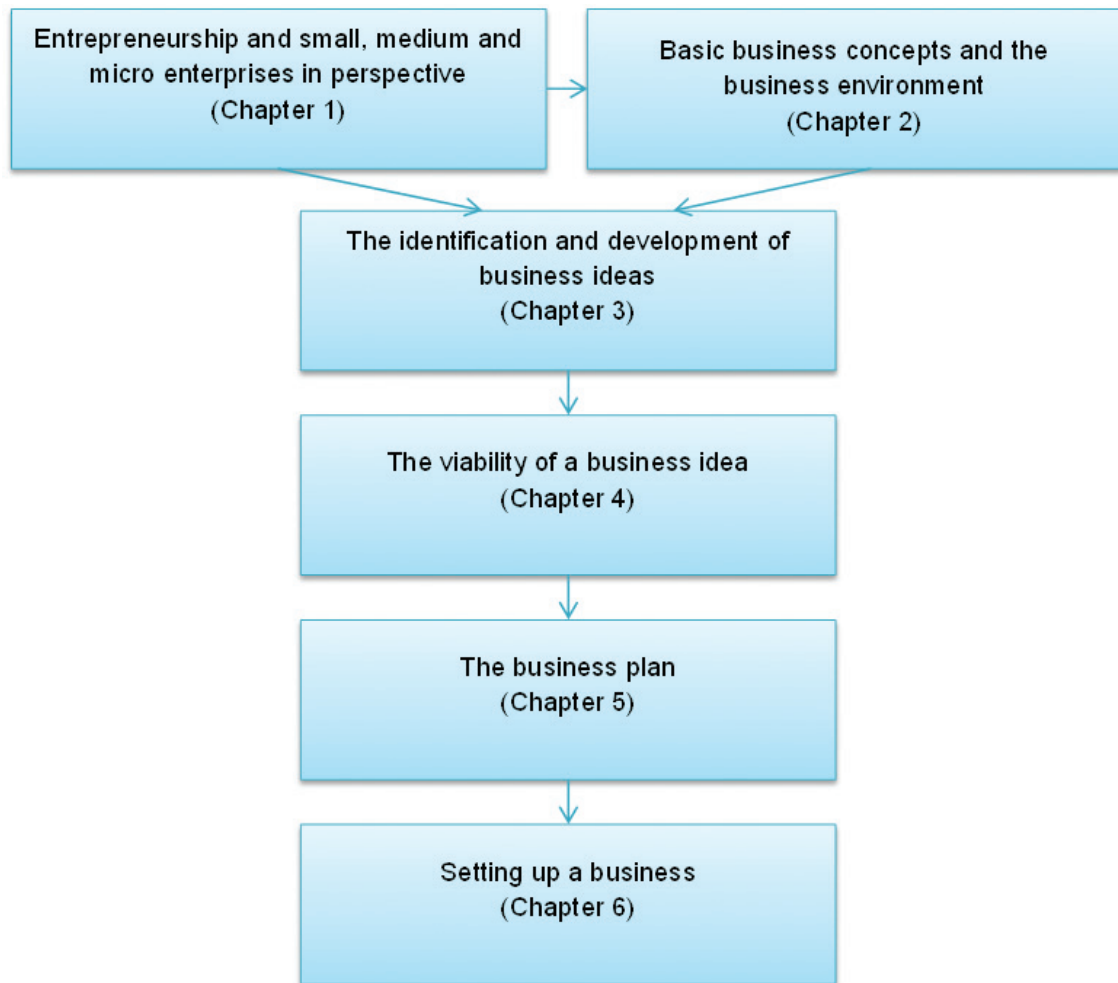
Framework of the module

The following six chapters of the prescribed textbook provide the framework for this module:

CONTENTS
CHAPTER 1 – ENTREPRENEURSHIP AND SMALL, MEDIUM AND MICRO ENTERPRISES IN PERSPECTIVE
CHAPTER 2 – BASIC BUSINESS CONCEPTS AND THE BUSINESS ENVIRONMENT
CHAPTER 3 – THE IDENTIFICATION AND DEVELOPMENT OF BUSINESS IDEAS
CHAPTER 4 – THE VIABILITY OF A BUSINESS IDEA
CHAPTER 5 – THE BUSINESS PLAN
CHAPTER 6 – SETTING UP A BUSINESS

A mind map for the prescribed textbook

Entrepreneurship and how to establish your own business



Composition of the study/learning package for the module

The study package for this module consists of this study guide and tutorial letter 101. You must purchase the prescribed book as soon as possible. The prescribed book is vital because you will not be able to complete this module successfully without it.

COMPLETING ACTIVITIES, SELF-ASSESSMENT QUESTIONS AND ASSIGNMENTS

We consider the completion of the activities and self-assessment questions in the tutorial letters and the assignments as crucial to the successful understanding of this module.

Activities

You will come across various types of activities in this study guide:

- reflecting on work covered
- completing self-assessment questions
- doing self-assessment by means of the suggested solutions to the self-assessment questions

We consider your completion of the activities in the study guide and the assignments as crucial to your successful completion of this module. The activities in the study guide will guide you on how to manage the content of the study material.

Self-assessment questions

At the end of each learning unit you will find self-assessment questions based on the work done in the chapter. We advise you to work through these questions diligently, since they provide extremely useful opportunities to prepare yourself for possible examination questions. Self-assessment plays a very important role in mastering learning outcomes and you should therefore complete the self-assessment activities in the study guide. You will find most of the answers to these questions in the study material covered in the study guide and the prescribed textbook.

Assignments

By completing the assignments that appear in Tutorial Letter 101, you will get an idea of the types of questions you can expect in the examination and obtain first-hand feedback from your lecturer. The assignments as well as the examination comprise only multiple-choice questions. For every question there are four options, numbered from 1 to 4, of which you must select only one. For example:

*The **internal business environment** consists of the ...*

- (1) micro-environment.
- (2) market environment.
- (3) macro-environment.
- (4) economic environment.

You cannot select more than one option. In other words, your answer will be option 1 or 2 or 3 or 4.

Sometimes the question asks you to select the wrong statement. You should be extra careful when answering such questions and not get confused by marking a statement that is correct (because you will not earn a mark). Please look at the assignments in Tutorial Letter 101. You will find the occasional question asking you to indicate which of the options is wrong.

In some questions, however, there will be several statements that could be correct. In such cases the statements will always be indicated by letters (a, b, c and d) and the answer will still be option 1, 2, 3 or 4, but these answers may refer to more than one statement. For example:

The market environment consists of the ...

- a. mission and objectives of the enterprise.
- b. consumers.
- c. factors of production.
- d. competitors.

Choose the correct option:

- (1) a, b
- (2) b, c
- (3) c, d
- (4) b, d

This question asks you to indicate which of the statements are correct. If you therefore think that statements b and d are correct, you will mark only option 4 as the correct answer.

In all the above examples the stem of the question asks you to identify the correct statement(s). Sometimes the alternatives are a continuation of the stem. For example:

The needs and preferences of consumers refer to the ... environment.

- (1) economic
- (2) physical
- (3) social
- (4) technological

In an example such as the above you have to read the stem plus option 1, then you have to read the stem again plus option 2, the stem plus option 3, and so on.

Answering a multiple-choice question

Make a photocopy or record your answers on a separate page

You will find the multiple-choice questions in the assignment extremely useful when you prepare for the examination. However, if you mark your answers (or the correct answers) on the actual page in Tutorial Letter 101, you will not be able to use these questions for revision. We strongly recommend that you either make a photocopy of the assignments and use that for revision, or else write down your answers on a separate sheet of paper to avoid making any marks on Tutorial Letter 101 itself. You will then be able to work through these questions again in preparation for the examination, without seeing the marks that indicate the correct answers.

Decide on each option independently

When answering a multiple-choice question, much time is often wasted (especially in the examination) by reading all four options, before deciding which one is correct. The secret is to read and decide on each option separately. For example, look at question 1 above. The stem asks you to identify which statement is correct. Take a ruler and cover

the other three statements so that you see only statement 1. Read it and then, without reading any other statement, decide whether the statement is correct, wrong or that you don't know. Put a tick next to it if you think it is correct; put a cross next to it if you think it is wrong; and put a "?" if you are not sure. Then move the ruler down so that you can read statement 2. Again decide and mark the category in which it falls.

When you have done that with every one of the four statements, you may find that you have marked one statement correct and three statements wrong. The former is then your answer. If you find that you have marked two correct, then compare the two statements and choose the one that seems to be the most correct, or the most comprehensive.

Write down your reasoning

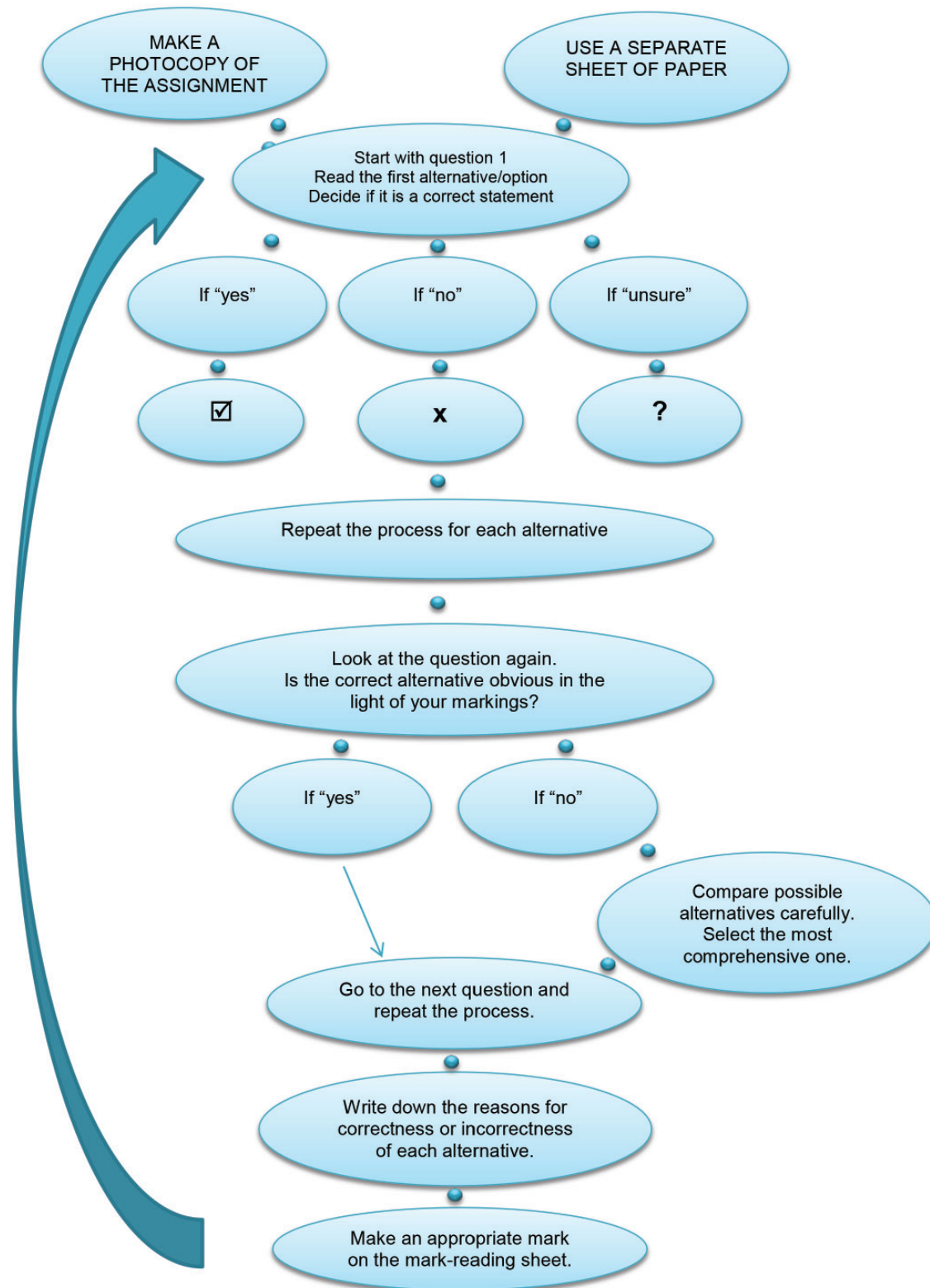
When you have selected your answer to a particular question, it is essential that you write down your reasons for doing so. For example, if you choose option 4 as the correct answer to question 2 above, implying that statements b and d are correct, you should write on a separate sheet of paper why you think statements b and d are correct. Write down the actual reference in the prescribed book on which you base your reasoning. However, you must even go a step further. You must also write down why options a and c are wrong. Again make specific reference to the prescribed book to back up your reasoning.

This is probably the most important learning step that you can take. We want our students to understand the tutorial matter and to be able to explain the concepts and apply the principles. We are not interested in whether a student has memorised the tutorial matter and can repeat it in an examination. That is why it is so important for you to be able to give a reason for your answer.

It takes a few weeks from the time that you answer an assignment to the time that you get back the correct answers and explanations. By that time you will have forgotten why you chose a certain option for a particular question, unless you wrote down your reasons.

The real learning takes place when you compare your reasoning with that of the lecturers. So don't take the easy way out by just answering the multiple-choice questions.

The flow diagram below will help you to picture the process.



Assessment of your progress in this module

You will be assessed during the semester on your assignments and in the examination at the end of the semester against transparent assessment criteria which relate directly to the outcomes of this module.

The compulsory assignment marks will count in your final assessment towards your total mark. Further details of the assessment and examination requirements of this module are provided in Tutorial Letter 101.

HOW YOU WILL BENEFIT FROM THIS COURSE

This course will empower you with the ability to generate ideas for your own enterprise and to test the feasibility and viability of these ideas. It will also assist you in drawing up your business plan and implementing your idea in practice.

HOW TO APPROACH YOUR STUDIES IN BSM1501

Tutorial Letter 101 and the study guide will direct you on how to approach the study material and other resources and how to use them to your benefit. Tutorial Letter 101 also informs you who to contact for academic and administrative matters and it guides you on how to manage your time.

In the study guide we make a definite distinction between the parts of the prescribed textbook that you have to read and those parts that you have to study.

- **Studying**

The sections that you have to study are clearly indicated and form the basis of assignments and the examination. To be able to do the activities and assignments for this module, to achieve the learning outcomes and to be successful in the examination, you will need a deep understanding of the content of these sections in the study guide and the prescribed textbook. To deeply understand the study material, you must, firstly, accept responsibility for your own studies. Secondly, learning is not the same as memorising. You will be expected to show that you understand and can apply the information, not just remember it.

- **Reading**

In some parts of the study guide you will be required to read a certain section in the prescribed textbook or the study guide. This means that you should take note of the contents since it usually contains useful background information or offers another perspective or further examples. It will give you some context, improve your ability to take notes and enhance your understanding.

You must spend at least 120 hours on this module. This includes approximately 40 hours of reading and studying the study material, 40 hours of activities and assignments and 40 hours of preparing for the examination. We encourage you to compile a study plan that makes provision for enough time to cover the various topics, chapters, self-assessment questions and assignments.

- **How to approach a case study**

First read through the case study without trying to analyse it in any way, then read through the questions asked on the case study. Make sure that you understand the theoretical basis




for each question. You cannot look for a solution before you are completely sure what the question is about. Read through the case study again and remember the contents of the questions. Start working through the case study and identify the specific information you need to answer each question. Integrate the theory with the information from the case study by indicating how the theory has or has not been applied. Draw your own conclusions.








- **Preparing for the examination**


When preparing for the examination, we suggest that you study chapter 1 in the prescribed textbook first, then study the information in learning unit 1 in the study guide. After working through both chapter 1 and learning unit 1, try to answer the self-assessment multiple-choice questions in the study guide without looking at the answers. Evaluate your answers with the aid of the answers provided afterwards. Answer the questions about chapter 1 in Assignment 02 again. Evaluate your answers with the aid of the memorandum provided in Tutorial Letter 201. Repeat this exercise for each chapter in the prescribed textbook. Phone us if there is anything that you are not sure about – before the exams!

USE OF ICONS

Certain icons are used throughout the study guide:

ICON	DESCRIPTION
	The key concepts icon draws your attention to certain keywords or concepts that you will come across in the chapter concerned.
	The learning objectives indicate what aspects of the particular chapter you have to master.
	Mind maps are provided to help you to identify the relationship between various parts of the study material.

<p>STUDY</p> 	<p>The study icon indicates which sections of the prescribed textbook or study guide you need to study.</p>
<p>READ</p> 	<p>The read icon will direct you to certain sections of the prescribed textbook which you should read for background information.</p>
<p>ACTIVITY</p> 	<p>The activity icon refers to activities that you must do to develop a deeper understanding of the study material.</p>
<p>FEEDBACK</p> 	<p>The feedback icon indicates that comments are provided on how you could have answered the self-assessment activities.</p>
<p>ASSESSMENT</p> 	<p>When you see the assessment icon, you will need to test your knowledge, understanding and application of the material you have just studied.</p>
<p>TIME OUT</p> 	<p>The time-out icon indicates that you should take a rest because you have reached the end of a chapter or topic.</p>
<p>WEBSITE</p> 	<p>The website icon will refer you to a website link with additional relevant and interesting information about a certain topic.</p>

<p>VIDEO</p> 	<p>The video icon will refer you to a youTube video to watch. This video will contain additional relevant and interesting information on a certain topic.</p>
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CONCLUDING REMARKS

In the remaining parts of study guide we provide you with the learning units of this module (available under the “Learning Units” tab/tool on myUnisa).

You need to access myUnisa for any additional information and study material (for example online activities, self-assessments, material and – most importantly – announcements).

We hope that you will enjoy your studies! We certainly look forward to being your partners in this learning journey.

Best wishes

Your lecturer for BSM1501
Department of Business Management
Unisa

Learning Unit 1

Entrepreneurship and small, medium and micro enterprises in perspective

STUDY CHAPTER 1 IN THE PRESCRIBED BOOK

CONTENTS

- Definition of the concept of entrepreneur
 - The relationship between entrepreneurship and small business management
 - The relationship between entrepreneurship and intrapreneurship
 - Types of entrepreneurial businesses
 - Franchisors and franchisees
 - Key success factors of entrepreneurs
-



LEARNING OBJECTIVES

When you have worked through learning unit 1, you should be able to

- *explain the terms “entrepreneur”, “intrapreneur” and “small business manager”*
 - *explain the similarities and differences between entrepreneurship, intrapreneurship and small business management*
 - *distinguish between informal and formal businesses*
 - *explain the role of informal businesses in South Africa*
 - *distinguish between micro, very small, small, medium and large enterprises*
 - *explain the difference between the franchisor and the franchisee*
 - *describe the key success factors that contribute to successful entrepreneurship*
 - *explain and give a critical evaluation of the following concepts:*
 - *personal skills, expertise and aptitudes*
 - *personal characteristics of an entrepreneur*
 - *functional management skills of an entrepreneur*
-



KEY CONCEPTS

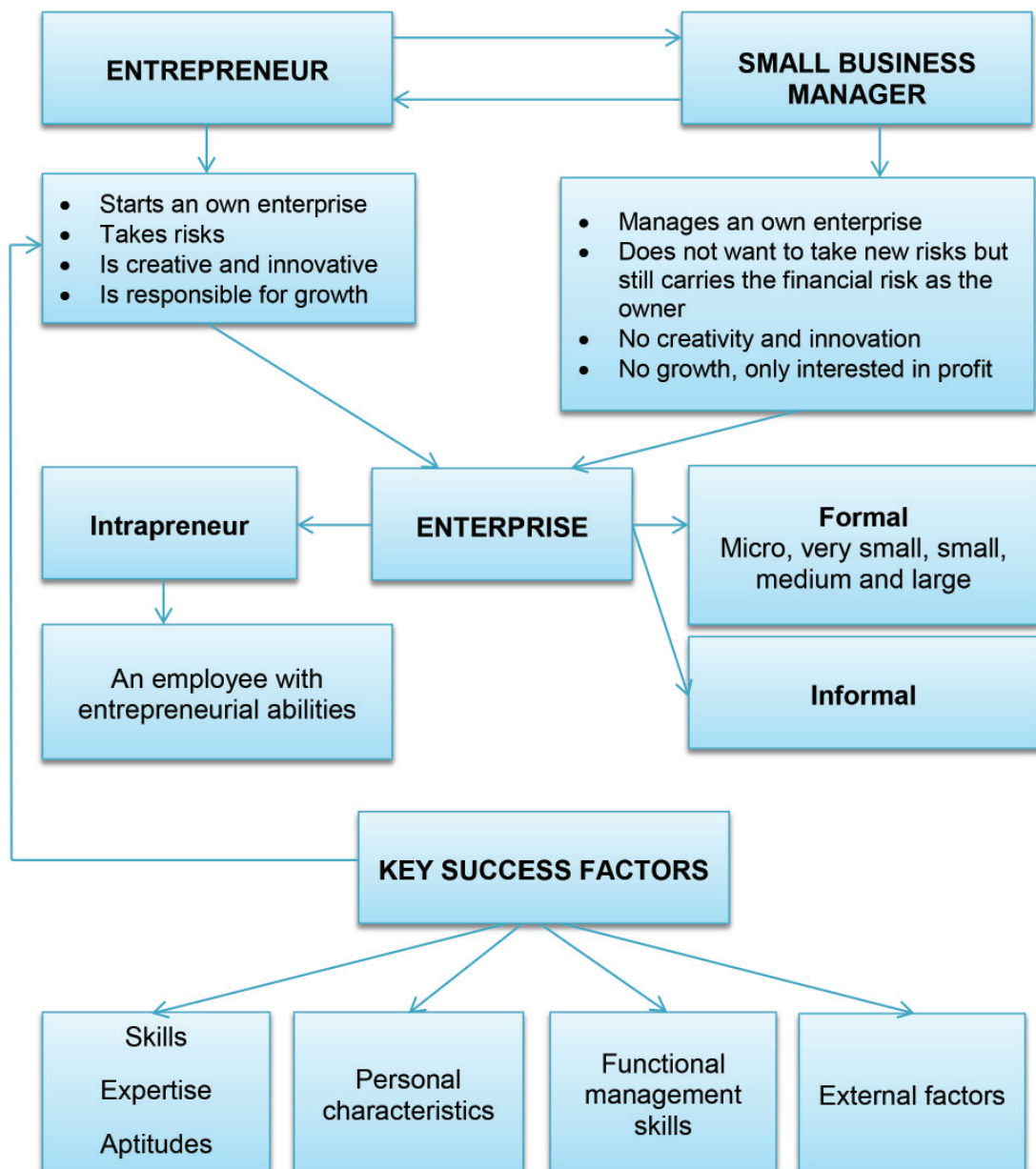
You will need to master the following key concepts to achieve the learning objectives for this learning unit:

- entrepreneur
- intrapreneur
- small business manager

- informal business
- formal business
- franchisor
- franchisee
- growth
- skills
- expertise
- aptitudes
- functional management skills
- personal characteristics



A MIND MAP FOR LEARNING UNIT 1



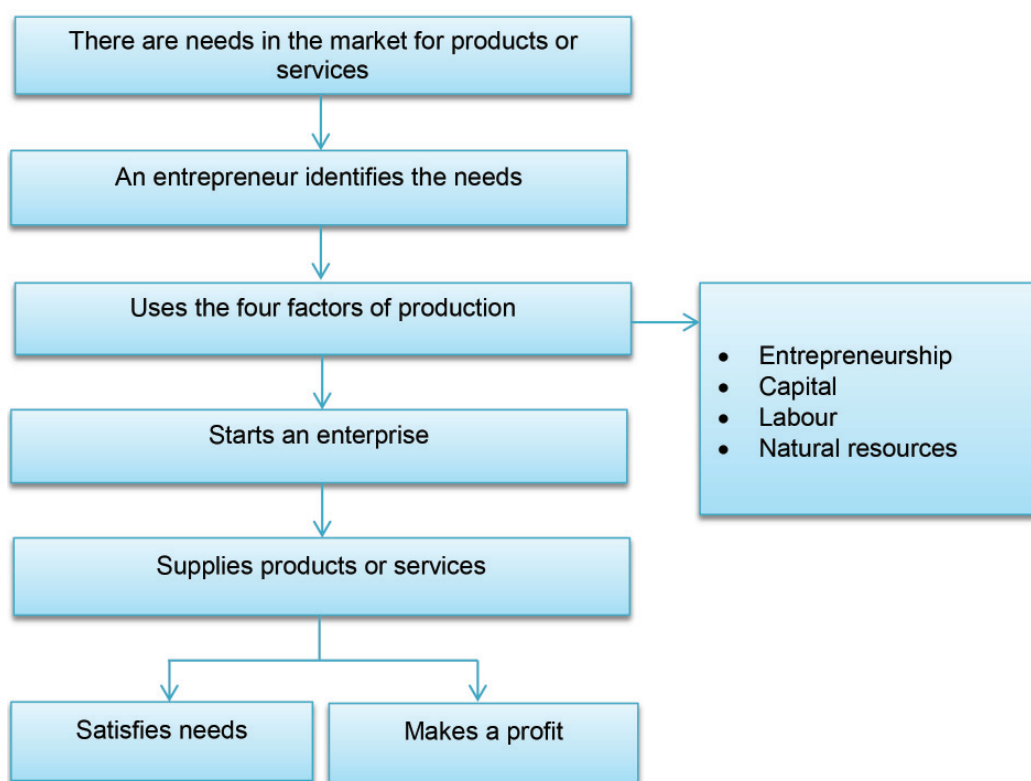
OVERVIEW

In learning unit 1 we will introduce you to entrepreneurship. We will explain what it is, discuss the main characteristics of an entrepreneur and distinguish between entrepreneurship, intrapreneurship and small business management. The key factors that contribute to successful entrepreneurship are discussed in detail. We are going to look at the important role that your skills, expertise and aptitudes will play, as well as the personal characteristics and management skills that you must have to become a successful entrepreneur.

INTRODUCTION



A MIND MAP FOR THE CREATION OF AN ENTERPRISE



1.1 DEFINITION OF THE CONCEPT OF ENTREPRENEUR



Definition of an entrepreneur

Entrepreneurs have the ability to identify and seize an opportunity and create and develop a business by adding value. They do this by applying resources that include finance, time, effort, people and skills. They are willing to take risks and through their businesses they organise, manage and achieve results.



Do you know any South African young entrepreneurs?

Check out: SA's Top 10 young entrepreneurs to watch

<http://www.thesouthafrican.com/sas-top-10-young-entrepreneurs-to-watch/>

Entrepreneurs should be willing to take risks, but ...

Check out: Business in Africa riskier <http://www.iol.co.za/business/companies/business-in-africa-riskier-1906584#.VeGhYPaqqko>



Activity 1.1

List the main characteristics of an entrepreneur.

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering assignments and for exam preparation.

You must study these characteristics very well, as we are going to use them to distinguish between an entrepreneur, a small business manager and an intrapreneur.

1.2 THE RELATIONSHIP BETWEEN ENTREPRENEURSHIP AND SMALL BUSINESS MANAGEMENT

Most enterprises that entrepreneurs start begin as micro or small enterprises. These enterprises are usually started and entrepreneurially managed by one person. They can grow and become larger small enterprises or even medium and large enterprises if the entrepreneur does not become a small business manager. An entrepreneur and a small business manager have very different ways of thinking. If the entrepreneur becomes too comfortable with the level of growth within the enterprise, he or she becomes a small business manager that is averse to risk, change and innovation. The entrepreneurial enterprise is then replaced by a managerially focused small enterprise.



Study section 1.2 in your prescribed book to gain a deeper understanding of the relationship between entrepreneurship and small business management.

1.2.1 Definition of a small business manager



A small business manager is a person who

- *manages an existing business or franchise without ensuring growth*
- *works full- or part-time in a lifestyle business that does not generate sufficient income to cover all living expenses*
- *is satisfied with a no-growth, single-premise business*
- *inherits or take over a business and runs it in the same way as the previous owner, without expanding or improving it (no creativity and innovation)*
- *is appointed by the owner of a small business as the manager*



Activity 1.2

What is meant by the concept of “creativity and innovation”?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

Creativity and innovation can be accomplished, among other things, by introducing new products, using better methods to market existing products or entering new markets, using better or other resources, or applying new technology or better production processes.



Activity 1.3

What is meant by the concept of growth?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

1.2.2 Differences and similarities between an entrepreneur and a small business manager

Entrepreneur	Small business manager
Starts own enterprise and manages it	Manages own enterprise or an existing business or franchise
Is creative and innovative	No creativity and innovation

Entrepreneur	Small business manager
Is willing to take calculated risks	Does not want to take new risks but still carries the financial risk as the owner
Is responsible for growth	Not interested in growth, interested only in profit and the survival of the enterprise

1.3 THE RELATIONSHIP BETWEEN ENTREPRENEURSHIP AND INTRAPRENEURSHIP

Study section 1.4 in your prescribed book to gain a deeper understanding of the concept of intrapreneur/corporate entrepreneur.

1.3.1 Definition of the concept of intrapreneur



An intrapreneur does not want to take the risk of starting an own enterprise, but prefers to use his or her entrepreneurial ability in an existing enterprise. An intrapreneur is an employee with entrepreneurial abilities who identifies an opportunity in an existing enterprise.

1.3.2 Differences and similarities between an entrepreneur and an intrapreneur

Entrepreneur	Intrapreneur
Starts own enterprise and is the owner of the enterprise	Does not want to start own enterprise and is an employee
Identifies opportunities and seizes them	Identifies business opportunities within an existing enterprise
Is creative and innovative	Is creative and innovative
Is willing to take calculated risks	Does not want to take risks
Is responsible for growth	Is responsible for growth



Activity 1.4

Is a small business manager and an intrapreneur the same?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

1.4 TYPES OF ENTREPRENEURIAL BUSINESSES



Section 1.3 of the prescribed textbook distinguishes between formal and informal entrepreneurial businesses. Each of these types of business has very specific characteristics according to specific needs and features.

1.4.1 The informal business sector

The informal business sector includes all businesses that are not registered for income tax and value-added tax (VAT).

Businesses in the informal sector range from commercial activities to production and service, with most of these businesses operating in the retail trade sector. These businesses meet the specific needs of the poor and less affluent people in society, because they provide products and services at more affordable rates.

The role of the informal sector remains controversial, as these businesses provide much needed income opportunities but their owners tend not to comply with tax, labour and other regulations.

1.4.2 The formal business sector

The formal business sector includes micro, very small, small, medium and large enterprises.

1.4.2.1 Micro, very small and small business sector



Type	Employees	Turnover per annum
Micro	5 or fewer	R100 000
Very small	6 to 10	More than R100 000 but less than R3 million
Small	11 to 50	R3 – R32 million



Refer to Table 1.1 in your prescribed textbook for the definition of a small business according to the industrial sector, employment and turnover.

1.4.2.2 Medium-sized and large business sectors



Type	Employees
Medium	Up to 200
Large	200 and more



Activity 1.5

List a few examples of prominent young international and South African entrepreneurs.

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.



Refer to section 1.3.1 and Example 1.3 in the prescribed textbook for more examples of famous entrepreneurs.

1.4.3 Advantages and disadvantages of formal and informal businesses



Carefully study the following table showing the differences between and the advantages and disadvantages of informal and formal businesses.

Formal	Informal
Advantages	Disadvantages
Registered form of enterprise	Not a registered form of enterprise
Recognised business premises	Does not have recognised premises
Easier access to finance	Difficult to obtain finance
Easier access to resources	Difficult to obtain resources
Disadvantages	Advantages
Has to keep financial records	Does not have to keep financial records
Has to pay tax	Does not have to pay tax

1.5 FRANCHISORS AND FRANCHISEES

Section 1.4.1 in the prescribed book discusses franchisors and franchisees in more detail.

1.5.1 Definition of the concept of franchising

Franchising is an arrangement in which an individual or business (the franchisor) grants an independent party (the franchisee) the right to sell the products or services of the business according to guidelines set down by the franchisor.

The franchisor retains control over the conduct of the business and offers the franchisee a comprehensive business package.

1.5.2 Definition of the concepts of franchisor and franchisee



Activity 1.6

Would you classify franchisors as micro, small, medium or large businesses? How would you classify franchisees?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

1.6 KEY SUCCESS FACTORS OF ENTREPRENEURS



Successful entrepreneurs take advantage of certain key success factors such as personal characteristics and functional management skills. Make sure that you understand these concepts.

Refer to Table 1.2 displaying the key success factors in the prescribed textbook.

The profile of an entrepreneur is an indication of the personal abilities and characteristics he or she has. Many researchers have tried to describe a typical entrepreneur, but they have found that there is no typical entrepreneur. Few, if any, entrepreneurs have all the key success factors, but through their introspection and self-evaluation they can identify what their strengths and weaknesses are.



Activity 1.7

How can entrepreneurs apply their strengths and overcome their weaknesses?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

In the next subsections the role played by the following factors in entrepreneurial success will be considered:

- skills, expertise and aptitudes
- important personal characteristics
- important functional management skills
- external factors

1.6.1 Skills, expertise and aptitudes



We can distinguish between skills, expertise and aptitudes as follows:

Skills: Refer to *manual work* and can be *learned*.

Expertise: Expertise is based on knowledge that you acquire through *experience*.

Aptitudes: Each person is born with certain aptitudes and *talents*.

It is best to start an enterprise in something you are interested in and feel comfortable with (aptitudes), of which you have experience (expertise) and in which you are trained (skills). Usually your skills, expertise and knowledge are a product of your natural aptitudes, talents and interests.



Refer to Example 1.6 in the prescribed textbook for examples on skills, expertise and aptitudes.

1.6.2 Important personal characteristics

Skills, expertise and aptitudes in isolation do not guarantee a successful enterprise. To ensure success in your enterprise, you must have certain personal characteristics.



We can identify the following personal characteristics:

- *perseverance*
- *commitment to the enterprise*
- *involvement in the enterprise*
- *willingness to take risks*
- *sound human relations*
- *creativity and innovative ability*
- *positive attitude and approach*

Study section 1.5.2 where these characteristics are discussed in detail in the prescribed textbook.



Did you know that entrepreneurs should embrace their failures?

Check out the story: Can this movement get SA entrepreneurs to finally embrace failure?

<http://www.smesouthafrica.co.za/16527/Can-this-movement-get-SA-entrepreneurs-to-finally-embrace-failure/>

More stories:

Ten rules for entrepreneurs to live by

<http://www.howwemadeitinafrica.com/ten-rules-for-entrepreneurs-to-live-by/52994/>

Success is all in the attitude

<http://www.entrepreneur.com/article/204504>

Being a successful entrepreneur in South Africa – The reality

<http://southafrica.smetoolkit.org/sa/en/content/en/8834/Being-a-successful-entrepreneur-in-South-Africa-%E2%80%93-The-Reality>

1.6.3 Important functional management skills

The management skills of an entrepreneur indicate how well the entrepreneur can perform important tasks or activities in an enterprise.



Activity 1.8

List the tasks or activities that an entrepreneur has to perform.

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.



Three characteristics of the above functions of the enterprise:

- *All these functions occur in every enterprise, regardless of the size of the enterprise.*
- *These functions must operate as a system.*
- *There must be constant interaction between these functions.*

In this section, we discuss the ability of the entrepreneur to perform specific management activities in the enterprise. Entrepreneurs must be aware of their strengths and weaknesses in terms of management skills in the various functions of the enterprise, so that they can build a successful enterprise.



As an entrepreneur, you should have a combination of the following nine management skills:

- *planning an enterprise before it is established*
- *general management skills and the use of advisers*
- *customer service*
- *knowledge of competitors*
- *market orientation*
- *the importance of quality products and/or services*
- *accounting for all purposes*

- *insight into expenditure, income, profit and loss*
- *the ability to use income carefully*

Study section 1.5.3 where these management skills are discussed in detail in the prescribed textbook.



Check out the stories on these management skills:

To succeed as an entrepreneur, know your customer

<http://www.forbes.com/sites/alanhall/2012/06/14/to-succeed-as-an-entrepreneur-know-your-customer/>

Know your competition <http://www.entrepreneur.com/article/78596>

1.6.4 External factors

Study section 1.6, which gives a short description of each external factor, in your prescribed textbook. The external factors will be discussed in detail in learning unit 2.



You have now reached the end of learning unit 1.

SUMMARY

Successful entrepreneurs play an extremely important role in a country's economic development, wealth and employment creation. In this chapter we discussed the most important concepts related to this role.

You need to realise that all the success factors we have discussed must be analysed in personal terms. This may be discouraging to some potential entrepreneurs, but it is vital for you, as an aspiring businessperson, to be aware of all these important aspects. You must be critical of yourself, but, at the same time, positive about solving problems. You can make adjustments in order to start an enterprise that has been your dream. As an entrepreneur, you will realise how important it is to evaluate personal strengths and weaknesses realistically in order to achieve your goals.



SELF-ASSESSMENT

To test and assess your knowledge of this learning unit, you can now do the following activities:

- (i) Complete the self-assessment questions on learning unit 1 below. Remember: The only way you can test your knowledge is by answering the questions without looking at the solutions that is contained in Appendix A.
- (ii) Do the self-assessment questions in the prescribed textbook at the end of Chapter 1.

Read the case study below and answer all the questions that follow.

Case study: New Romantics

Nadene Marx started New Romantics ten years ago in Bergbron, a small suburb in North-cliff. Nadene is a qualified fashion designer who specialises in making bridal gowns, bridesmaids' gowns, mother-of-the-bride outfits and couture evening gowns.

After the birth of their first child, Nadene and her husband decided that she should resign from her job. She started her own enterprise and registered it as a sole proprietorship. After careful consideration, they decided that Nadene should rather work from home instead of spending thousands of rands per month on renting a small space in a shopping centre. Nadene contributed R100 000 of her savings to convert their double garage into a studio. The studio consisted of a small reception and display area, a fitting room and a workshop for two seamstresses.

Nadene's enterprise became so popular that she could no longer accept all the orders. She had to employ another two seamstresses and an administrative assistant. Owing to the appointment of the additional staff members her premises became far too small. When their neighbours wanted to sell their house, Nadene decided to buy the property for her enterprise. She had to apply for a loan of R900 000 to buy the premises and offered their own home, worth R1 million, as collateral. She also applied for financing of R80 000 to buy more advanced sewing machines, overlockers, office equipment and furniture. The new premises had enough space for Nadene to open a small shop that sells accessories such as veils, hair accessories, jewellery and underwear. She appointed a full-time shop assistant to handle the sales.

After numerous complaints from customers that they could not find affordable bridal shoes, one of the new seamstresses, Nicky, suggested that they use off-cuts from the fabric to cover ordinary shoes with the same fabric of which the wedding gown is made. The brides would buy shoes of their choice and bring them to Nicky to cover them with matching fabric.

The process of making a wedding gown starts when a potential bride phones Nadene to make an appointment to see her at the studio. Nadene will then sketch a design according to the bride's preferences and show her samples of fabric that will suit that particular design. As soon as the bride has decided on a design and matching fabric, Nadene will work out a quotation for the dress. The bride must then sign a contract to confirm acceptance of the quotation and pay a deposit of 50% of the final price so that Nadene has enough

cash to buy the fabric and accessories. Nadene will then cut the fabric according to the design and the seamstresses will start the sewing. The bride has to come to the studio for regular fittings and a final fitting will take place one week before the wedding. The remainder of the money has to be paid when the bride collects the dress from the studio.

Nadene's target market is in Randburg and Roodepoort, and she competes with various other dress designers in nearby areas, as well as with big businesses such as Bride & Co and The Bridal Couture in Rivonia. Although her dresses are more expensive than those of Bride & Co, she has the competitive advantage that her designs are unique – each bride can decide for herself what her dress should look like.

Although Nadene's designs are original, she has to be aware of the latest trends in fashion and overseas designs play an extremely important role in the choices of her customers. The fabric, designs and trimmings of bridal gowns change constantly and Nadene has to be aware of new methods of stitching and ironing. Her equipment also has to be of the best quality, therefore she has to upgrade her sewing machines and overlockers regularly.

Nadene advertises on the internet and the name of her enterprise, her website and her contact details are also displayed on her car. In addition, she displays some of her gowns at various local wedding expos. However, most of her customers are referrals from satisfied previous customers.

Multiple-choice questions

- (1) Nadene Marx could be classified as **an entrepreneur** because she _____ .
- (a) did not display any signs of creativity or innovation
 - (b) took calculated risks
 - (c) managed the business without ensuring growth
 - (d) started her own enterprise

Choose the correct option:

- (1) a, b, c
 - (2) b, c
 - (3) b, d
 - (4) a, b, c, d
- (2) **Nicky**, who suggested that they should **use off-cuts from the fabric to cover ordinary** shoes with the same fabric of which the wedding gown is made, could be classified as a/an _____ .
- (1) intrapreneur
 - (2) entrepreneur
 - (3) small business manager
 - (4) franchisor
- (3) Nadene registered New Romantics as a sole proprietorship. **An advantage of a formal enterprise** is that Nadene _____ .
- (1) does not have to pay tax

- (2) does not have to keep financial records
 - (3) has to pay tax
 - (4) has easier access to finance
- (4) Nadene used R100 000 of **her savings** to convert their double garage into a studio. This could be regarded as an example of her _____ .
- (1) involvement
 - (2) commitment
 - (3) positive attitude and approach
 - (4) perseverance
- (5) Nadene **sketches the designs** according to the brides' preferences, works out quotations for the dresses and cuts the fabric according to the designs. This could be regarded as an example of her _____ .
- (1) involvement
 - (2) commitment
 - (3) positive attitude and approach
 - (4) perseverance
- (6) Nadene **applied for financing** of R80 000 to buy more advanced sewing machines, overlockers, office equipment and furniture. This could be regarded as an example of her _____ .
- (1) creativity and innovative ability
 - (2) perseverance
 - (3) positive attitude and approach
 - (4) willingness to take risks
- (7) The **opening of a small shop** that sells accessories such as veils, jewellery and underwear could be regarded as an example of Nadene's _____ .
- (1) creativity and innovative ability
 - (2) perseverance
 - (3) positive attitude and approach
 - (4) willingness to take risks
- (8) Owing to the appointment of the additional staff members Nadene's **premises became far too small** and she bought their neighbours' property. This is an indication of _____ .
- (1) her general management skills
 - (2) New Romantics' growth
 - (3) New Romantics' survival
 - (4) her insight into profit and loss
- (9) Although Nadene advertises on the internet, most of her customers are **referrals from satisfied previous customers**. Her ability to _____ would therefore play an extremely important role in New Romantics' success.
- (1) maintain sound human relations

- (2) carry on despite setbacks
 - (3) take calculated risks
 - (4) use her own money to establish the enterprise
- (10) Nadene should know that the **difference between income and profit** is that _____ .
- (a) profit must first be used to pay her operating expenses
 - (b) income is the amount she gets from the sales of the wedding gowns
 - (c) profit is the amount that is left after she has bought more fabric and paid all her operating expenses
 - (d) income must first be used to purchase more fabric and accessories

Choose the correct option:

- (1) a, b, d
- (2) a, b, c
- (3) b, c, d
- (4) a, c, d

SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS



Please refer to Appendix A for the suggested solutions to the self-assessment questions.

Learning Unit 2

Basic business concepts and the business environment

STUDY CHAPTER 2 IN THE PRESCRIBED BOOK

CONTENTS

- The relationship between an enterprise and an establishment
 - The branch of industry and the production branch
 - The three sectors in which an enterprise can operate
 - The industrial column
 - The business environment
 - The variables of the business environment
-



LEARNING OBJECTIVES

When you have worked through learning unit 2, you should be able to

- *describe what an enterprise is*
 - *explain the motive for creating an enterprise*
 - *explain the difference between an enterprise and an establishment*
 - *list the four factors of production and give an example of each*
 - *explain the difference between a branch of industry and a production branch*
 - *explain the three sectors into which enterprises can be classified and give an example of an enterprise in each sector*
 - *explain what an industrial column entails*
 - *draw an industrial column for manufacturing and distributing a product*
 - *define the term "business environment"*
 - *list and explain the characteristics of the business environment*
 - *explain the difference between the internal and external environments*
 - *explain what the micro-environment entails and give an example of each of the variables of the micro-environment*
 - *explain what the market environment entails and give an example of each of the variables of the market environment*
 - *explain the types of market that can be served by an enterprise*
 - *explain the different types of competition*
 - *explain what the macro-environment entails*
-



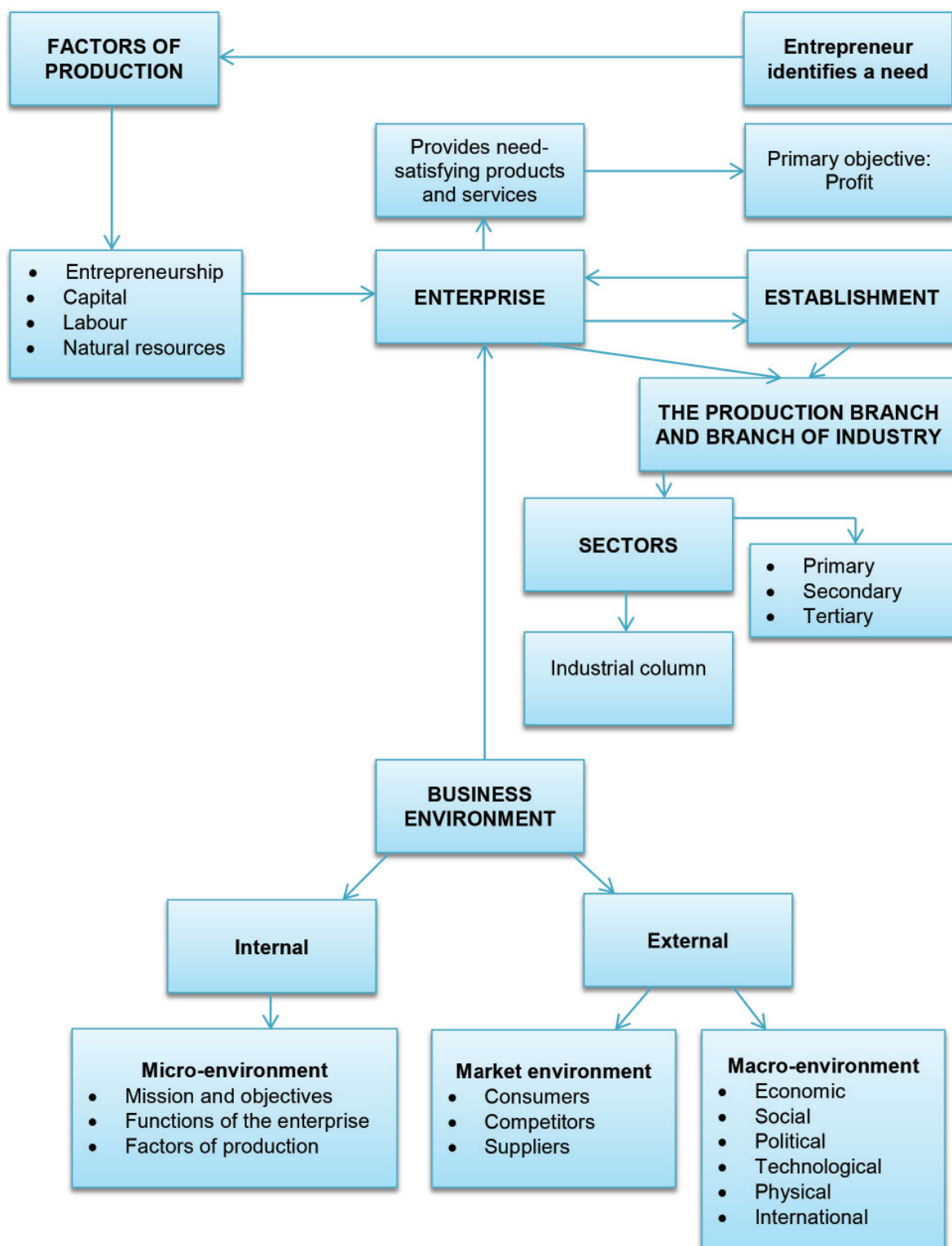
KEY CONCEPTS

You will need to master the following key concepts to achieve the learning outcomes for this learning unit:

- enterprise
 - establishment
 - branch of industry
 - production branch
 - primary sector
 - secondary sector
 - tertiary sector
 - industrial column
 - business environment
 - micro-environment
 - market environment
-



A MIND MAP FOR LEARNING UNIT 2



OVERVIEW

In learning unit 2 we will explain basic business concepts to help you understand the special language of the business world. This chapter explains the difference between an enterprise and an establishment, the difference between a production branch and a branch of industry, the sectors into which businesses can be classified, as well as the four factors of production that are essential for the existence of an enterprise, so that you can have a better understanding of what the business world entails.

We will also discuss and explain how the enterprise relates to the business environment as a whole, so that you can see how it fits into the bigger picture. An enterprise cannot exist in isolation, therefore we will distinguish between the three main divisions of the business environment, namely the micro-, market and macro-environments. We will also explain the different variables of each of these environments and indicate the significant role they play in the existence and growth of an enterprise.

2.1 THE RELATIONSHIP BETWEEN AN ENTERPRISE AND AN ESTABLISHMENT

This section refers to sections 2.2 and 2.2.1 in the prescribed book.



Definition of the concept of enterprise

An enterprise is an independent body that is established by an entrepreneur to provide products and services that will meet the needs of consumers, with the main aim or motive of making a profit. The enterprise consists of all the functions of the enterprise and the establishment.



Definition of the concept of establishment

An establishment is the place where inputs are converted into outputs. This is the place where physical production takes place, in other words, the factory or plant.



Activity 2.1

We just mentioned that the enterprise consists of all the functions of the enterprise and the establishment. Can you still remember these functions? They were mentioned in learning unit 1 of the study guide.

.....



Refer to Figure 2.1 in the prescribed textbook where the relationship between the enterprise and the establishment is explained by means of an illustration.



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

2.2 THE BRANCH OF INDUSTRY AND THE PRODUCTION BRANCH



Definition of a production branch

A production branch refers to all the enterprises that use more or less the same production processes or perform the same activities.



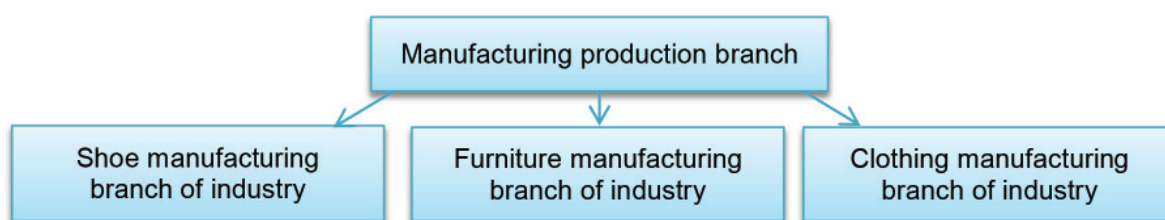
Definition of a branch of industry

A branch of industry refers to all the enterprises that produce or sell more or less the same products or provide the same services.



In the prescribed textbook, Table 2.1 indicates the difference between a production branch (industry) and a branch of industry. Also pay attention to the following sketches that provide examples of enterprises that can be classified under the same production branch.

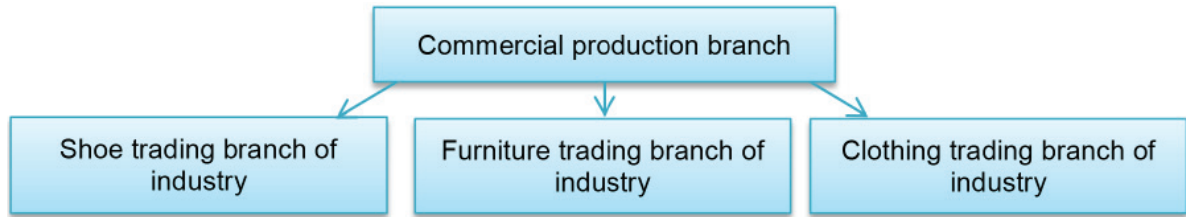
Example 1



Feedback

From the above example it is clear that although these enterprises manufacture different products, they all use raw materials (inputs) which they process into final products (outputs). Therefore, they all fall under the manufacturing production branch.

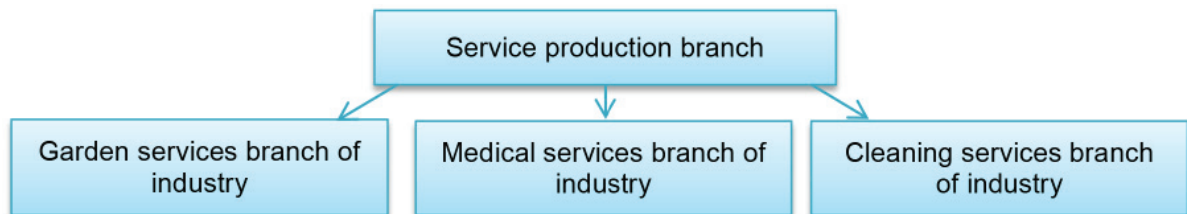
Example 2



Feedback

From the above example it is clear that although these enterprises sell different products, they all sell final products to consumers. Therefore, they all fall under the commercial production branch.

Example 3



Feedback

From the above example it is clear that although these enterprises provide different services, they only provide services – they do not manufacture or sell products. Therefore, they all fall under the service production branch.

2.3 THE THREE SECTORS IN WHICH AN ENTERPRISE CAN OPERATE



An enterprise can exist or operate in the following three sectors:

- *primary sector*
- *secondary sector*
- *tertiary sector*

It is important that you study the definitions of each of these sectors. In other words, you must know which activities take place in each sector and also give examples of enterprises that can be classified under each sector.

The primary sector

Definition: Exploitation of natural resources in their raw, unprocessed form.

Examples: Crude oil extracted from the sea, agriculture, forestry, fishing and mining.

The secondary sector

Definition: Processing of natural resources into final products.

Examples: Crude oil refined and processed into petroleum, food processing and energy production.

The tertiary sector

Definition: Conveying or distributing final products from the manufacturer to the consumer. This includes wholesalers, retailers and the end consumers. The tertiary sector therefore includes all enterprises that sell final products to consumers, as well as enterprises that provide services.

Examples: Distribution of goods – petroleum distributed to wholesalers, filling stations, consumers; provision of services – pest control or entertainment.



Feedback

Enterprises are classified into these three sectors according to the activities that they perform. Manufacturing enterprises fall under the secondary sector and commercial (trade) and service enterprises fall under the tertiary sector.



Check out this video explaining the three business sectors.

Business sectors <https://www.youtube.com/watch?v=8KDxAWfMwf4>



Activity 2.2

To test your knowledge of each of these sectors, you must decide under which sector each of the following enterprises can be classified:

- Jacks' Fruit Farm (where fruit is cultivated)
 - ABC Fruit Factory (where fruit is processed and canned)
 - Susan's Fruit Shop (where fruit is sold to consumers)
 - Woolworths
 - Old Mutual (insurance)
 - Pick n Pay
 - De Beer's Mining Company
 - a furniture factory
-



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

2.4 THE INDUSTRIAL COLUMN



In the prescribed textbook, Figure 2.2 is a sketch of an industrial column for the manufacturing and distribution of paper.

Definition of the concept of industrial column



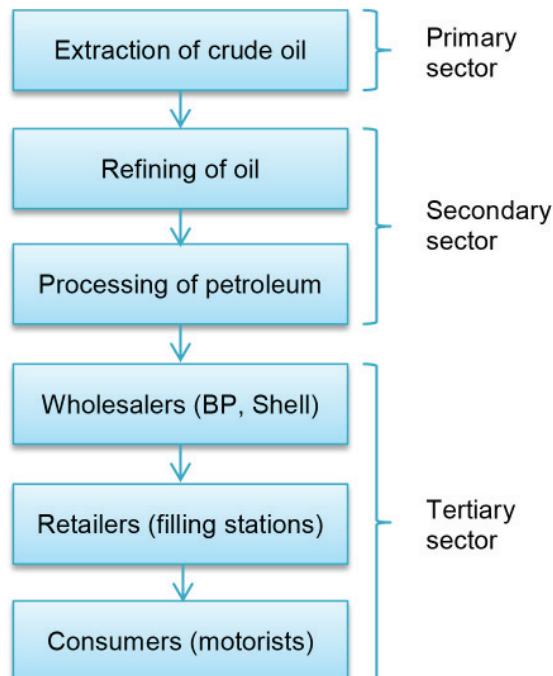
An industrial column represents the route that an individual product follows from its original stage until it ends up in the hands of the consumer.

It is important to remember that we classify enterprises into sectors according to the activities they perform. However, if we look at an individual product, we combine all the processes and transactions that take place from the primary sector, through the secondary sector, along to the tertiary sector where the product ends up in the hands of the end consumer. In other words, we combine the sectors in an industrial column.



Look at the following example which indicates the route that an individual product (crude oil) follows from its original stage until it ends up in the hands of the consumer. All the sectors that are involved (primary, secondary and tertiary) are combined in an industrial column.

Industrial column for petroleum





Activity 2.3

Draw the industrial column for the following products:

- wine
 - a diamond ring
 - a table (wood)
 - bread
 - leather shoes
-



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

2.5 THE BUSINESS ENVIRONMENT

2.5.1 Definition of the concept of business environment



The business environment includes all the factors and variables which influence the establishment, growth and continued existence of the enterprise positively and/or negatively, thereby promoting or hindering the achievement of the enterprise's objectives.



In the prescribed textbook, Figure 2.3 is an illustration of the business environment. This illustration gives an overall picture of the internal environment (the micro-environment or the enterprise itself) and the external environment (the market and the macro-environments).



Activity 2.4

List the three main components of the business environment.

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

2.5.2 Characteristics of the business environment



You must be familiar with the following characteristics of the business environment:

- *The business environment changes constantly.*
- *The enterprise must keep up with the changing environment.*
- *The establishment, growth and continued existence (survival) of the enterprise are directly influenced by the business environment.*
- *The business environment influences the future of the enterprise.*
- *There are both opportunities and threats in the business environment.*
- *The variables are interdependent.*
- *The complexity of the influence of the business environment depends on the type of enterprise.*

The business environment can positively and/or negatively affect the enterprise. The entrepreneur must be aware of the variables in the business environment, since they represent the strengths, weaknesses, opportunities and threats that can benefit or harm the enterprise. The strengths, weaknesses, opportunities and threats form the basis of a SWOT analysis that the entrepreneur has to compile for his or her enterprise.



The micro-environment (internal environment) represents the strengths and weaknesses of the enterprise.

The market and macro-environments (external environment) represent the opportunities and threats of the enterprise.

The SWOT analysis will be discussed in more detail in learning unit 4.

2.6 THE VARIABLES OF THE BUSINESS ENVIRONMENT

2.6.1 Micro-environment



Definition of the micro-environment

The micro-environment is the sum total of all the factors and variables which occur internally in the enterprise and is influenced directly or indirectly by the decisions of the enterprise's management. The internal environment is the enterprise itself and is under direct control of the enterprise's management.



Activity 2.5

List the variables of the micro-environment.

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.



Study each of these variables very well. Be aware of their definitions and subdivisions, and how they can influence the establishment, growth and continued existence of the enterprise.

2.6.1.1 The mission and objectives of the enterprise

The mission and objectives indicate what you want to achieve with the business and how you want to achieve it. We distinguish between primary and secondary objectives.

The primary objective

The primary objective is the main or overall objective of the enterprise, therefore there can be only one main objective. This objective is a long-term objective which determines the direction of the enterprise. The main objective of starting an enterprise is to **make a profit**.

The secondary objectives

Secondary objectives are additional objectives which are set to support the achievement of the primary objective. Secondary objectives are short-term objectives which change constantly. There must be more than one secondary objective – each function of the enterprise will set its own secondary objectives in order to help the enterprise achieve the primary objective. Examples of secondary objectives are to sell quality products at affordable prices (the marketing function), to pay market-related salaries (the human resources function) and to maintain good relations with suppliers (the purchasing function).



Check out these other important objectives of a business:

10 most important business objectives

<http://smallbusiness.chron.com/10-important-business-objectives-23686.html>

2.6.1.2 The functions of the enterprise

All enterprises, regardless of their size, have eight functions. These functions should operate as a system, which means that there should be constant interaction between them.

The general management function

General management includes all the activities that are performed in the enterprise to enable the enterprise to attain its goals. These activities consist of four elements, namely planning, organising, leading and control, and are found in all the other functions of the enterprise.

The financial function

This function determines what the capital requirement or need of the enterprise is and how this need will be financed. This includes decisions on applying funds effectively and the best possible use of sources of finance.

The marketing function

Marketing is responsible for transferring the products from the manufacturer to the consumer, as well as the activities that make this transfer possible.

The operations function

This function is concerned with transforming inputs into outputs by using the four factors of production to manufacture a product or to provide a service.

The logistics function

Logistics deals with the procurement of resources, ensuring that production means of the right quality are supplied to the enterprise in the right quantities, at the right time, to the right place and at the right price.

The human resources function

This function is responsible for the effective use of a competent, motivated labour force. Responsibilities include compiling job descriptions and job specifications, as well as recruiting, selecting, employing and training personnel.

The information management function

The information management function (administrative function) is responsible for collecting, processing, storing and distributing information to enable management to make informed decisions.

The public (external) relations function

This function is responsible for promoting the image of the enterprise among all the interest groups of the enterprise by ensuring positive support from all the relevant interest groups.

2.6.1.3 The factors of production

All enterprises need four factors of production. These factors are scarce and expensive and must be used carefully to produce products or to provide services that will satisfy the unlimited needs of consumers.



Activity 2.6

Can you still remember the factors of production?
They were mentioned in the mind map for learning unit 2.

.....

Entrepreneurship

The entrepreneur is the person who takes the initiative and risk to combine the other three factors of production to start an enterprise in order to offer products or services that will satisfy needs.

Labour

Labour refers to human resources – people with knowledge and skills to produce the products or to provide the services.

Capital

We distinguish between financial capital (own or borrowed money), physical capital (land, buildings, machinery, equipment and vehicles) and human capital (technical knowledge and skills).

Natural resources

This includes raw materials to produce products or stock to sell.

2.6.2 Market environment



Definition of the market environment

The market environment is defined as the sum total of all the factors and variables which exist externally and which can positively or negatively influence the existence and growth of the enterprise. The market environment is the link between the enterprise and the macro-environment. It surrounds the micro-environment and is surrounded by the macro-environment. The enterprise has limited or no control over this environment.



Activity 2.7

List the variables of the market environment.

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.



Study each of these variables very well. Be aware of their definitions and subdivisions, and how they can influence the establishment, growth and continued existence of the enterprise.

2.6.2.1 The consumers and their needs

This variable includes all individuals, groups or institutions that have a specific need for the enterprise's products or services and that are prepared to pay for them. In other words, they are the people to whom the entrepreneur is going to sell his or her products.



In the prescribed textbook, section 2.3.2, you will see that we can identify more than one type of market. You must be able to name each of these markets, define them and also give examples of each of them.

We distinguish between the following types of market:

- *consumer market*
- *industrial market*
- *resale market*
- *international market*
- *government market*



As an entrepreneur, you should also be aware that consumers have certain rights. You must be able to name each of these rights, define them and also give examples of each of them.

We distinguish between the following rights of consumers:

- *the right to be informed*
- *the right to exercise personal choice*
- *the right to be heard*
- *the right to be protected*

The right to be informed

Consumers should receive objective information. This means that the enterprise may not mislead consumers by withholding information about their products.

The right to exercise personal choice

Consumers have the right to choose. They can decide which products or services they prefer.

The right to be heard

Consumers have the right to complain about poor-quality products or poor service.

The right to be protected

Consumers' safety is important and they should be protected against harmful products.

2.6.2.2 The competition

Competition means that each enterprise tries to convince a consumer that its products and services are the best and that the consumer should therefore buy products and services from this specific enterprise.



You must be able to distinguish between direct and indirect competition.

Direct competition

Direct competition refers to enterprises selling the same products.

Examples:

- *If a consumer wants to buy margarine, he or she can choose between various types of margarine, such as Rama, Flora and Stork.*
- *An enterprise that provides garden services will compete directly with all the other enterprises that provide garden services in the same area.*
- *Coca-Cola's direct competition is Pepsi, as they offer almost the same product.*

Indirect competition

Indirect competition refers to the use of substitute products.

Examples:

- *If a consumer cannot find margarine, he or she can decide to buy butter.*
- *An enterprise that provides garden services competes indirectly with informal garden workers and with homeowners who prefer to maintain their gardens themselves.*
- *If a consumer is thirsty and cannot find Coca-Cola, he or she can decide to buy Bonaqua Pump still water.*



As an entrepreneur, you should also be aware that businesses compete with one another's products or services, but we can also identify four other types of competition. Study section 2.3.2 in the prescribed textbook. You must be able to name each of these types of competition, define them and also give examples of each of them.

We can distinguish between various types of competition:

- *competition between the needs of consumers*
- *competition between mechanisms for satisfying needs*
- *competition between product forms*
- *competition between different trademarks*



Did you know?

Your business's competitors extend well beyond those with similar products:

<http://www.entrepreneur.com/article/246648>

10 ways competition can improve your business:

<http://www.entrepreneurmag.co.za/advice/growing-a-business/compete-to-win/10-ways-competition-can-improve-your-business/>

2.6.2.3 The suppliers of resources and services

This variable deals with all the businesses and institutions that supply resources (factors of production) to the enterprise. Examples include suppliers of raw materials or stock,

suppliers of capital and suppliers of labour. It also includes suppliers of services, such as water and electricity, municipal services and telephone services.



Study the examples given in Example 2.5 in the prescribed textbook.

2.6.3 Macro-environment



Definition of the macro-environment

The macro-environment consists of all the variables and factors outside (external to) the enterprise which have a positive or negative influence on the growth and continued existence of the enterprise and which encourage or hinder the achievement of objectives. The enterprise has no control over this environment or the variables which operate within it.



Activity 2.8

List the variables of the macro-environment.

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.



Study section 2.3.3 in your prescribed textbook. You need to know each of these variables very well. Be aware of their definitions and subdivisions, and how they can influence the establishment, growth and continued existence of the enterprise.

The economic environment

The economic environment includes aspects such as inflation, interest rates, trade cycles, economic growth rate and the purchasing power or disposable income of consumers.

The social environment

This environment refers to the needs and preferences of consumers. It includes aspects such as the size and composition of the market, geographic location of consumers (needs differ between regions), the changing role of women (more working women), changing lifestyles (consumers are more health-conscious) and the development level of the market (consumers are more informed).

The technological environment

The technological environment includes aspects such as new products, new machinery or equipment and more advanced production processes.

The physical environment

This environment refers to aspects such as limited and expensive resources, natural disasters, pollution (air, water and noise pollution) and environmentalism, as well as power shortages.

The political environment

The political environment not only refers to the legislation and influence of the government (such as labour and tax laws), but also to legislation of the local authorities (such as health requirements). It also includes statutory provisions, trade unions, associations and institutes.

The international environment

This environment includes aspects such as the international economy (exchange rates), international politics (sanctions or wars) and international technology (imported technology and more advanced machinery and equipment).



Check out:

How technology can help you manage business at the speed of your people:

<http://www.entrepreneur.com/article/243336>



You have now reached the end of learning unit 2.

SUMMARY

After you have studied this learning unit, you will realise that it is quite impossible for an enterprise to function in total isolation. Interaction with the business environment is of the utmost importance. The management of an enterprise should continually analyse the environment and determine its general trends. Valuable information can be used to help the enterprise achieve its objectives and to identify its strengths, weaknesses, opportunities and threats. In this way the enterprise is able to ensure growth and continued existence. However, the opposite is also true. If an enterprise ignores important signals in the business environment, this can cause it to close down.

The three components of the business environment identified in this chapter, namely the micro-, market and macro-environments, are in constant interaction with one another and cannot function independently. Remember that the variables we have identified influence these environments and play a significant role in the growth and continued existence of the enterprise.



SELF-ASSESSMENT

To test and assess your knowledge of this learning unit, you can now do the following activities:

- (i) *Complete the self-assessment questions on learning unit 2 below. Remember: The only way you can test your knowledge is by answering the questions without looking at the solutions contained in Appendix A.*
- (ii) *Do the self-assessment questions in the prescribed textbook at the end of Chapter 2.*

Read the case study below and answer all the questions that follow.

Case study: Lazy to Cook

Lazy to Cook is a catering and event management enterprise that concentrates on wedding receptions. The enterprise designs original invitations, arranges and decorates venues, provides catering for the receptions and offers advice and assistance to the bridal couples to make their wedding day special and enjoyable. Zanele Makhubo started Lazy to Cook in 2008. At that stage, she catered only for small functions for family and friends in Soweto, and the enterprise operated as an informal business. Being a career-oriented woman in the corporate world and an external marker for Business Management at Unisa, Zanele soon realised that there was an ongoing demand for her services and that this type of business, if managed well, could be very profitable. She decided to register the enterprise as a sole proprietorship and applied for a loan to buy her own equipment to cut the costs of hiring tents, furniture, crockery and accessories for each function.

Although Zanele is the sole owner of the enterprise, her whole family is actively involved in it. Her daughter designs the invitations for the functions, her son acts as a photographer, her husband helps with the decoration of the venues and her sister-in-law, Nonkabi, is in charge of the catering. Nonkabi is responsible for hiring and supervising kitchen staff to help her prepare the food and she also hires and supervises students to act as waiters during the functions. Zanele is responsible for the flower arrangements and for the overall management of the events. She also acts as a wedding planner and coordinator by giving advice to the bridal couples on invitations, colour schemes, flowers, venues and menus.

Although the demand for catering services is great, Zanele's business is still struggling. She managed to get only a small loan of R20 000 because she could contribute only an amount of R5 000 as own capital. The business still operates below break-even point, as she currently has to use the income from the functions to pay for her operating expenses. The family also moved to Roodepoort, while their target market is in Soweto. This causes a tremendous increase in transport costs every time they have to cater for a function in Soweto. The poor economic situation in the country has also had a serious effect on her business. People simply do not have the money any more to pay for big weddings.

Although there are smaller functions during the year, the most popular season for weddings is during the summer months, which means that the enterprise does not generate a stable monthly income. Zanele has to make provision for quiet months in order to have enough cash flow to pay her operating expenses.

However, Zanele is not one to give up easily. She decided that, despite setbacks and difficult situations, she would make a success of this enterprise. She wants to increase her mortgage bond by R150 000 to convert her double garage into a formal office so that the enterprise has a more professional appearance and build a storeroom for storing her equipment, tents and accessories properly, so that she will be able to exercise better control over these assets. She also wants to include a small display area in the office to show her clients different options in decorating the venues, as well as examples of her daughter's invitations and her son's photographs. Zanele wants to apply for vehicle financing of R250 000 to buy a bakkie to transport her equipment and decorations to and from the various venues. She also decided to contribute R60 000 of her own savings to upgrade her kitchen with new stoves and refrigerators to enable the enterprise to prepare some of the food in advance.

Zanele is aware that there are many catering businesses in Roodepoort. The West Rand is also known for its beautiful wedding venues that offer complete packages to bridal couples. However, she has identified a gap in the market for smaller and cheaper functions – something that these big venues cannot offer.

Multiple-choice questions

- (1) Zanele acts as a wedding planner and coordinator. Lazy to Cook could therefore be classified under the _____ production branch.
 - (1) commercial
 - (2) bridal services
 - (3) service
 - (4) manufacturing
- (2) Lazy to Cook offers catering services by preparing the food for the functions and Zanele also acts as a wedding planner and coordinator by giving advice to the bridal couples. Lazy to Cook could therefore be classified under the _____ sectors.
 - (a) primary
 - (b) secondary
 - (c) tertiary
 - (d) commercial

Choose the correct option:

- (1) a, b
- (2) b, c
- (3) a, d
- (4) b, d

- (3) The primary objective of Lazy to Cook would be to _____.
- (1) make a profit
 - (2) provide an excellent service to bridal couples
 - (3) maintain good relations with their suppliers
 - (4) generate enough cash to pay for their operating expenses
- (4) The ingredients that Lazy to Cook uses to prepare the food for the functions could be regarded as an example of their _____.
- (1) natural resources
 - (2) labour
 - (3) entrepreneurship
 - (4) capital
- (5) When Zanele places her advertisements, she should keep in mind that her clients must receive objective information and that she may not mislead them by withholding any information. Her consumers have the right to _____.
- (1) be informed
 - (2) exercise personal choice
 - (3) be heard
 - (4) be protected
- (6) After a bridal couple has decided that they want to serve a formal dinner at their wedding reception, they have to decide what food Zanele has to serve. This relates to competition between _____.
- (1) the needs of consumers
 - (2) mechanisms for satisfying needs
 - (3) product forms
 - (4) different trademarks
- (7) The culture of the wedding couple would determine the type of reception that they would want for their wedding. This is an example of how the _____ environment could influence Lazy to Cook.
- (1) economic
 - (2) social
 - (3) political
 - (4) physical
- (8) An increase in the price of petrol would have a direct influence on Lazy to Cook's operating expenses. This is an example of how the _____ environment could influence Lazy to Cook.
- (1) political
 - (2) social
 - (3) economic
 - (4) international

- (9) The most popular season for weddings is during the summer months. If a bridal couple wants their reception to be held outdoors, Zanele has to take the weather into account, since summer is the rainy season in Gauteng. This is an example of how the _____ environment could influence Lazy to Cook.
- (1) political
 - (2) economic
 - (3) international
 - (4) physical
- (10) Zanele registered her enterprise as a sole proprietorship and since she does catering for functions, she also has to comply with health requirements of the local municipality. This is an example of how the _____ environment could influence Lazy to Cook.
- (1) political
 - (2) economic
 - (3) social
 - (4) physical



SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS

Please refer to Appendix A for the suggested solutions to the self-assessment questions.

Learning Unit 3

The identification and development of business ideas

STUDY CHAPTER 3 IN THE PRESCRIBED BOOK

CONTENTS

- The three stages in creating an enterprise
 - Cultivating a creative attitude
 - Generating business ideas
 - The development and evaluation of business ideas
 - The feasibility of business ideas
-



LEARNING OBJECTIVES

When you have worked through learning unit 3, you should be able to

- *list and explain the three stages in creating an enterprise*
 - *define creativity*
 - *distinguish between divergent thinking and convergent thinking and explain why both these abilities are essential for creative output*
 - *list and explain the five methods that can be used to cultivate a creative attitude*
 - *list and discuss the five approaches that can be followed to generate business ideas*
 - *explain what a feasibility study is*
 - *explain the purpose of using a bow-tie diagram*
 - *list the four questions that must be answered when you conduct a feasibility study*
 - *explain the difference between a feasibility study and a viability study*
-



KEY CONCEPTS

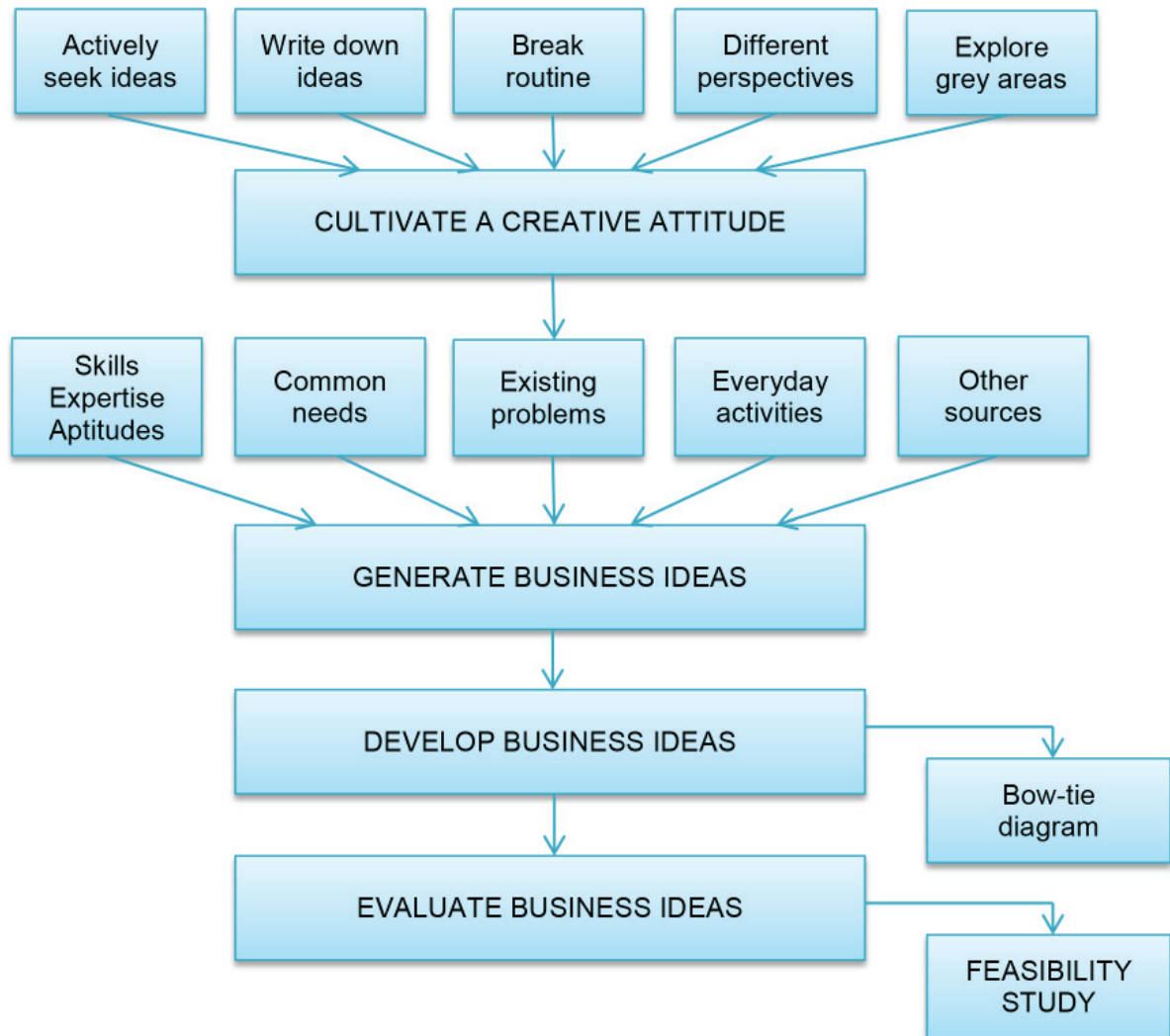
You will need to master the following key concepts to achieve the learning outcomes for this learning unit:

- idea stage
- planning stage
- implementation stage
- creativity
- creative attitude
- divergent thinking
- convergent thinking
- feasibility study

- viability study
- bow-tie diagram



A MIND MAP FOR LEARNING UNIT 3



OVERVIEW

Learning unit 3 deals with the idea stage, the first stage in the creation of an enterprise. The idea stage focuses on identifying, developing and evaluating feasible business ideas. As a prospective entrepreneur, you have probably already thought of possible business ideas, or you may still be looking for a good idea. In this chapter you will get the opportunity to identify and develop various ideas.

Since identifying business ideas is a creative process, you must be able to assume a creative attitude. We will explain how you can apply divergent and convergent thinking in

order to become more creative, and we will introduce you to different techniques to help you to cultivate a creative attitude. We will also discuss the different approaches that you can use to generate business ideas.

Only one of the ideas that you have generated can be converted into an enterprise. You must therefore be familiar with the methods you can use to develop and evaluate your business idea. We will explain how you can use a bow-tie diagram to develop your idea and a feasibility study to evaluate your idea. We will also explain the difference between a feasibility study and a viability study.

3.1 THE THREE STAGES IN CREATING AN ENTERPRISE

This section relates to section 3.1 in your prescribed book.



The creation of an enterprise can be divided into three main stages:

- *the idea stage (chapter 3)*
- *the planning stage (chapters 4 and 5)*
- *the implementation stage (chapter 6)*

These three stages form the theme of the rest of the prescribed textbook.

The idea stage

Definition: Identifying and generating feasible business ideas.

During this stage, the entrepreneur cultivates a creative attitude, **identifies opportunities**, generates and develops business ideas, chooses a suitable idea and tests the feasibility of this idea.

The planning stage

Definition: Investigating the profitable exploitation of the idea and drawing up a business plan.

This is the **decision-making** stage where the entrepreneur tests the viability of the idea by investigating the market and profit potential of the idea. The entrepreneur has to decide on the products he or she wants to offer and determine the potential consumers, target market and expected market share. He or she has to calculate the total cost per unit, decide on the selling price and determine the profit potential of the idea. If the entrepreneur is satisfied with the results of the viability study, he or she has to draw up a business plan.

Implementation stage

Definition: Put the idea into practice by starting the enterprise.

This stage entails all the actions that the entrepreneur has to take to start the enterprise. The entrepreneur has to register the form of enterprise, comply with legal requirements and implement the eight functions of the enterprise.



Refer to Figure 3.1 in the prescribed textbook where this three-stage process is illustrated.

3.2 CULTIVATING A CREATIVE ATTITUDE

In learning unit 1 we mentioned that creativity is one of the personal characteristics of an entrepreneur. An innovative business idea can be very satisfying, but it can also become a huge headache. You must convince people that there is a need for your product or service and therefore you should try to provide specialised or exceptional products or services to distinguish your enterprise from other competitive enterprises. To be able to do this, you must act creatively.

3.2.1 What is creativity?



Creativity is the ability to consider a topic in various ways and come up with something new or identify new ideas.

We could also define creativity by saying that it is seeing the same thing as everybody else but thinking of something different. You must be able to generate new possibilities or alternatives.

3.2.2 Divergent and convergent thinking



Creative thinking can be divided into divergent and convergent thinking. It is important that you study the definitions of both of these concepts in section 3.2.2 in the prescribed textbook. Both of these abilities are essential for creative output.

Divergent thinking

- the ability to think of many original, diverse and elaborate ideas
- essential to the novelty of creative products
- right brain dominant – see things in a perceptual manner

Convergent thinking

- the ability to logically evaluate and choose the best idea from a selection of ideas
- essential to the appropriateness of the products
- left brain dominant – see things in an analytical manner

3.2.3 Methods of cultivating a creative attitude



Activity 3.1

We sometimes wonder if creativity is a given.

Try to answer the following question: Are you born with creativity or is it possible to develop and improve your creative abilities?

.....



Some people are born with the gift of being creative, and it is possible to develop and improve your creative abilities. Creativity is just as much an attitude as it is a manner of thinking. You can think of new ideas by getting used to being creative. Refer to section 3.2.2 in the prescribed textbook.



You can cultivate a creative attitude using the following methods:

- *actively seeking ideas*
- *writing down your ideas*
- *viewing a topic from another person's perspective*
- *breaking your routine*
- *exploring grey areas*

Study these methods in the prescribed textbook.



Check out:

Three unexpected ways to boost creativity:
<http://www.entrepreneur.com/article/247164>

3.2.4 Techniques to enhance the creativity of teams



Read the discussion on the techniques and tools that can be used to enhance team creativity in section 3.2.3 in the prescribed textbook.

3.3 GENERATING BUSINESS IDEAS



The techniques for generating business ideas can be divided into five broad approaches. You must be able to explain these approaches and give examples of each of them.

The entrepreneur's skills, expertise and aptitudes

Skills refer to **manual work** and can be **learned**.

Expertise is based on **knowledge** you acquire. Expertise and knowledge are obtained by **formal studies** and/or **experience**.

Aptitudes refer to **inborn talents**.

Common needs

Try to satisfy a need among various people for the same product by grouping people with the same need together.

Existing problems

Make a list of your problems, or a list of problems that other people experience.

Everyday activities

Be aware of activities that you perform every day, such as going shopping, looking at advertisements or talking to other people.

Other sources

Consider the use of sources such as the Yellow Pages, business publications, inventors' associations, expired patents, advertisements and trade shows.

3.4 THE DEVELOPMENT AND EVALUATION OF BUSINESS IDEAS

3.4.1 The development of business ideas

It is important to realise that although you were encouraged not to limit your creativity in the previous section, not all of these creative ideas will work. Only one of your ideas can be converted into an enterprise on its own or in combination with one or more of the other ideas on your list.



Check out

Five ways to salvage promising ideas that are not working out:
<http://www.entrepreneurmag.co.za/advice/starting-a-business/start-up-advice/5-ways-to-salvage-promising-ideas-that-arent-working-out/>



Before you can evaluate your business idea, you must be clear about the following two matters:

- *What are the main business activities?*
- *Who are your consumers?*

What are the main business activities?

The main business activities may be one or more of the following:

- the manufacturing of a product
- the provision of a service
- the selling of other people's products or services

Who are your consumers?

The consumers may be either or both of the following:

- individuals
- organisations

3.4.1.1 The bow-tie diagram



The bow-tie diagram is illustrated in Figure 3.4 in the prescribed textbook.



A bow-tie diagram can be used to illustrate the possible business activities and consumers of an enterprise, and to help the entrepreneur to develop his or her business idea.

The bow-tie diagram provides six options for your business:

- manufacturing products for individuals
- providing services for individuals
- selling other people's products or services to individuals
- manufacturing products for organisations
- providing services for organisations
- selling other people's products or services to organisations



The bow-tie diagram can be used to develop your business idea in terms of

- *the essence of the idea*
- *the possible combination of ideas*
- *taking a new direction with the idea*

3.4.1.2 The evaluation of business ideas



Activity 3.1

How do you choose the right business idea?

.....



Evaluate each of the ideas on your list by means of a feasibility study.



Check out

The secrets to select and evaluate innovative business ideas:

<http://www.entrepreneurmag.co.za/slideshow/starting-a-business-slideshow/the-secrets-to-select-and-evaluate-innovative-business-ideas/>

3.5 THE FEASIBILITY OF BUSINESS IDEAS

3.5.1 What is feasibility?



Activity 3.2

How would you define a feasibility study? Explain the focus of this study.

.....



Definition of a feasibility study

A feasibility study is a general examination of the potential of the idea to be converted into an enterprise. This means the entrepreneur has to determine whether it would be practically possible to convert the idea into an enterprise.

Focus of a feasibility study

This study focuses on the ability of the entrepreneur to convert the idea into an enterprise. This means the entrepreneur has to determine whether he or she has the skills and expertise to convert the idea into an enterprise, and whether the idea matches his or her aptitudes.

To be feasible, it must be practically possible to convert the idea into an enterprise.

3.5.2 Why do we do a feasibility study?



We do a feasibility study to determine the

- *potential of the idea to be converted into an enterprise*
- *ability of the entrepreneur to convert the idea into an enterprise*

3.5.3 How do we do a feasibility study?



We do a feasibility study by answering the following four questions:

- *Do I want to do what the idea suggests?*
- *Is there a market for my idea?*
- *Can I meet the needs of my consumers?*
- *Can I get the idea to my consumers?*



To understand, interpret and apply these questions, you can read the discussion in section 3.4.2 in the prescribed textbook. It provides a detailed explanation of how a feasibility study is done.

3.5.4 The difference between feasibility and viability

Although feasibility and viability are two different concepts, they are easily confused. We have already explained that a feasibility study entails a general examination of the potential of the idea to be converted into an enterprise and that it focuses on the ability of the entrepreneur to convert the idea into an enterprise.



Activity 3.3

How would you define a viability study? Explain the focus of this study.

.....



Definition of a viability study

A viability study is an in-depth investigation of the market and profit potential of the idea.

Focus of a viability study

This study focuses on the market and profit potential of the idea. This means that the entrepreneur has to determine whether consumers would buy his or her products and whether the expected market share would be sufficient. The entrepreneur has to determine a competitive selling price that covers the cost per unit and would still generate enough profit.

To be viable, the enterprise has to generate enough cash over the short term, as well as sustainable profits over the long term.

Important: Remember that you can only proceed to the viability stage if your idea turns out to be feasible. If your idea is not feasible, you have to identify, develop and evaluate new ideas.



You have now reached the end of learning unit 3.

SUMMARY

In this learning unit you have learned the first step in the creation of an enterprise, namely identifying, developing and evaluating feasible business ideas. We explained the importance of creativity, how to apply creativity techniques, as well as the approaches to generate business ideas. We also paid attention to developing and evaluating the feasibility of business ideas.

We hope you have gained the necessary knowledge to do a feasibility study so that you can evaluate your business ideas. It is important to remember that if your idea turns out not to be feasible, you cannot continue to the next stage in the creation of an enterprise. You will then have to identify new ideas, develop them and test the feasibility of these ideas again.

If your idea is feasible, you can move on to the first part of the planning stage, the viability study, which we will discuss in learning unit 4.



SELF-ASSESSMENT

To test and assess your knowledge of this learning unit, you can now do the following activities:

- (i) *Complete the self-assessment questions on learning unit 3 below. Remember: The only way you can test your knowledge is by answering the questions without looking at the solutions contained in Appendix A.*
- (ii) *Do the self-assessment questions in the prescribed textbook at the end of chapter 3.*

Read the case study below and answer all the questions that follow.

Case study: Power for the Nation

Power cuts have become a real problem for all South Africans, as we suddenly have to schedule our daily lives around Eskom's load shedding. This situation also has a serious effect on the business sector – without power, no manufacturing, trading or service can take place. Businesses have to choose to either close their doors for the period of load shedding and, as a result, suffer losses of thousands of rands, or provide their own power by means of their own generators.

However, the old proverb that "one man's death is another man's breath" also applies to the above situation. When Eskom announced its plans for load shedding, Martin Crous immediately identified an opportunity to sell generators to households and small businesses. After speaking to some of their acquaintances and shop owners in Randburg, Martin and his wife, Jessica, came to the conclusion that the biggest demand would be

for small generators that could meet the basic power needs of an average household for at least four hours, and slightly bigger generators for small businesses.

Martin and Jessica decided to import generators from China and started their own enterprise, Power for the Nation. They registered the enterprise as a partnership. As they only needed some office space and could use their garage to store the generators, they decided to run the enterprise from their home in Randburg. They invested R100 000 of their savings in the enterprise and applied for vehicle financing of R200 000 to buy a small second-hand truck. They also applied for a loan of R90 000 to finance the import of their first consignment of generators. Since Martin and Jessica decided to place orders according to the orders they had received from their customers, they would have a guaranteed income at the end of each transaction. Customers would have to pay for the generators as soon as they had been delivered and installed, so that Power for the Nation could have enough cash to pay for the next consignment from China.

They found a supplier in China that agreed to manufacture the generators on an order basis. The supplier would then use a shipping agent to load a container to be sent by ship to Durban harbour. From there the generators would be transported by road to Randburg by an independent transport agency.

The first consignment was sold out within the first week, and Power for the Nation already had a waiting list of customers who had placed orders. The prices of their generators were slightly higher than those of their main competitors. Since big hardware stores and chain stores such as Builders Warehouse and Game could order in bulk, they could charge lower prices. The competitive advantage of Power for the Nation, however, was that their selling price included the cost of delivery and installation. Martin would deliver the generators personally to the customers and do the installation, should the need arise. As Martin was a qualified electrician, he went to China for training in servicing and repairing the generators. An ordinary generator needs to be serviced after every 1 000 hours. Part of the purchasing agreement with the manufacturer in China entailed that Martin would receive free spare parts equal to 10% of the monetary value of each consignment of generators.

Since Martin and Jessica started importing these generators six months ago, the enterprise has grown to such an extent that they had to rent a warehouse in an industrial area to store the generators. The need for alternative power will definitely not decline within the near future, since Eskom has already indicated that there is no short-term solution to the electricity shortage in South Africa. However, Martin and Jessica are aware of the fact that if they want to survive over the long term, they will have to extend their target market to other suburbs as well.

Multiple-choice questions

- (1) Martin Crous **identified the opportunity to sell generators** to households and small businesses during the _____ stage in the creation of Power for the Nation.
 - (1) idea
 - (2) planning
 - (3) viability
 - (4) implementation

- (2) Martin and Jessica **invested R100 000 of their savings in the enterprise** during the _____ stage in the creation of Power for the Nation.
- (1) idea
 - (2) planning
 - (3) viability
 - (4) implementation
- (3) Martin and Jessica **decided to import generators from China** during the _____ stage in the creation of Power for the Nation.
- (1) idea
 - (2) feasibility
 - (3) planning
 - (4) implementation
- (4) To come up with creative ideas, Martin and Jessica had to apply divergent and convergent thinking. **Divergent thinking** _____ .
- (a) entails the ability to evaluate ideas logically
 - (b) is essential to the novelty of creative ideas
 - (c) entails the ability to think of many original ideas
 - (d) is essential to the appropriateness of the products

Choose the correct option:

- (1) a, b
 - (2) b, c
 - (3) c, d
 - (4) b, d
- (5) If Martin and Jessica judged everything they observed on **the strength of the ideas they could develop from it**, they would have _____ as a method to cultivate a creative attitude.
- (1) actively sought ideas
 - (2) written down their ideas
 - (3) viewed the topic from another person's point of view
 - (4) explored grey areas
- (6) If Martin and Jessica used the **breaking of their routine** as a method to cultivate a creative attitude, they would have _____ .
- (a) taken note of how they performed their everyday activities
 - (b) started conversations with strangers
 - (c) done things that they had never done before
 - (d) explored the grey areas between right and wrong

Choose the correct option:

- (1) a, b
- (2) a, c, d

- (3) a, b, c, d
(4) a, b, c
- (7) As Martin was a **qualified electrician**, he went to China for training in servicing and repairing the generators. Martin used his _____ to generate the idea of servicing and repairing the generators himself.
- (1) skills
(2) expertise
(3) aptitudes
(4) natural talents
- (8) After **speaking to some of their acquaintances and shop owners**, Martin and Jessica came to the conclusion that there was a big need for generators in Randburg. They used _____ to generate the idea of importing generators from China.
- (1) everyday activities
(2) Martin's skills, expertise and aptitudes
(3) common needs
(4) other sources
- (9) Martin and Jessica would have used a _____ to **develop their business idea** of selling generators to the residents of Randburg.
- (1) bow-tie diagram
(2) profit analysis
(3) feasibility study
(4) viability study
- (10) Martin and Jessica had to conduct a **feasibility study** to _____ .
- (a) do a general examination of the idea
(b) determine their ability to convert the idea into an enterprise
(c) determine the market potential of the idea
(d) determine the profit potential of the idea

Choose the correct option:

- (1) a, b
(2) a, c
(3) a, d
(4) c, d

SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS



Please refer to Appendix A for the suggested solutions to the self-assessment questions.

Learning Unit 4

The viability of a business idea

STUDY CHAPTER 4 IN THE PRESCRIBED BOOK

CONTENTS

- The viability of a business idea
 - The market potential of a business idea
 - The profit potential of a business idea
 - When is an idea viable?
-



LEARNING OBJECTIVES

When you have worked through learning unit 4, you should be able to

- *explain the answers that the market research should provide*
 - *explain the method that can be used to establish whether there is a need for a specific product or service*
 - *define the mission and objectives of an enterprise*
 - *list the four segments into which the total potential market can be divided and give examples of each segment*
 - *explain what a target market is*
 - *compile a SWOT analysis for an enterprise*
 - *list and explain the two factors that determine the size of the expected market share*
 - *list the three scenarios for which the expected market share should be calculated and explain why we must calculate the expected market share for these three scenarios and the purpose for which these calculations are used*
 - *explain the components for classifying costs*
 - *explain the different methods of calculating the total cost per unit for a manufacturing enterprise, a commercial enterprise and a service enterprise*
 - *explain what factors should be considered when we calculate the selling price of a product or service*
 - *explain what a pro forma income statement is and how to calculate the expected gross profit and the expected net profit*
 - *explain what the break-even point is, how it is calculated and how it can be lowered*
 - *explain the importance of having enough cash available*
 - *define a cash budget and explain the purpose and components of a cash budget*
-



KEY CONCEPTS

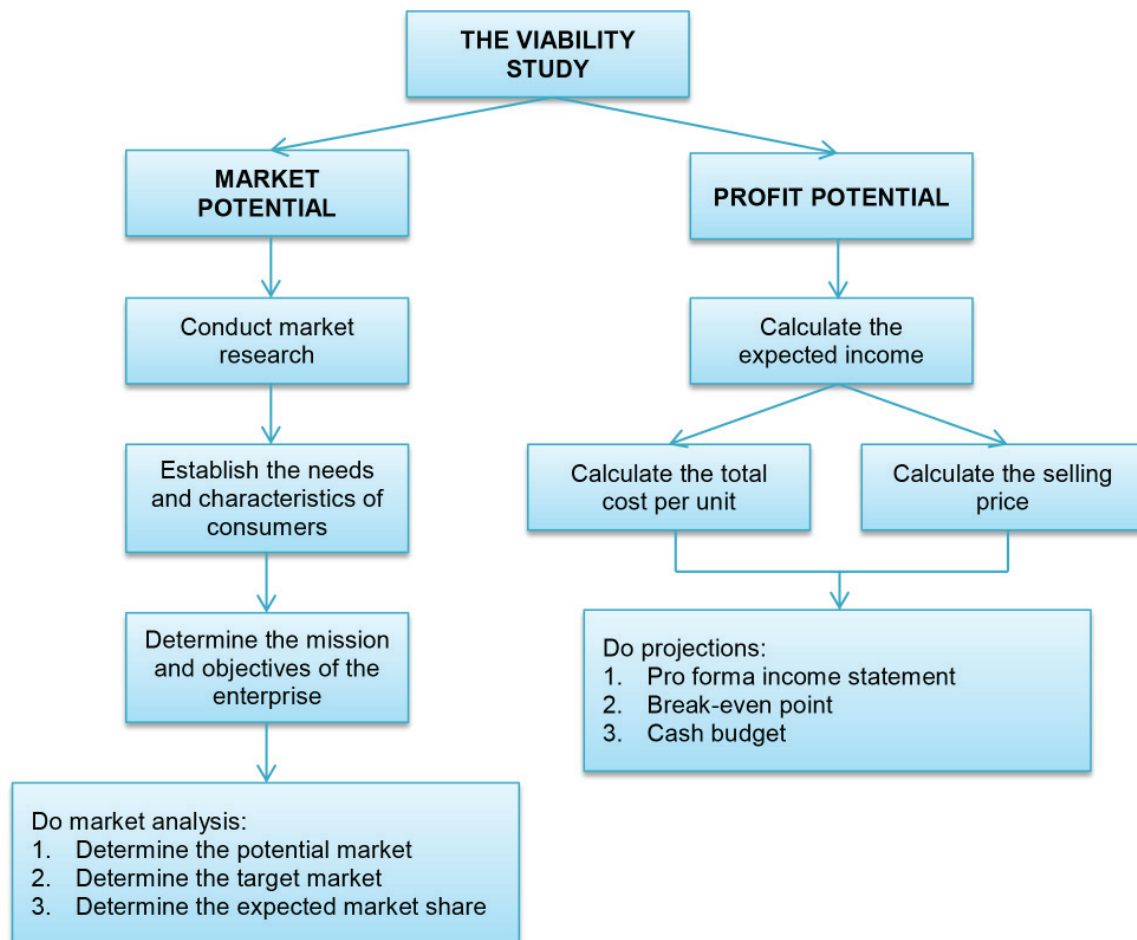
You will need to master the following key concepts to achieve the learning outcomes for this learning unit:

- viability study
- market research
- mission and objectives
- total potential market
- market segmentation
- target market
- SWOT analysis
- market share
- fixed and variable costs
- direct and indirect costs
- total cost per unit
- cost price
- selling price
- pro forma income statement
- break-even point
- cash budget



A MIND MAP FOR LEARNING UNIT 4

The planning stage



OVERVIEW

This learning unit deals with the essence of a viability study – the importance of estimating the interest in the enterprise and its offering, the expected sales in units at a certain price and the different costs involved. You will also come to terms with the importance, meaning and necessity of a SWOT analysis to test the viability of your business idea. You will learn how market research is conducted, what market segmentation entails and how to determine the expected market share of your potential enterprise. We will also teach you how to do projections and introduce you to some financial statements and budgets.

When you have studied this learning unit, we hope that you will be able to test the viability of your business idea.

4.1 THE VIABILITY OF A BUSINESS IDEA

In learning unit 3 we explained the three stages to which an entrepreneur must pay attention before he or she can start an enterprise and we discussed the first stage, the idea stage, in detail. We now move on to the second stage, the planning stage, in the creation of an enterprise. The planning stage consists of two parts – the viability study and the business plan. In learning unit 4 we will discuss the first part of the planning stage, namely the viability study.

To see where the viability study fits in, refer to Figure 4.1 in the prescribed textbook that illustrates the planning stage.

Before committing resources to a new enterprise, it is essential that the entrepreneur establish whether the business idea is viable. This requires a viability study.

4.1.1 Why do we do a viability study?



Activity 4.1

Can you still remember the definition of a viability study?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

It is extremely important to investigate the market and profit potential of the business idea before we can continue with the second part of the planning stage, namely drawing up the business plan. If an idea is not viable, we are going waste our time and money by drawing up a business plan.

4.2 THE MARKET POTENTIAL OF A BUSINESS IDEA

To determine the market potential, the following four steps should be taken:

- Step 1:** Conduct market research.
- Step 2:** Establish the needs and characteristics of consumers.
- Step 3:** Determine the mission and objectives of the enterprise.
- Step 4:** Do a market analysis to determine the total potential market, target market and expected market share.

4.2.1 Step 1: Conduct market research



Definition of the concept of market research

Market research entails gathering information on a certain market so that better and more informed decisions can be made.

Market research will provide answers to the following questions:

- Is there a **need** for the products? (Need analysis)
- **Who** is going to buy the products? (Customer profile)
- How **many** products can be sold? (Market share)
- What **price** can be charged for the products? (Price analysis)

Market research will also provide answers to make the following assumptions:

- The number of products that must be sold to show a **profit** (Profit analysis)
- Whether the **cash flow** will be sufficient to run the business (Cash flow analysis)

4.2.2 Step 2: Establish the needs and characteristics of consumers

It is essential that the entrepreneur do a proper needs analysis of the consumers and their characteristics.

As an entrepreneur, you must find out the following:

- Who are your consumers and what are their needs?
- What products or services do the consumers want?
- How do consumers make their buying decisions?

The products or services that consumers want may not necessarily be what you want to offer. This implies that you require information on the characteristics, needs and purchasing power of your customers.



Activity 4.2

What is a customer profile?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.



Did you know:

The better you know your customer, the better you can position your brand?

<http://www.entrepreneur.com/article/236628>

Five steps you can use to find your niche:

<http://www.entrepreneurmag.co.za/advice/starting-a-business/launch/5-steps-you-can-use-to-find-your-niche/>

Why it pays to know your customers:

<http://www.smesouthafrica.co.za/16238/Why-it-pays-to-know-your-customer/>

The needs of the market (consumers) form the basis of the marketing strategy. After you have analysed the needs of the consumers, it is important to determine how you are going to meet those needs profitably.

You must work out how you can provide the right products or services at the right prices and in so doing also make a profit. You must also determine how you are going to distribute the products or services to the market and how you are going to make the consumers aware of the products or services.



Activity 4.3

What is a marketing strategy?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

The marketing strategy is based on the following four elements:

- product
- price
- distribution
- marketing communication

We will discuss the marketing strategy in more detail in learning unit 6.

How do we establish whether there is a need for a product or service?

It is important to take the four steps below in order to obtain the information you require in deciding about the need for a product or service.

(1) List the features of the product or service.

This will help the entrepreneur to focus on those features that may be important to the market, evaluate the offering to see if it really adds value to the market and use it as a guide to test the needs of the market.

(2) Determine who occupies the market (the major competitors) and who the industry leaders, suppliers and other role players in the market are.

Make a thorough analysis of your competitors to establish who they are, where they are, how big their enterprises are, what products they offer and what prices they charge.

(3) Identify the possible consumers and segment the market.

Determine the total market potential, do market segmentation, evaluate the segments according to size, demand and profitability and decide on the target market.

(4) Use the information obtained and draw up a final list of the following:

- the features of the product or service
- the needs and profiles of the consumers
- the potential number of consumers



Study the above steps in section 4.3 in the prescribed textbook.

Once you have information on the needs and characteristics of your potential consumers, you can

- *determine what kind of enterprise you want to start*
- *define your business and determine your objectives*



Check out:

Advertising legend Ivan Moroke on the five questions your marketing strategy absolutely has to answer:

<http://www.entrepreneurmag.co.za/advice/marketing/marketing-tactics/the-golden-rules-of-marketing/>

4.2.3 Step 3: Determine the mission and objectives of the enterprise



Activity 4.4

In learning unit 2 we discussed the mission and objectives of an enterprise. Can you still remember how we defined the mission and objectives?

.....



We defined the mission and objectives broadly as what you want to achieve with the enterprise and how you want to achieve it.

You have already decided what type of enterprise you will be running. You must now pay attention to the mission of the enterprise so that you know exactly what you intend to do with your enterprise. You should spend enough time on determining the mission and objectives of your enterprise.



Definition of the mission of the business

The mission is the broad goal of an enterprise. It defines the fundamental and unique purpose of an enterprise and identifies its products or services and consumers.

After the mission has been set, it is possible to formulate objectives for the enterprise. An objective is something that the enterprise wants to achieve over a specific time. Objectives must be set so that you have something against which to measure progress. Refer to learning unit 2 for the discussion on primary and secondary objectives.

Objectives should meet the following requirements:

- Objectives must be measurable.
- Objectives must be realistic and attainable.
- Objectives must be clear and understandable.
- Objectives must be set within a specific time frame.



Check out:

How to write one inspiring mission statement:

<http://www.entrepreneurmag.co.za/advice/starting-a-business/start-up-advice/video-how-to-write-one-inspiring-mission-statement/>

4.2.4 Step 4: Do a market analysis



Activity 4.5

List the three steps that must be taken to do a market analysis.

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

4.2.4.1 Determine the total potential market

(a) Do market segmentation



Definition of market segmentation

The division of the total potential heterogeneous consumer market into smaller homogeneous groups that have similarities or characteristics in common.

This means that the total consumer market, which consists of consumers who are all different (heterogeneous), is divided into groups of people who are all similar (homogeneous).

How do we do market segmentation?



Geographic

- **Where are the consumers** or where do they live (in which area)?

Demographic

- **Who are the consumers** – what are their occupation and **average income**?
- What are their average age, gender, social class and the size of their households?

Psychographic (Lifestyle)

- **What products do they buy** (prefer) or on what products do they spend their money?
- What type of lifestyle do they maintain?

Behaviouristic (Buying pattern)

- **When do they buy the products?**
- How **often** do they buy?

It is **important** to remember that the types of question that you will ask under each segment will depend on the **type of enterprise** and the **types of product** that you are going to offer.

(b) Examine each segment according to the following:

- **Accessibility** – will you be able to reach your consumers?
- **Measurability** – can you determine the number of consumers in the segment?
- **Profitability** – can the consumer pay the price for your product that will enable you to make a profit?

4.2.4.2 Determine the target market



Definition of a target market

The target market is the portion of the total market that you can reach with your products or services.

This refers to a specific market segment or segments at which you will **direct** your products or services or the **people** to whom you are going to sell your products or services.

(a) How do we determine the target market?



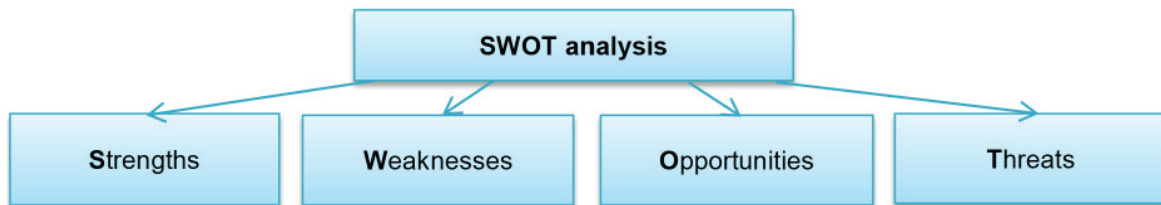
- (1) First find out what part of the total potential market is served by your competitors by making a list of your competitors and determining which market segment is their target market.
- (2) Then deduct their market share from the total potential market.



(b) How do we examine the competitors?

Do a thorough **analysis of your competitors** by determining, for example, who they are, where they are, what products they sell and what prices they charge.

Now determine how well you can **compete** with them by compiling a **SWOT analysis**. A SWOT analysis is a list of the strengths, weaknesses, opportunities and threats of the entrepreneur. Remember, the strengths and weaknesses come from the **micro-environment** and the opportunities and threats from the **market and macro-environments**.



Example of a SWOT analysis

Strengths	Weaknesses
<ul style="list-style-type: none"> • good location • sufficient capital • experienced labour • experience in management • quality products 	<ul style="list-style-type: none"> • premises too small • lack of capital • inexperienced staff • lack of management skills • product quality below standard
Opportunities	Threats
<ul style="list-style-type: none"> • no competition in the area • cheaper supplies of raw materials • technologically advanced machinery • enter new markets • can include other products • can expand enterprise 	<ul style="list-style-type: none"> • competition • unreliable suppliers • outdated machinery • increase in interest rates • crime in the area • consumer boycotts

Please note: The above are only a few examples – your SWOT analysis will depend on your particular situation.

Remember: You cannot list the same example as both a strength and a weakness – it cannot be both. For example, the amount of available capital may be either a strength or a weakness. The same applies to opportunities and threats. You must use different examples when you compile a SWOT analysis.



Did you know?

Do you know your business strengths and weaknesses?

<http://www.smesouthafrica.co.za/Do-you-know-your-business-strengths-and-weaknesses/>

SWOT analysis examples

<http://www.entrepreneurmag.co.za/advice/business-plans/business-plan-research-and-preparation/swot-analysis-examples/>

4.2.4.3 Determine the expected market share



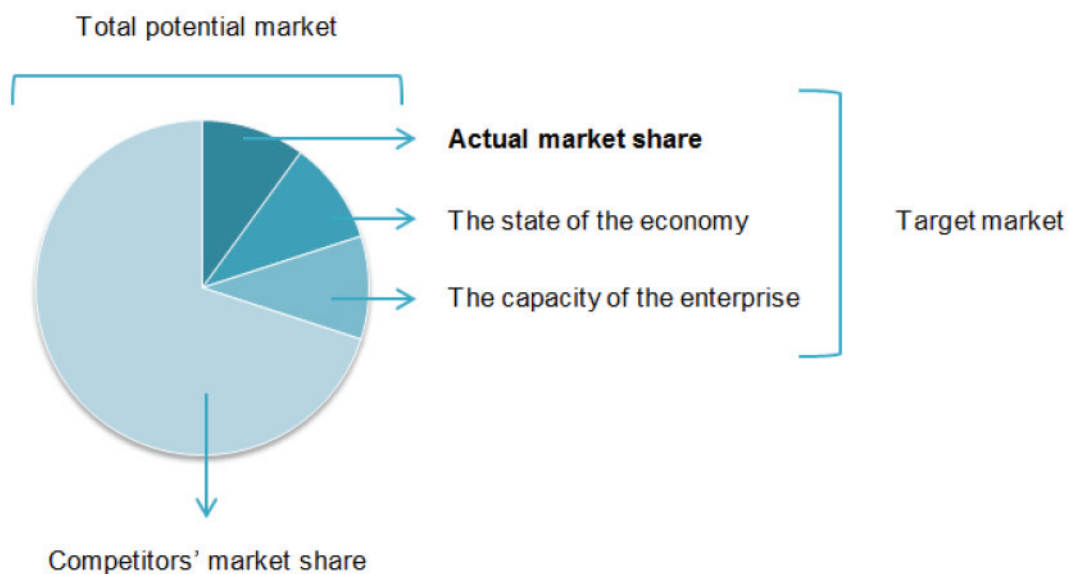
Definition of the expected market share

*The expected market share is that part of the target market that an **enterprise will be able to serve** on the basis of its **production capacity** and the **state of the country's economy**.*

This means that an entrepreneur cannot assume that he or she would be able to serve the total potential target market, as the state of the country's economy and the capacity of his or her enterprise could restrict the size of the actual market share.

The size of the expected market share will be determined by the

- capacity of the enterprise
- state of the economy



(a) The capacity (production capacity) of the enterprise



Definition of the capacity of the enterprise

*The capacity of the enterprise is the **greatest possible workload** that an enterprise can handle **within a certain period**.*

This means the **maximum number of products** that an enterprise can manufacture or sell **within a certain period**. If the capacity of the enterprise is too small, it restricts the number of products or services that can be provided and the ability of the enterprise to satisfy the potential demand.

(b) The state of the economy



The state of the country's economy

*The state of the country's economy determines the interest rate and inflation rate, which directly influence the **disposable income or buying power** of consumers.*

There may be a very big demand for the product or service, but if the economy of the country is in a decline, consumers do not have the necessary money to buy the product or service. If inflation increases, the buying power of consumers decreases and therefore they would rather spend money on necessities than on luxuries. The type of product or service that the entrepreneur offers will determine how the economy will influence his or her enterprise.



Check out:

The top 3 economic challenges facing entrepreneurs in 2016:
<http://www.entrepreneur.com/article/253473>

Why do we calculate the expected market share?

Calculating the expected market share helps determine whether to go ahead with the business idea. It indicates the number of consumers that will buy the products or services; in other words, it indicates how many products or services (or units) the enterprise can sell. We use this figure to calculate the sales figure or turnover in the income statement (units sold multiplied by the price per unit), which is the starting point of determining the profit potential of the business idea.



To make provision for restrictions and uncertain conditions, the entrepreneur must calculate the expected market share for the following **three scenarios**:

- *a very prosperous scenario*
- *a most probable or likely scenario*
- *a very conservative or weak scenario*

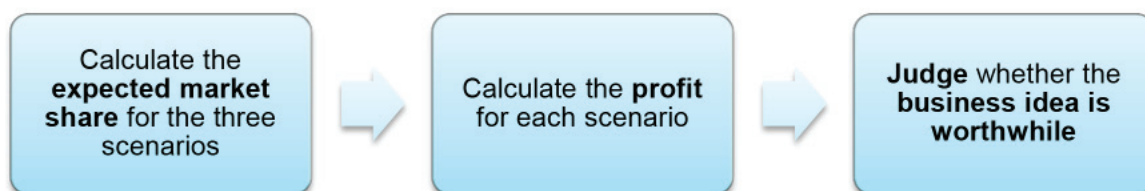
It is extremely important to **calculate the market share as accurately as possible**, as it has a direct influence on the calculation of your **income**. To be realistic and to reduce risk, the entrepreneur must calculate the market share for all three different scenarios or circumstances.

The entrepreneur must then calculate the profit for each of these scenarios and judge from that whether it is worth going ahead with the business idea.

The above process can be summarised and illustrated as follows:

- Calculate the expected market share for the three different scenarios.

- Calculate the profit for each scenario.
- Judge from this whether it is worth going ahead with the idea.



We have now reached the second part of the viability study in which we are going to determine the profit potential of the business idea. Remember that the viability study consists of two main parts, namely determining the market potential and determining the profit potential.

4.3 THE PROFIT POTENTIAL OF A BUSINESS IDEA

To determine the profit potential, the following two steps must be taken:

Step 1: Calculate the expected income.

Step 2: Do projections.

4.3.1 Step 1: Calculate the expected income

After calculating the expected market share and the number of units that can be sold, it is time to calculate the expected income from the sales.



Activity 4.6

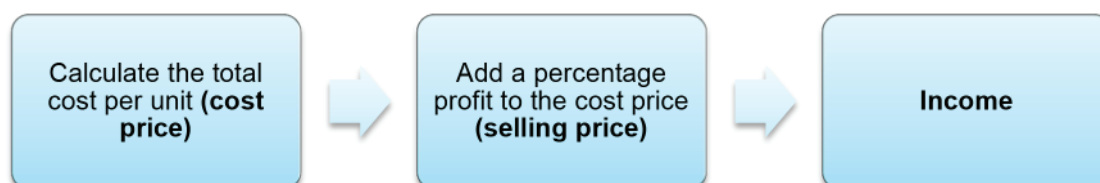
Name the two steps in calculating the expected income.

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

Calculating the expected income can be illustrated as follows:



4.3.1.1 Calculate the total cost per unit (cost price)

(a) Classify costs

Before we can calculate the total cost per unit, we must first look at the classification of the different costs.

We distinguish between the following types of cost:

- fixed costs and variable costs
- direct costs and indirect costs



You must be able to explain the different cost concepts and to give examples of each of them.

Important: We will NOT expect you to do any calculations.

Fixed costs

Definition: Costs that remain the same, regardless of the number of units manufactured. Fixed costs are fixed in total but variable per unit.

Examples: Rent or salaries.

Variable costs

Definition: Costs that increase proportionally with the number of units manufactured. Variable costs are variable in total but fixed per unit.

Examples: Cost of raw materials or wages for overtime.

Direct costs

Definition: Costs that can be allocated directly to the manufacturing of a product.

Examples: Direct material costs or direct labour costs.

Indirect costs

Definition: Costs that cannot be allocated directly to the manufacturing of a product. Indirect costs are also known as overheads.

Examples: Rent or indirect wages.



Read the explanations of the different types of costs in section 4.7.1 in the prescribed textbook.



Check out

The relationship of direct and indirect costs with fixed and variable costs:
<http://www.efinancemanagement.com/costing-terms/relationship-of-direct-indirect-costs-with-fixed-variable-costs>

(b) Calculate the total cost per unit

The way the cost of a product is calculated depends on the type of enterprise. There are specific differences in calculating the cost per unit for the following types of enterprise:

- (1) manufacturing enterprises
- (2) service enterprises
- (3) commercial (trade) enterprises

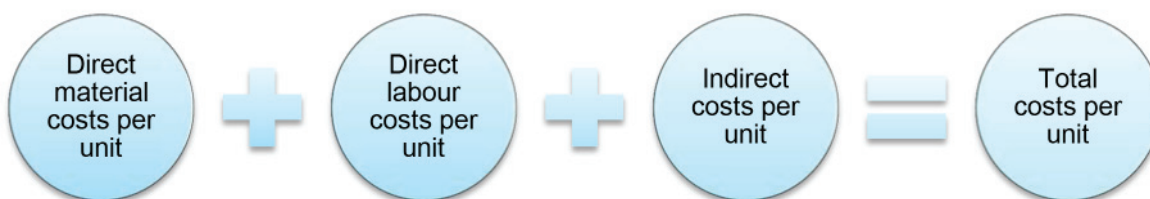


Study the different formulae or methods to calculate the cost per unit for a specific type of enterprise. See figures 4.10, 4.11 and 4.12.

Important: We will NOT expect you to do any calculations.

1. Calculating the total cost per unit for a manufacturing enterprise

Manufacturing costs + Commercial overheads = Total costs



Method

- (1) Calculate the direct costs of materials used to manufacture one unit.
- (2) Calculate the direct costs of labour needed to manufacture one unit.
- (3) Calculate the indirect costs per unit:
 Add manufacturing overheads, administrative overheads and marketing overheads.
 Divide the total overhead costs by the number of products manufactured in the same period in which the costs were incurred.
- (4) Add all the costs together (steps 1, 2 and 3) to get the total cost per unit.

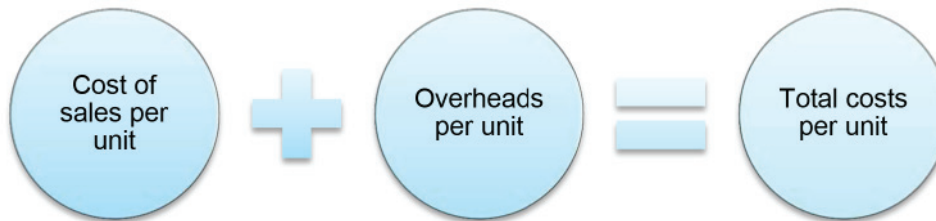
2. Calculating the total cost per unit for a service enterprise



Method

- (1) **Calculate the total costs per month.**
- (2) **Calculate the number of business hours per month.**
 $\text{Hours per day} \times \text{Days per week} \times \text{Weeks per year} \div \text{Months per year}$
 $= \text{Hours per month}$
- (3) **Calculate the cost per hour.**
 $\text{Total costs per month} \div \text{Number of working hours (business hours) per month}$

3. Calculating the total cost per unit for a commercial (trade) enterprise



Method

- (1) **Calculate the cost of sales of one product.**
 $\text{Opening stock} + \text{Cost of purchased stock} - \text{Closing stock} = \text{Cost of sales}$
 $\div \text{Number of items sold}$
 $= \text{Cost of sales per unit}$
- (2) **Calculate the contribution of the overheads.**
Add administrative and marketing overheads.
Divide the total by number of units sold.
- (3) **Add cost of sales per unit and overheads per unit.**



Read the explanations of calculating the total cost per unit for the different types of enterprise in section 4.7.1 in the prescribed textbook.

4.3.1.2 Calculate the selling price



There are two very important factors that have to be considered when determining the selling price of a product or service:

- *The selling price should at least cover all the costs incurred.*
- *The selling price is directly influenced by the competitors' prices.*

(a) The selling price should at least cover the costs incurred

If the costs are not covered by the selling price, the enterprise will show a loss from the start and will not survive. The selling price must make a contribution towards profit. Remember, the main reason (primary objective) for starting an enterprise is to make a profit. The profit is the return on the investment that the entrepreneur has made in his or her enterprise.

(b) The selling price is directly influenced by the competitors' prices

Your price must be more or less the same as the competitors' prices, unless you offer more benefits. If your business has exceptional strengths, this can justify high prices. However, if your business has many weaknesses, you will be obliged to charge lower prices than your competitors.

How do we calculate the selling price?



Having established the selling price, we can now calculate the potential income and net profit from the sales of our products or services.

4.3.2 Step 2: Do projections

The final part of our viability study is based on the following financial projections:

- (1) Calculate the expected net profit (pro forma income statement).
- (2) Calculate the break-even point.
- (3) Do cash planning by preparing the cash budget (cash forecast).



Study these financial projections carefully. You must be able to define them, know how they are compiled (the formulae) and explain the main entries.

Important: We will NOT expect you to do any calculations or to prepare financial statements.

4.3.2.1 Calculate the expected net profit

How do we calculate the expected net profit?

We calculate the expected net profit by drawing up a pro forma income statement.



Definition of an income statement

An income statement is a summary of the **income and expenditure** of an enterprise **over a specific period**.

To be viable, the business idea must be profitable. To determine whether the idea would be profitable, we have to multiply the expected number of units that would be sold (which we determined in the market analysis) by the selling price (which we determined in the first part of our profit analysis) to get our sales figure (turnover). From the turnover, we

then have to deduct the cost of sales to get the amount of gross profit. Then we have to deduct all the expenses from the gross profit to get the expected net profit.

The main entries on an income statement are as follows:

Sales (units sold multiplied by the selling price)

– Cost of sales

= Gross profit/income

– Expenses

= Net profit/income

Refer to learning unit 5 of the study guide for the explanations of the main entries and examples of income statements.



Activity 4.7

Are an income statement and a pro forma income statement the same?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

What is the purpose of drawing up a pro forma income statement?

The purpose of drawing up a pro forma income statement is to calculate the net profit for the three scenarios we have used to determine our expected market share.



Activity 4.8

Can you still remember these three scenarios?

.....

To make an informed decision about our expected net profit, we are going to draw up a pro forma income statement for a very prosperous scenario, a most probable scenario and a very weak scenario.

4.3.2.2 Calculate the break-even point

During the first part of the profit analysis we emphasised the role that cost plays in determining the selling price of a product or service. We are now going to determine how many products the entrepreneur has to sell in order to cover all the costs.



Definition of a break-even point

A break-even point is the **number of units that must be sold for the income and expenditure to be equal**. In other words, this is the point where all the costs and expenditure are covered. At this point the net profit will be equal to R0, which means neither a profit nor a loss is shown.

How do we calculate the break-even point?

The break-even point can be calculated in rand value or in units.

Example 1: Calculate the break-even point in units

Formula

$$\text{Units} = \frac{\text{Fixed costs}}{\text{Price per unit} - \text{Variable cost per unit}}$$

Example 2: Calculate the break-even point in rand value

Formula

$$\text{Rand} = \frac{\text{Fixed costs}}{\text{Gross profit margin \%}} \times 100$$

Refer to learning unit 5 of the study guide for an example of the calculation of the break-even point in units.

Ways to lower the break-even point

The lower the break-even point, the sooner the enterprise can start making a profit. Therefore, the entrepreneur should recalculate the break-even point regularly.

The break-even point can be lowered by

- lowering direct costs
- exercising cost control over fixed expenses
- increasing prices



Study the ways to lower the break-even point in section 4.9.1 in the prescribed textbook.

Benefits of calculating the break-even point

By knowing the break-even figure, the entrepreneur can manage the business more effectively.

- The entrepreneur can allocate sales and marketing efforts (such as advertising) to sell more products in order to reach the break-even point sooner.
- Cost can be controlled if a “slow” month is predicted.
- Profits can be maximised by knowing and understanding the break-even figure.

4.3.2.3 Do cash planning: the cash budget



Activity 4.9

Why is it so important for an enterprise to have enough cash available?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.



Definition of a cash budget

A cash budget is a formal plan for forecasting future receipts and payments of cash. It is designed to cover a period of one year and is divided into twelve monthly or four quarterly periods.

The purpose of a cash budget

- It shows how cash flows in and out of the enterprise.
- It may be used to plan short-term credit needs.
- It determines future ability to pay debts and expenses, because it helps the entrepreneur to predict months when there may be a cash shortfall.
- Financial institutions require proper cash budgets before making a capital expenditure for new assets and expansion. Financial institutions would be more inclined to grant loans because it shows that the entrepreneur exercises proper financial planning.
- A business that operates on a cash basis will stand a better chance of getting loans in difficult times.
- It highlights problem areas in payment schedules, which can then be used to spread payments evenly throughout the entire year.

The main entries on a cash budget are as follows:

Total cash receipts
– Total cash payments
= Net cash balance

+ Opening cash balance
= Closing cash balance

Refer to learning unit 5 of the study guide for the explanations of the main entries and an example of a cash budget.



Read the discussion in section 4.10 on the cash budget in the prescribed textbook.

4.4 WHEN IS AN IDEA VIABLE?

To be viable, the enterprise must be able to

- generate sustainable profits over the long term
- generate enough cash (money) to meet its daily expenses

If these requirements cannot be met, the entrepreneur cannot start the enterprise. The entrepreneur then has to start over by looking for a new idea, testing the feasibility of the new idea and going through the entire process of the viability study again.

If the entrepreneur decides that the idea is viable, the next step in the planning stage will be to draw up a business plan.



You have now reached the end of learning unit 4.

SUMMARY

In this learning unit you have learned that, before you can turn a business idea into an enterprise, you must do a viability study. In the first part of the viability study you must determine the market potential of the idea. To do this, you must establish the needs in the market, conduct market research, set the mission and objectives of the enterprise and decide on the types of product and the consumers you want to focus on. Then you have to do market segmentation, choose your target market and determine the expected market share to establish how many products you can sell.

In the second part of the viability study you must determine the profit potential of the idea. You must calculate your cost price, decide on the profit percentage and determine your selling price in order to calculate your income and net profit. You must calculate the break-even point and make estimations by using tools such as the pro forma income statement and the cash budget.

Finally you must decide whether your business idea is viable. In other words, you must decide whether the enterprise can generate sustainable profits over the long term, as well as enough cash to meet the daily expenses.

If the market and profit potential do not yield satisfactory results, it is not worthwhile going ahead with the idea and then you will have to look for a new idea, test the feasibility of the idea and go through all the steps in the viability study again. If the market potential and profit potential show that your business idea is viable, you can move on to the second part of the planning stage, which entails drawing up a business plan. We will discuss the business plan in learning unit 5.



SELF-ASSESSMENT

To test and assess your knowledge of this chapter, you can now do the following activities:

- (i) *Complete the self-assessment questions on learning unit 4 below. Remember: The only way you can test your knowledge is by answering the questions without looking at the solutions contained in Appendix A.*
- (ii) *Do the self-assessment questions in the prescribed textbook at the end of chapter 4.*

Read the case study below and answer all the questions that follow.

Case study: The Feather Dusters

While working as an administrative manager for a big insurance company and raising two toddlers, Wendy Williams always wished that she could find a team of reliable people to clean her house thoroughly in just a few hours. She talked to her neighbours and acquaintances in Boston, a suburb in Bellville, and realised that most of them worked full-time and that they all experienced a common problem, namely the lack of reliable, trained domestic workers. She established that people had to employ and train new domestic workers on a regular basis, many houses in the suburb did not have staff quarters, legislation regulating the employment of domestic workers had persuaded many people to rather not employ full-time domestic workers and there were no cleaning services in the immediate area of Boston. She resigned from her job and started her own enterprise, The Feather Dusters.

Wendy started on a small scale, since she did not have much capital. She used her pension payout and savings to convert her garage into an office and had to take out a loan of R30 000 to purchase two vacuum cleaners and office equipment. She also applied for a bank overdraft to purchase cleaning detergents, feather dusters and brooms. Wendy employed six employees – two to do the dusting and sweeping, two to vacuum the carpets and two to clean the bathrooms, kitchens and tiles. She used her own vehicle, a Volkswagen Kombi, to transport the employees and equipment from one workplace to another.

Initially Wendy started by cleaning only the homes of her friends. She offered only two services – a basic cleaning service that included dusting, vacuuming and cleaning bathrooms and floors, and a more comprehensive service that also included cleaning kitchen appliances such as stoves and ovens, polishing furniture and washing windows. Her prices were determined according to the type and amount of work, as well as the size of the house.

As more and more people became aware of her enterprise, the orders started streaming in and she could not accept all of them. Wendy had to employ more people, put together different teams and appoint a supervisor for each team. She had to buy equipment for each team, as well as vehicles to transport the teams. Her premises became far too small to store the stock and to accommodate so many employees and vehicles.

Wendy realised that she could no longer handle the enterprise on her own. She decided to involve four of her friends in the enterprise to accumulate more capital and to help her with the management, and they registered the new enterprise as a partnership. The enterprise was divided into formal departments, with an experienced person in charge of every function. Although Wendy and her partners invested R100 000 of their own capital in the business, they still had to apply for financing to purchase new cleaning equipment, office equipment and vehicles. They rented a building in an office park in Bellville with enough space for a reception area, offices for each of the departments, a storeroom, a training centre for new employees, a room where the employees could relax between their shifts and safe parking for the vehicles.

Wendy and the other owners decided to include washing and ironing curtains and linen, as well as steam cleaning carpets and lounge suites in their range of services. They also realised that they had to advertise their services to retain and increase their market share and decided to launch a marketing campaign to make potential clients in the surrounding suburbs aware of their cleaning services.

Multiple-choice questions

- (1) Before Wendy **could determine her expected market share**, she had to _____ .
- (a) calculate the total cost per unit of the cleaning services
 - (b) calculate the selling price of the cleaning services
 - (c) determine the total potential market for cleaning services
 - (d) determine her target market

Choose the correct option:

- (1) a, b
 - (2) b, c
 - (3) c, d
 - (4) b, d
- (2) The people in Boston indicated that **they would rather use cleaning services than employ domestic workers**. This relates to the _____ segment of the total potential market for cleaning services.
- (1) geographic
 - (2) demographic
 - (3) psychographic
 - (4) behaviouristic
- (3) Most people would most probably **use the basic cleaning services on a weekly basis**. This relates to the _____ segment of The Feather Dusters' total potential market.

- (1) geographic
 - (2) demographic
 - (3) psychographic
 - (4) behaviouristic
- (4) Most of the women in Boston **work full-time and do not have enough time** to clean their houses themselves. This relates to the _____ segment of the total potential market for cleaning services.
- (1) geographic
 - (2) demographic
 - (3) psychographic
 - (4) behaviouristic
- (5) Power cuts could prevent The Feather Dusters from keeping to their daily schedules. They could list this example as _____ in their SWOT analysis.
- (1) a strength
 - (2) a weakness
 - (3) an opportunity
 - (4) a threat
- (6) Legislation regulating the employment of domestic workers had persuaded many people to rather not employ full-time domestic workers. This could be regarded as _____ for The Feather Dusters.
- (1) a strength
 - (2) a weakness
 - (3) an opportunity
 - (4) a threat
- (7) As more and more people became aware of her enterprise, the orders started streaming in and Wendy **could not accept all of them**. This is an example of how the _____ could restrict the ability of The Feather Dusters to satisfy the potential demand for cleaning services.
- (1) capacity of the enterprise
 - (2) economy of the country
 - (3) buying power of the target market
 - (4) size of the market
- (8) The amount that The Feather Dusters **have to spend on fuel** to transport the cleaning ladies from one workplace to another could be regarded as _____ costs.
- (1) fixed
 - (2) variable
 - (3) overhead
 - (4) indirect
- (9) To **calculate the total costs per unit** of providing cleaning services, The Feather Dusters would divide the total costs per month by the _____ .

- (1) direct labour costs
 - (2) cost of renting the premises
 - (3) hours worked per month
 - (4) overheads per month
- (10) To **calculate the break-even point in units**, The Feather Dusters would deduct the _____ cost per unit from the price per unit and divide the fixed costs by this figure.
- (1) direct material
 - (2) indirect
 - (3) direct labour
 - (4) variable

SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS



Please refer to Appendix A for the suggested solutions to the self-assessment questions.

Learning Unit 5

The business plan

STUDY CHAPTER 5 IN THE PRESCRIBED BOOK

CONTENTS

- The business plan
 - The structure of a business plan
 - Guidelines for writing a business plan
 - Writing a business plan
-



LEARNING OBJECTIVES

When you have worked through learning unit 5, you should be able to

- *explain what a business plan is*
 - *explain the purpose of a business plan*
 - *explain the three principles that are applicable to a business plan*
 - *explain the benefits of drawing up a business plan*
 - *list the potential users of a business plan*
 - *explain the character of a business plan*
 - *explain the guidelines for writing a business plan*
 - *list the four possible structures of business plans*
 - *list and explain the main components of the general structure of a business plan*
 - *explain the marketing and financial plan in detail*
 - *list and explain the three most important financial statements that should be included in the financial plan*
 - *explain the break-even point*
-



KEY CONCEPTS

You will need to master the following key concepts to achieve the learning outcomes for this learning unit:

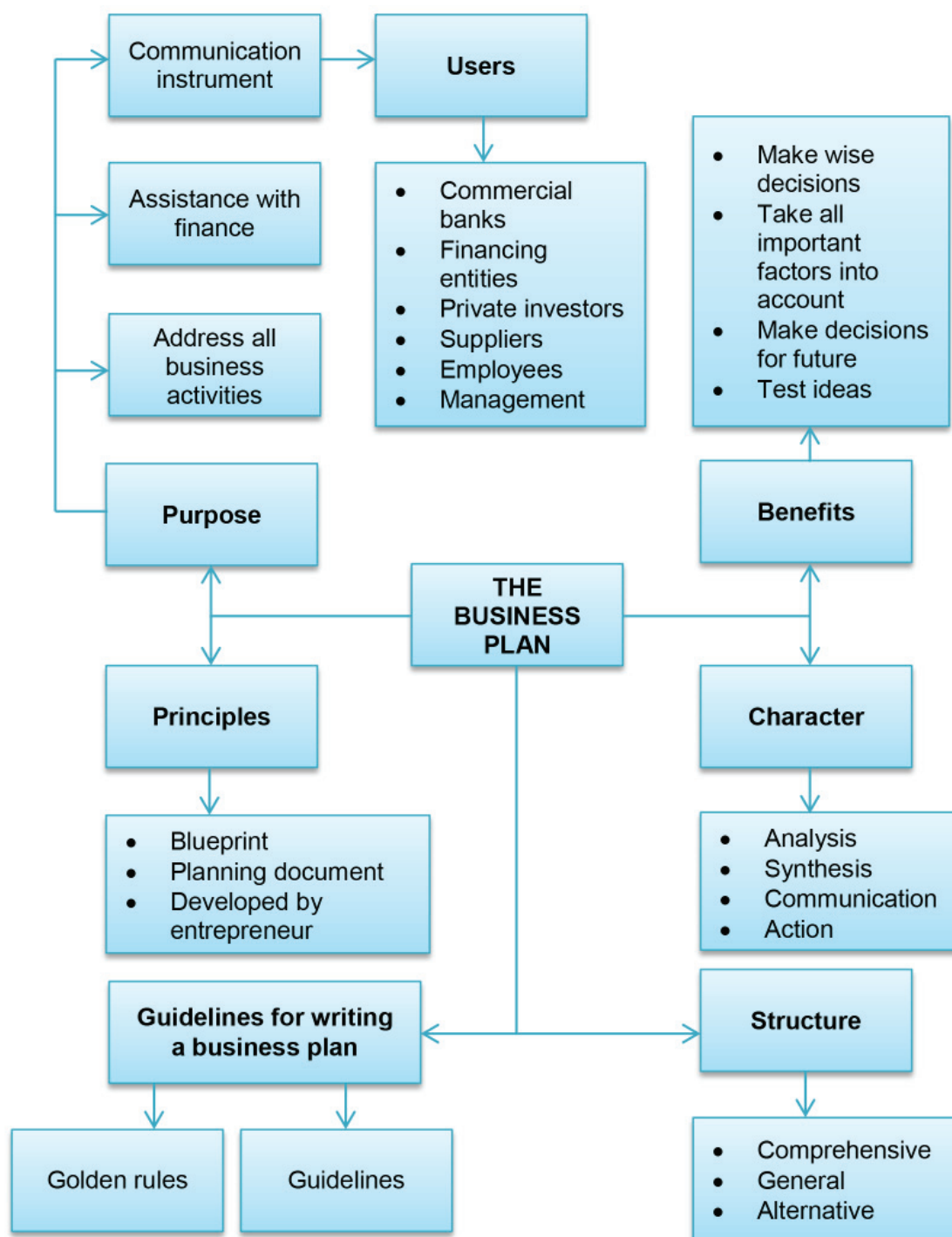
- business plan
- blueprint
- feasibility study
- viability study
- analysis
- synthesis
- comprehensive structure
- general structure

- balance sheet
- internal and external capital sources
- capital employed and employment of capital



A MIND MAP FOR LEARNING UNIT 5

The planning stage



OVERVIEW

In learning unit 5 you will learn that a business plan forms a pivotal part of the entrepreneurial process. The previous chapters dealt with all the components of the entrepreneurial process, which we are now going to combine into a business plan.

This learning unit explains the purpose and principles of a business plan, its potential users, as well as the character and structure of this important document. To help you write your own business plan, we will discuss the guidelines for writing a business plan, explain the components of a general business plan and provide important additional information on the financial plan.

5.1 THE BUSINESS PLAN

5.1.1 What is a business plan?



Activity 5.1

How would you describe a business plan?

.....



Definition of a business plan

A business plan is a detailed plan of action that sets out the nature and strategy of an enterprise.

This means that the business plan provides a description of the proposed enterprise. It provides information about the entrepreneurial team, the organisational structure, the form of enterprise, the products or services the enterprise wants to offer, the location of the enterprise, the target market, the capital contribution of the owners and the need for external capital, as well as a summary of the market and profit analysis. The entrepreneur uses the business plan to put all his or her ideas and findings on paper.

5.1.2 The purpose of a business plan

A business plan is compiled for the following reasons:

- to obtain financing
- to address all business activities
- to serve as a communication instrument to help the entrepreneur sell his or her management ability and business idea to everyone that has an interest in the business (the users of the business plan)

5.1.3 The principles of a business plan



Activity 5.2

List the principles of a business plan.

.....



The three principles of a business plan are as follows:

- *The business plan is a blueprint of the enterprise.*
- *The business plan is a flexible planning document.*
- *The business plan should be developed by the entrepreneur.*

The business plan is a blueprint of the enterprise

The business plan lists all the facets of the proposed enterprise. It explains exactly what the opportunity is and how the entrepreneur will exploit it. It serves as a road map that indicates the route the entrepreneur has to follow in the future.

The business plan is a flexible planning document

As we mentioned in learning unit 2, the business environment changes constantly. The business plan should be updated regularly to make provision for these changes.

The business plan should be developed by the entrepreneur

The only way to understand your enterprise properly is to develop the business plan yourself. External consultants can be used, but as the entrepreneur and owner of the enterprise, you should still be actively involved in the process. As the business plan also acts as a management instrument and guideline, it is vital for the entrepreneur to be personally involved in order to get an operational framework of the enterprise.



Activity 5.3

Is a business plan necessary only for a new enterprise or does an existing enterprise also need one?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

5.1.4 Potential users of a business plan

You know by now that the entrepreneur is the main user of his or her business plan. However, there are other people that would also have an interest in the business plan, for example:

- commercial banks, financing entities and private investors
- suppliers of resources
- employees and management

Commercial banks, financing entities and private investors

In order to make an informed decision on the viability of the proposed enterprise, financial institutions and other investors insist on a business plan. These institutions are also businesses and would not enter into a business transaction if the risk of losing their capital is too high.

Suppliers of resources

Before suppliers would allow an enterprise to buy resources on credit (grant suppliers credit), they will ensure that the enterprise can generate enough cash to pay them on a regular basis.

Employees and management

The business plan can be used to motivate employees. By knowing the objectives of the enterprise, employees will be more motivated to do their part in achieving them. Management, as we have already indicated in our previous discussions, uses the business plan as a management instrument and guideline.



Refer to Figure 5.2 in the prescribed textbook for an illustration of the potential users of a business plan.

5.1.5 Benefits of drawing up a business plan

- By identifying problems early on, the entrepreneur can make wise decisions and fewer mistakes.
- The entrepreneur is forced to take all the important factors into account.
- The entrepreneur can make decisions for the future.
- Drawing up a business plan provides the ideal opportunity for testing ideas.

5.1.6 The character of a business plan



Activity 5.4

What role does a business plan actually play in starting or growing an enterprise?

.....



A business plan is a tool or instrument for

- *analysis*
- *synthesis or integration*
- *communication*
- *action*

Analysis

The business plan contains information on each variable in the business. It serves as a checklist of all the sets of information needed.

Synthesis or integration

The information should be integrated to make business sense. The information in the business plan should correspond, for example, to the sales figures and the selling price in the marketing plan should correspond to the calculation of the income in the income statement.

Communication

It serves as a communication tool for all the users of the business plan. It contains information on the nature of the opportunity and how it will be exploited. For example, the bank can now see how you will pay back the loan by looking at your cash flow projections.

Action

The business plan should be implemented, otherwise it has no use. The business plan must therefore contain information on methods to implement the planned activities.



In your prescribed textbook, Figure 5.3 illustrates how the interaction between these characteristics contributes towards the success of an enterprise.

It is important to remember that the business plan is merely a planning instrument defining the entrepreneurial process and indicating how the entrepreneur will implement the process. Having the plan on paper does not mean success will inevitably follow. Business success and entrepreneurial performance are dependent on much more. The viability study is a decision-making platform for the entrepreneur and serves as a fundamental source of information in drafting an effective business plan. It is extremely important for the entrepreneur to realise that a business plan can be written only if a viable business opportunity exists in the market environment.

5.2 THE STRUCTURE OF A BUSINESS PLAN

As an entrepreneur, you must keep in mind that, although a business plan is such an important document, there is no single or standardised business plan structure. It must

correspond to the nature of your enterprise and must be adjusted according to the potential reader or user. However, you must always keep in mind that you, as the entrepreneur, are the first reader and user of your business plan.



We distinguish between the following three structures:

- *comprehensive structure*
- *general structure*
- *alternative structure*

The comprehensive structure

This is an all-inclusive plan that serves as the blueprint of the business. It includes all the planned activities, how they will be implemented and how they will be managed to exploit the opportunity.

The general structure

This is a more general approach and suitable for applying for finance and communicating with suppliers.

The alternative structure

This is also a general approach and suitable for applying for finance and communicating with suppliers.



Refer to figures 5.2, 5.3 and 5.4 in the prescribed textbook for examples of these three different structures.

5.3 GUIDELINES FOR WRITING A BUSINESS PLAN

5.3.1 Guidelines for writing a business plan

When writing the business plan, the entrepreneur should keep the following guidelines in mind:

- Keep the plan relatively short.
- Organise and package the plan appropriately.
- Orient the plan towards the future.
- Avoid exaggeration.
- Highlight critical risks.
- Give evidence of an effective entrepreneurial team.
- Do not overdiversify.
- Identify the target market.
- Write in the third person.
- Capture the reader's interest.



Study the explanations of these guidelines in the prescribed textbook.

5.3.2 Golden rules for writing a business plan

- A business plan should be based on facts and figures.
- It should provide a short, logical description of the enterprise.
- Proper headings should be used to indicate the topics under discussion.



Do you know:

The five common business plan mistakes that torpedo start-ups?

<http://www.entrepreneurmag.co.za/advice/business-plans/business-plan-advice/5-common-business-plan-mistakes-that-torpedo-start-ups/>

5.4 WRITING A BUSINESS PLAN

5.4.1 The general structure



You must be able to list and explain the main topics of a general business plan. Study the information below together with the information in section 5.9 in the prescribed textbook, as well as the example of a business plan (which is also based on the general structure) at the back of the prescribed textbook.

Important: We will NOT expect you to draw up a business plan.

5.4.1.1 Cover page

The cover page contains the details or general information of the enterprise, such as the name and address of the enterprise, the name and contact details of the entrepreneur and the date on which the business plan was compiled.

5.4.1.2 Confidentiality agreement

Since the business plan contains confidential information, the readers should sign a confidentiality agreement to safeguard its content.

5.4.1.3 Table of contents

A table of contents is an index of the business plan with page references which guide the reader on where to find certain information in the business plan. It should include all the

main headings and subheadings, accompanied by the relevant page numbers. It should be compiled after the business plan has been completed and inserted on a separate page.

5.4.1.4 Executive summary

This is a **short summary of the highlights** of the business plan, which provides the reader with an overview of the business plan. It should be written after the business plan has been completed and inserted on a separate page, after the table of contents and before the description of the enterprise. It should be written in paragraph format.

The executive summary should include information on the following aspects:

- name and location of the enterprise
- products or services that the entrepreneur offers
- need for the product or service
- target market
- expected sales figures
- amount of capital required (capital need)
- own capital invested by the entrepreneur
- collateral to cover debt and the expected profit

5.4.1.5 The description of the enterprise

(a) General description of the enterprise

This topic provides the reader with a short summary of the main activities of the enterprise.

(b) Information on the production branch (industry) and the branch of industry

This provides a short summary of the characteristics of the production branch and branch of industry under which the enterprise falls.

(c) The objectives of the enterprise

The entrepreneur must state the short-, medium- and long-term objectives of the enterprise.

(d) Uniqueness of the product or service

The entrepreneur must explain why his or her products or services are different from those of the main competitors.

(e) Suppliers

Indicate who and where the suppliers of resources are.

5.4.1.6 The marketing plan

(a) Market research and analysis of the total potential market

This entails a short summary of the findings of the market research and an explanation of the segmentation of the market according to the geographic, demographic, psychographic and behaviouristic segments.

(b) The target market

The entrepreneur must define the target market by explaining on which market segments he or she is going to concentrate.

(c) Size of the market and the market share

This entails figures about the total potential market and the actual percentage of the expected market share.

(d) Competition

This entails information on who the competitors are, where they are and what products or services they offer.

(e) The marketing strategy

The marketing strategy must be discussed in detail. The products or services must be explained and the selling prices must be indicated. The entrepreneur must explain how the products or services will reach the market (distribution). The entrepreneur must also indicate how he or she is going to make consumers aware of the products or services by explaining which elements of marketing communication he or she will use (advertising, sales promotions, personal sales or publicity).

5.4.1.7 Location

The entrepreneur must explain the advantages of the specific location. In other words, he or she must explain the reasons for deciding on the particular place of establishment by indicating which establishment factors were considered.

*5.4.1.8 Management***(a) Organisational structure**

The organisational structure serves as an illustration of the people (management and employees) that are involved in the enterprise and their responsibilities. The different management levels in the enterprise must also be indicated.



You will find an illustration of an organisational structure in the example of the business plan at the back of the prescribed textbook.

(b) Human resources plan

This entails an explanation of the recruitment and selection methods that will be followed, as well as a summary of compliance with labour legislation.

(c) Form of enterprise and ownership structure

The entrepreneur must indicate the form of enterprise (sole proprietorship, partnership, close corporation or private company), how many owners there are, as well as the percentage ownership of each owner according to their respective capital contributions.

5.4.1.9 The financial plan

(a) Financial forecasting (capital need)

The entrepreneur must indicate the capital need of the enterprise and how he or she intends to finance the capital need (the sources of funds).

(b) Income statement

A pro forma income statement must be compiled.

(c) Break-even analysis

A calculation of the break-even point must be done.

(d) Balance sheet

A balance sheet must be compiled.

(e) Cash budget

A cash budget must be compiled.

5.4.1.10 Critical risks

The entrepreneur must explain potential problems, obstacles and risks and indicate how he or she intends to deal with these issues.

5.4.1.11 Conclusion

This serves as a final motivation of why the enterprise would succeed and why it should be able to obtain a loan. The entrepreneur must highlight the need for the product or service and the expected sales figures once again, as well as the amount of own capital invested in the enterprise, the collateral that is offered and the expected net profit.

5.4.1.12 Addendum or appendix

This contains additional documentation on market research and product specifications, or any other additional information the entrepreneur wants to add.

5.4.2 Important notes on the financial plan

5.4.2.1 Sources of capital



We distinguish between internal and external sources of capital.

Internal sources

This refers to capital invested by the owners of the enterprise (own capital) which they obtained, for example, from savings, inheritances or pension payouts. Own capital can also be obtained from profits of the enterprise that are ploughed back into the business.

External sources

This refers to capital obtained from non-owners of the enterprise. Examples of external capital are loans, leases and creditors.

The importance of own capital

Financial institutions require owners to make a significant contribution to the financing of the enterprise. They regard this as a sound business principle if owners are prepared to take the risk of investing some of their own funds in the enterprise.

The assumption is that the entrepreneur will be more committed and motivated to achieve success. If the enterprise fails, it will not only be the financial institution that will lose money, but also the entrepreneur.

5.4.2.2 Collateral



When you apply for a loan, the financial institution will require some form of **collateral (security)** which they can repossess if you are unable to repay the loan.

Examples of collateral:

- property
- fixed assets
- policies
- investments (which are not linked to the enterprise)

It is important to realise that the capital that the entrepreneur has invested in the enterprise (own capital) cannot be regarded as collateral. If an enterprise becomes bankrupt, it loses all its capital, including the own capital contribution. Therefore, the own capital contribution cannot be repossessed by the financial institution to cover the debt of the enterprise.

5.4.2.3 Financial statements



The following financial statements must be included in the business plan:

- *income statement*
- *cash budget*
- *balance sheet*

Important: We will NOT expect you to prepare financial statements or to do any calculations. However, you must be able to define the statements and to explain the main entries and methods of calculations.

(a) The income statement



Definition of an income statement

An income statement is a summary of the **income and expenditure** of an enterprise **over a specific period**.



Activity 5.5

We briefly explained the income statement in learning unit 4.

Can you still remember the main entries?

.....



The main entries on an income statement are as follows:

Sales
– *Cost of sales*
= *Gross profit/income*
– *Expenses*
= *Net profit/income*

Explanation of the main entries on an income statement

Sales or turnover

To calculate the sales figure, we have to multiply the number of units sold by the selling price. In other words, this is the income we get from the sales of the products or services.

Cost of sales

Cost of sales is the money we have to spend to manufacture or buy the products. To calculate the cost of sales of a commercial enterprise, we have to add the purchases of stock to the opening stock and deduct the closing stock from this figure. To calculate the cost of sales of a manufacturing enterprise, we have to add all the direct manufacturing costs.

Gross profit

To calculate the gross profit, we have to deduct the cost of sales from the sales figure. In other words, this is the profit we get before any expenses have been paid.

Expenses

To calculate the expenses for a commercial enterprise, we have to add all the fixed costs. To calculate the expenses for a manufacturing enterprise, we have to add all the indirect costs (overheads).

Net profit

To calculate the net profit, we have to deduct the expenses from the gross profit.

Example of an income statement for a commercial enterprise

Income statement of The Seven Dwarfs (Pty) Ltd for the year ended 28 February 2013

	R	R
Sales		1 125 000
Cash sales	725 000	
Credit sales	400 000	
Less: Cost of sales		675 000
Opening stock: 01/03/2012	50 000	
Plus: Purchases	690 000	
Less: Closing stock: 28/02/2013	65 000	
Gross profit		450 000
Less: Expenses		247 600
Rent	30 000	
Telephone	6 600	
Water and electricity	9 000	
Salaries	120 000	
Marketing	34 000	
Interest	18 000	
Loan repayments	30 000	
Net profit		202 400
Less: Tax		60 720
Net profit after tax		141 680

Sales

Price per unit: R75

Units sold per month: 1 250

Units sold per year: 15 000

Example of an income statement for a manufacturing enterprise

Income statement of Humpty Dumpty (Pty) Ltd for the year ended 28 February 2013

	R	R
Sales		900 000
Cash sales	574 000	
Credit sales	326 000	
Less: Cost of sales		374 000
Direct material	180 000	
Direct labour	186 000	
Water and electricity (factory)	8 000	
Gross profit		526 000
Less: Expenses		209 600
Rent	48 000	
Telephone	5 600	
Water and electricity (office)	4 000	
Salaries	80 000	
Marketing	24 000	
Interest	18 000	
Loan repayments	30 000	
Net profit		316 400
Less: Tax		94 920
Net profit after tax		221 480

Sales

Price per unit: R60

Units sold per month: 1 250

Units sold per year: 15 000

(b) The cash budget



Definition of a cash budget

A cash budget is a formal plan for forecasting future receipts and payments of cash. It is designed to cover a period of one year and is divided into twelve monthly or four quarterly periods.



Activity 5.6

We briefly explained the cash budget in learning unit 4.

.....



Can you still remember the main entries?

The main entries on a cash budget are as follows:

Total cash receipts
 – *Total cash payments*
 = *Net cash balance*
 + *Opening cash balance*
 = *Closing cash balance*

Explanation of the main entries on a cash budget

Cash receipts

Cash receipts are all items that result in cash inflows in a given financial period. They consist of cash sales and cash received from debtors (people who owe the enterprise money).

Cash payments

These include all payments made in cash in a given financial period, such as all cash purchases, payments to creditors (people the enterprise owes money), rent or lease payments, loan repayments, interest, wages and salaries, and tax payments.

Net cash balance

To calculate the net cash balance, we have to deduct the total cash payments from the total cash receipts.

Opening cash balance

The opening cash balance of a period is the closing cash balance from the previous period.

Closing cash balance

To calculate the closing cash balance, we have to add the opening cash balance to the net cash balance.

Example of a cash budget prepared in quarterly periods and for the financial year
Cash budget of Humpty Dumpty (Pty) Ltd for the year ended 28 February 2013

	1st	2nd	3rd	4th	Year
	R	R	R	R	R
Cash receipts					
Cash sales	115 000	135 000	152 000	172 000	574 000
Cash from debtors	58 000	67 000	76 000	86 000	287 000
Total cash receipts	173 000	202 000	228 000	258 000	861 000
Less: Cash payments					
Direct material	45 000	43 816	44 259	46 925	180 000
Direct labour	31 500	41 500	51 500	61 500	186 000
Rent	12 000	12 000	12 000	12 000	48 000
Telephone	1 400	1 400	1 400	1 400	5 600
Water and electricity	3 000	3 000	3 000	3 000	12 000
Salaries	20 000	20 000	20 000	20 000	80 000
Marketing	5 500	6 000	6 000	6 500	24 000
Interest	4 500	4 500	4 500	4 500	18 000
Tax	23 730	23 730	23 730	23 730	94 920
Loan repayment	7 500	7 500	7 500	7 500	30 000
Total cash payments	154 130	163 446	173 889	187 055	678 520
Net cash balance (surplus/deficit)	18 870	38 554	54 111	70 945	182 480
Opening cash balance	(35 754)	(16 884)	21 670	75 781	(35 754)
Closing cash balance	(16 848)	21 670	75 781	146 726	146 726

(c) The balance sheet



Definition of a balance sheet

*A balance sheet is a summary of the financial position, or a summary of the **assets and liabilities**, of the enterprise at a particular time or date.*

*A balance sheet reflects **the capital employed and the employment of capital**. In other words, it shows how the **available funds** (capital employed) were used to acquire the **necessary assets** (employment of capital). **The capital employed and the employment of capital should balance at all times.***

Explanation of the main entries on a balance sheet

Capital employed

- own capital (equity)
- long-term liabilities such as long-term loans and mortgage bonds
- current liabilities such as creditors, short-term loans and bank overdrafts

Employment of capital

- fixed assets such as land, buildings, machinery, equipment and vehicles
- current assets such as stock, cash and debtors

Example of a balance sheet

Balance sheet of Humpty Dumpty (Pty) Ltd as at 28 February 2013

	R	R
Capital employed		
Own capital		663 980
Reserves	442 500	
Accumulated profits	221 480	
Long-term liabilities		140 000
Long-term loans	140 000	
Current liabilities		67 805
Creditors	57 805	
Short-term loans	10 000	
Total liabilities		871 785

Employment of capital	R	R
Fixed assets		369 384
Vehicles	120 000	
Machinery	189 130	
Equipment	60 254	
Current assets		502 401
Stock	29 675	
Cash	146 726	
Debtors	326 000	
Total assets		871 785

5.4.2.4 Financial analysis: the break-even point



Activity 5.7

We explained the break-even point in learning unit 4.

Can you still remember the definition and the formulae?

.....



Definition of a break-even point

A break-even point is the number of units that must be sold for the income and expenditure to be equal. In other words, this is the point where all the costs and expenditure are covered. At this point the net profit will be equal to R0, which means neither a profit nor a loss is shown.

Example of a break-even point calculated in units

Break-even point of Humpty Dumpty (Pty) Ltd for the year ended 28 February 2013

Step 1: Calculate the variable costs.

	R	R
Total variable costs		374 000
Direct material	180 000	
Direct labour	186 000	
Water and electricity (factory)	8 000	

Step 2: Calculate the fixed costs.

	R	R
Total fixed costs		304 520
Rent	48 000	
Telephone	5 600	
Water and electricity (office)	4 000	
Salaries	80 000	
Marketing	24 000	
Interest	18 000	
Loan repayments	30 000	
Tax	94 920	

Step 3: Calculate the break-even point in units.

Price per unit: R60

Units sold per month: 1 250

Units sold per year: 15 000

Formula

$$\begin{aligned}
 & \text{Units} = \frac{\text{Fixed costs}}{\text{Price per unit} - \text{Variable cost per unit}} \\
 & = \frac{304\,520}{\text{R}60 - 15\,000} \\
 & = 8\,683 \text{ units per year}
 \end{aligned}$$



You have now reached the end of learning unit 5.

SUMMARY

We trust that this learning unit has provided you with the knowledge to draw up your own business plan. Remember that you, as the entrepreneur, should either draw up the business plan yourself, or be actively involved in the process. This is the only way to understand your enterprise, since the business plan acts as a blueprint of the enterprise.

We have now reached the end of the second stage (the planning stage) in the creation of an enterprise. We have made all the decisions concerning our enterprise and concluded our planning. We now have to move on to the third and final stage, the implementation stage, which we will discuss in learning unit 6.



SELF-ASSESSMENT

To test and assess your knowledge of this learning unit, you can now do the following activities:

- (i) Complete the self-assessment questions on learning unit 5 below. Remember: The only way you can test your knowledge is by answering the questions without looking at the solutions contained in Appendix A.
- (ii) Do the self-assessment questions in the prescribed textbook at the end of chapter 5.

Read the case study below and answer all the questions that follow.

Case study: Tony's Garden Services

After working for many years as a horticulturist at a big nursery in Roodepoort, Tony Stevens decided to start an enterprise that provides garden services. Owing to the low start-up costs of such a business, there were quite a lot of competitors offering garden services in Roodepoort. Tony realised that, unless he could offer more specialised services,

he would not survive in this competitive market. He considered providing three services – a basic garden service, tree felling and pruning of trees and shrubs, as well as landscaping.

Tony decided to first conduct market research to determine the need for more specialised garden services. The outcome of the market research revealed the following:

- The demand for garden services will never decline, as people prefer to rather use a formal service than hiring someone from the street to work in their gardens.
- Since Johannesburg is known as the city that has more trees than inhabitants, people usually replace a tree once it has been cut down. This means that there will be a constant demand for the pruning and felling of trees.
- There were quite a lot of new developments in the area that would need his expertise in landscaping.

Since Tony's two sons, Paul and John, both completed a course in horticulture at Unisa, he decided to include them in the enterprise. Paul would be in charge of running the garden services, John would be responsible for the tree felling and pruning of trees and shrubs, while Tony would concentrate on landscaping. Tony's wife, Sharon, agreed to handle the administration and finances of the business. They registered the enterprise, Tony's Garden Services, as a private company with Tony as the director. Tony invested R70 000 of his pension money in the business and Paul, John and Sharon each contributed R10 000 of their savings. They applied for a loan of R300 000 to finance the purchase of four second-hand bakkies, equipment such as lawnmowers and edge trimmers, garden tools and chainsaws, as well as office equipment.

As this type of service is labour intensive, the enterprise had to employ quite a lot of new employees. Sharon appointed Tarryn to help her with the administrative work. Paul decided to appoint two supervisors and allocated a team of four workers to each supervisor. John decided that he was going to start with only one team and appointed six experienced tree fellers to help him. As tree felling is sometimes executed under extremely dangerous conditions, they had to take out insurance for their employees before they could start to work.

To provide a service on an order basis requires extremely good planning, as well as excellent administration. Sharon has to take all the orders and plan the daily activities of the teams very carefully. Every morning the workers report to the office, from where they are transported to the different gardens, together with the necessary equipment. Sharon has to calculate the time that is spent on transporting the teams from one garden to another and determine the shortest route to follow in order to save time and transport costs.

Today Tony's Garden Services is one of the biggest and best-known garden services on the West Rand. The owners of Tony's Garden Services believe that a healthy cash flow forms the cornerstone of any enterprise and all their operating expenses are financed by means of cash. They advertise in the Yellow Pages, occasionally in the local newspaper, and their name and contact details are on their vehicles. Tony, however, believes that satisfied clients telling others about their service offer the best exposure an enterprise can get. For this reason, the enterprise is always available, even over weekends. This means that they sometimes have to work seven days a week. Another reason for their success is that they

are constantly on the look-out for more efficient ways of providing their services. After dumping the garden refuse and trees at a dumping site for quite a while, the owners of Tony's Garden Services decided to buy the necessary equipment and a piece of land in Kya Sands where the garden refuse is now being used to make compost, which they then use to fertilise the clients' gardens.

Multiple-choice questions

- (1) When the owners of Tony's Garden Services compiled their business plan, they had to keep in mind that the **principles of a business plan** state that it should _____ .

- (a) serve as a blueprint of the enterprise
- (b) make provision for future changes in the business environment
- (c) be compiled by external consultants
- (d) include all the facets of the proposed enterprise

Choose the correct option:

- (1) a, b, c, d
 - (2) a, c, d
 - (3) a, b, c
 - (4) a, b, d
- (2) The owners of Tony's Garden Services had to keep in mind that the _____ of a business plan means that the business plan is useless **unless it is implemented**.
- (1) analysis
 - (2) integration
 - (3) communication
 - (4) action
- (3) The **garden workers are transported to the different gardens**, which indicate that Tony's Garden Services uses _____ distribution channel to transfer the garden services to their clients.
- (1) a direct
 - (2) no
 - (3) more than one
 - (4) an indirect
- (4) Tony **believed that satisfied clients telling others about their services** offer the best exposure that an enterprise can get. This is an example of _____ as an element of marketing communication.
- (1) advertising
 - (2) sales promotions
 - (3) personal sales
 - (4) publicity

- (5) As this type of service is labour intensive, the enterprise had to employ quite a lot of new employees. The owners of Tony's Garden Services would have **addressed the human resources plan** when they wrote the _____ .
- (1) description of the enterprise
 - (2) marketing plan
 - (3) management plan
 - (4) financial plan
- (6) Tony invested R70 000 of his pension money and Paul, John and Sharon each contributed R10 000 of their savings. According to their capital contribution, **Paul, John and Sharon each owns** _____ of Tony's Garden Services.
- (1) 100%
 - (2) 70%
 - (3) 30%
 - (4) 10%
- (7) Tony's Garden Services had to apply for a loan of R300 000. The owners could have **offered their home as collateral for this loan**, because it forms part of their _____ .
- (1) fixed assets
 - (2) current assets
 - (3) long-term liabilities
 - (4) current liabilities
- (8) To calculate their **net profit** in the income statement, the owners of Tony's Garden Services would _____ the gross profit.
- (1) deduct the expenses from
 - (2) add the cost of sales to
 - (3) deduct the cost of sales from
 - (4) add the expenses to
- (9) Tony's Garden Services' cash budget would play a very important role since all their operating expenses are financed by means of cash. To **calculate the closing cash balance** in the cash budget, the owners would _____ the net cash balance.
- (1) deduct the opening cash balance from
 - (2) add the opening cash balance to
 - (3) add the total cash receipts to
 - (4) deduct the total cash payments from
- (10) When the owners of Tony's Garden Services prepare their balance sheet, they will indicate the _____ as **capital employed**.
- (a) loan of R300 000
 - (b) four second-hand bakkies, lawnmowers and edge trimmers
 - (c) land in Kya Sands
 - (d) own capital of R100 000

Choose the correct option:

- (1) a, c
- (2) b, d
- (3) a, d
- (4) b, c



SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS

Please refer to Appendix A for the suggested solutions to the self-assessment questions.

Learning Unit 6

Setting up a business

STUDY CHAPTER 6 IN THE PRESCRIBED BOOK

CONTENTS

- The forms of enterprise
 - The duties and legal requirements
 - Labour legislation
 - Establishment factors
 - Setting-up factors related to the functions of the enterprise
-



LEARNING OBJECTIVES

When you have worked through learning unit 6, you should be able to

- *list and discuss the different forms of enterprise*
 - *list and explain the legal requirements that all enterprises must meet*
 - *explain the different employment contracts*
 - *list the different labour laws and give a brief discussion of the purpose or aim of each of them*
 - *list and explain the establishment factors applicable to commercial, service and manufacturing enterprises*
 - *define the marketing function and explain the marketing strategy*
 - *define the public relations function and explain how the entrepreneur can use this function to promote the enterprise*
 - *define the information management function and explain how administration and record keeping should be developed*
 - *define the financial function and explain the financing of different capital needs*
 - *define the human resources function and explain the steps that the entrepreneur has to take to plan staff appointments*
 - *define the purchasing function and explain the tasks of this function*
 - *define the operations function and explain the transformation process*
 - *define the general management function and explain the four elements of general management*
-



KEY CONCEPTS

You will need to master the following key concepts to achieve the learning outcomes for this learning unit:

- legal personality
- limited and unlimited liability
- limited and unlimited continuity
- Registrar of Companies
- full legal capacity
- VAT
- Unemployment Insurance Fund
- Compensation Commissioner
- service levies
- turnover levies
- employment contracts



A MIND MAP FOR LEARNING UNIT 6



OVERVIEW

So far in this module, you, as the potential entrepreneur, have learned several important aspects, such as the following:

- how to analyse yourself critically by determining your own strengths and weaknesses
- how to turn a business idea into an opportunity for a new business
- how to test the feasibility and viability of the business idea
- how to draw up a business plan

These activities all cover the idea and planning stages in creating an enterprise. When we discussed the character of a business plan in learning unit 5, we established that a business plan is useless unless it is implemented. We have now reached the implementation stage, the final stage in the creation of an enterprise. This is the stage where the real action begins – where we have to put the idea into practice.

In learning unit 6 we will discuss the practical factors to which the entrepreneur must pay attention in setting up a business. We are going to explain the different forms of enterprise that you can choose from and we will discuss the duties and legal requirements you have to comply with before you can start the enterprise. We are also going to discuss the labour legislation briefly, as well as the establishment factors that you have to consider before you decide on the location of your enterprise. Finally, we are going to explain how the eight functions of the enterprise should be implemented so that your enterprise can function as a unit.

6.1 THE FORMS OF ENTERPRISE

6.1.1 Different forms of enterprise (business forms or business structures)

Choosing the right form of enterprise can be quite complicated. The entrepreneur has to consider important factors such as the size of the enterprise, the extent of the capital need, legal personality, legal requirements and the procedures that must be followed to register the form of enterprise.

Although there are various forms of enterprise, we are going to concentrate only on those that are applicable to small businesses.



Forms of enterprise that is applicable to small businesses:

- *sole proprietorship*
- *partnership*
- *close corporation*
- *private company*

Important: You must study the information on forms of enterprise in section 6.2 together with the information on business structures in section 4.4.1 in the prescribed textbook. Also note that the discussion on the procedures for registering or setting up each form of enterprise follows after the discussion on labour legislation in the prescribed textbook, section 6.5.

6.1.1.1 Sole proprietorship

A sole proprietorship is usually a small enterprise which is owned by **one owner**. The name of the enterprise may be **any legal name** and this form of enterprise is easy and simple to establish. The owner is responsible for supplying the capital and managing the enterprise.

6.1.1.2 Partnership

A partnership is formed by **two to twenty partners**. The name of the enterprise **must end with "& Co"**. A partnership agreement is formed by means of a written or verbal agreement between the partners and a partnership is quite simple to establish. The partners are responsible for supplying the capital and managing the enterprise.

6.1.1.3 Close corporation

From 1 May 2011 no **new close corporations** can be formed, but existing ones can continue to exist. A close corporation has **one to ten members**. The name of the enterprise **must end with "CC"**. The members are responsible for supplying the capital and managing the enterprise.

6.1.1.4 The private company

A private company consists of **one to fifty shareholders**. The name of the enterprise **must end with "(Pty) Ltd"**. It is much more complicated to establish than a partnership and prescribed formal documents have to be submitted to the Registrar of Companies. Capital is obtained by making shares available to the shareholders. A private company is managed **by at least one director**.

6.1.2 Characteristics of the forms of enterprise



Carefully study Table 6.1 in the prescribed textbook that indicates the characteristics, advantages and disadvantages of each form of enterprise.

6.1.3 Factors that influence the choice of a form of enterprise



Activity 6.1

Using Table 6.1 in the prescribed textbook that indicates the characteristics, identify the factors that influence the choice of a form of enterprise.

.....



When choosing a form of enterprise, the entrepreneur has to keep the following factors in mind:

- *the nature of the product or service*
- *legal personality*
- *the liability of the owners*
- *the continuity of the enterprise*
- *tax obligations*
- *the specific legal requirements*
- *the need to involve third parties financially*

6.1.3.1 The nature of the product or service

The nature of the product or service will determine the size of the enterprise. The bigger the enterprise, the more formal the form of enterprise has to be.

6.1.3.2 Legal personality

Legal personality means that the enterprise can exist independently of its owners, which means the enterprise can act in its own name. Enterprises with legal personality, such as close corporations and private companies, can therefore conclude contracts, sue and apply for finance in the name of the enterprise. Enterprises without legal personality, such as sole proprietorships and partnerships, do not exist independently of their owners and all transactions are made in the name of the owners. Legal personality provides unlimited continuity to the enterprise and limited liability to the owners.

6.1.3.3 The liability of the owners

Liability refers to the degree to which the owners are responsible for the debts of the enterprise. If an enterprise has legal personality, the assets and liabilities of the enterprise are completely separated from those of the owners. The owners have limited liability for the debts incurred by the enterprise. This means they can lose only the money they have invested in the enterprise, in other words, their personal assets are separated from those of the enterprise. If an enterprise does not have legal personality, the owners have unlimited liability for the debts of the enterprise. This means they can lose their private assets if the enterprise becomes bankrupt, because there is no distinction between their private assets and those of the enterprise.

6.1.3.4 The continuity of the enterprise

If an enterprise has legal personality, it does not cease to exist if an owner dies, withdraws or when a new owner joins the enterprise. It has unlimited continuity or an indefinite lifespan. If an enterprise does not have legal personality, it has limited continuity, which means that the enterprise ceases to exist if an owner dies, withdraws or when a new owner joins the enterprise.

6.1.3.5 Tax obligations

The owner of a sole proprietorship and the partners of a partnership pay tax in their personal capacity. Since close corporations and private companies have legal personality, the enterprises are taxed according to a fixed rate.

6.1.3.6 The specific legal requirements

This refers to the legal requirements applicable to the establishment of the enterprise, as well as the provision, auditing and publishing of financial statements. Certain types of business also have to renew their licences annually.

6.1.3.7 The need to involve third parties financially

The capital need and the size of the enterprise will determine how many owners are needed. For example, a private company can issue shares to 50 shareholders and therefore can accumulate much more capital than a partnership with 20 partners or a sole proprietorship with one owner.

In addition to the above factors, the entrepreneur must also keep **the name of the enterprise, the number of members and the distribution of profit** in mind.

6.1.4 Procedures for registering (setting up) the forms of enterprise

6.1.4.1 Sole proprietorship

Setting up a sole proprietorship entails only a few legal requirements, such as obtaining a trading name and a trading licence.

6.1.4.2 Partnership

Establishment procedures of a partnership entail only a few legal requirements, such as obtaining a trading licence. A partnership agreement, in the form of a written or verbal agreement, must be formed.

6.1.4.3 Close corporation

Since no new close corporations are allowed, we are not going to discuss the establishment procedures.

6.1.4.4 Private company

Setting up a private company entails the following:

- (1) Reserve a name for the company.
- (2) A Memorandum of Association and Statutes/Articles must be drawn up.

- (3) Various documents and information must be submitted to the Registrar of Companies, such as information on the name and location of the company, copies of the Memorandum of Association and the Statutes and written proof that a chartered accountant will audit the annual financial statements.
- (4) The Registrar of Companies will issue a Certificate of Incorporation, which indicates that the company has received a legal personality.

6.2 THE DUTIES AND LEGAL REQUIREMENTS



Activity 6.2

Can you simply start your enterprise after choosing a suitable form of enterprise?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

The duties and legal requirements that apply to all forms of enterprise include the following:

- full legal capacity
- the type of economic activity
- naming the business
- registration of patents, trademarks and designs
- testing of products
- licensing
- registration with the South African Revenue Service (SARS) (previously called the Receiver of Revenue) as an employer, a taxpayer and for VAT
- registration with the Unemployment Insurance Fund
- registration with the Compensation Commissioner (previously called the Workmen's Compensation Commissioner)
- registration with local authorities
- registration with the Department of Trade and Industry
- general industrial and commercial legislation



Study the above duties and legal requirements in section 6.3 in the prescribed textbook.

6.3 LABOUR LEGISLATION



Activity 6.3

What is the purpose of labour legislation?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

6.3.1 Employment contracts

It is important to understand that an employee makes himself or herself available to an employer in an employment contract. This relationship between the employer and the employee comprises certain rights and obligations that have to be mutually agreed on. For example, in the contract the employer describes the duties to be performed by the employee and the employee agrees on a wage or salary. The contract also defines whether employment is for a fixed or an indefinite period.



Study the following forms of employment contracts in section 6.4.1 in the prescribed textbook:

- *written contracts*
- *verbal contracts*
- *tacit contracts*



Activity 6.4

Which type of contract would you use when you appoint your employees?

.....

6.3.2 Acts



You must study the following Acts in section 6.4.2 in the prescribed textbook:

- *Labour Relations Act*
- *Basic Conditions of Employment Act*
- *Employment Equity Act*
- *Skills Development Act*
- *Broad-Based Black Economic Empowerment Act*

Labour Relations Act

You must study the aim and the objectives of this Act.

Basic Conditions of Employment Act

You must study the purpose and the provisions of this Act.

Employment Equity Act, Skills Development Act and Broad-Based Black Economic Empowerment Act

You must study the purpose or aims of these Acts.

Important: You do NOT have to study the sections in which the information appears.

6.4 ESTABLISHMENT FACTORS

There are many factors that play a role in identifying a suitable location or place of establishment for the enterprise. The location of your enterprise will have a huge influence on your sales and your ability to compete with other enterprises.



Activity 6.5

Would the type of enterprise (manufacturing, commercial or service enterprise) influence the factors that you have to consider when you have to decide on a place of establishment for your enterprise?

.....



Contact your e-tutor via myUnisa for the answer to this activity. You will need it for answering your assignments and for exam preparation.

6.4.1 Establishment factors for commercial and service enterprises

The market

The enterprise must be visible and near the target market.

Accessibility

It must be easy for consumers to reach the enterprise.

Cumulative attraction

Other shops in the area, especially shopping centres, attract consumers.

Growth potential

The growth potential of the area where the enterprise plans to establish is important. For example, a newly developed residential area implies that further development can be expected.

Suitability of premises

Factors such as sufficient parking space, the availability of water, electricity and public transport, and the cost of rent must be considered.

Limited risk of competition

You have to determine how many competitors there are and how likely it is that other competitors will establish in the same area.

Interception of consumers

Consumers must be intercepted on their way to their traditional place of purchase.

6.4.2 Establishment factors for manufacturing enterprises

Raw materials

The enterprise must be near the source of raw materials to save transport costs.

Labour

The availability, skills and cost of labour are important.

Transport

Infrastructure, reliability and cost of transport must be considered, such as the availability of roads, rail, airports and harbours.

Energy and water

Electricity is needed to use machinery in the production process and water in the right quantities is also important.

Climate

The influence that the climate exerts depends on the type of product. For example, agricultural products are dependent on the climate of a certain region.

Nature of end product

If the end product is made up of different kinds of raw materials from different outlet points, it may be more beneficial to establish near the market or at a central point.

Incentives

Government or local authorities can offer incentives to persuade enterprises to establish in certain regions or in industrial areas.

6.5 SETTING-UP FACTORS RELATED TO THE FUNCTIONS OF THE ENTERPRISE



Activity 6.6

In learning unit 2 we briefly discussed the eight functions of the enterprise. Can you still remember them?

.....

In this section we are going to explain the functions in more detail and we are going to concentrate on how the functions must be implemented during the establishment of the enterprise. Although we are going to discuss these functions separately, there is a degree of overlap between them. It is extremely important to remember that all these functions occur in every enterprise, regardless of the size of the enterprise. There should be constant interaction between these functions to enable the enterprise to function as a unit or a system.

6.5.1 The marketing function



Definition

The marketing function is responsible for the transfer of the products from the manufacturer to the consumer and includes the activities that make this transfer possible. These activities include conducting market research and market segmentation, deciding on the target market and the marketing strategy, and compiling a marketing plan.

6.5.1.1 Initial marketing

Before you can sell your products or services, you must plan a marketing campaign by compiling a marketing plan which is based on your specific target market. The core of this marketing plan will consist of your marketing strategy – the products or services that you are going to sell, your selling price and the distribution channel and form of marketing communication that you are going to use. You must also decide on the name, logo and motto of your enterprise.



Activity 6.7

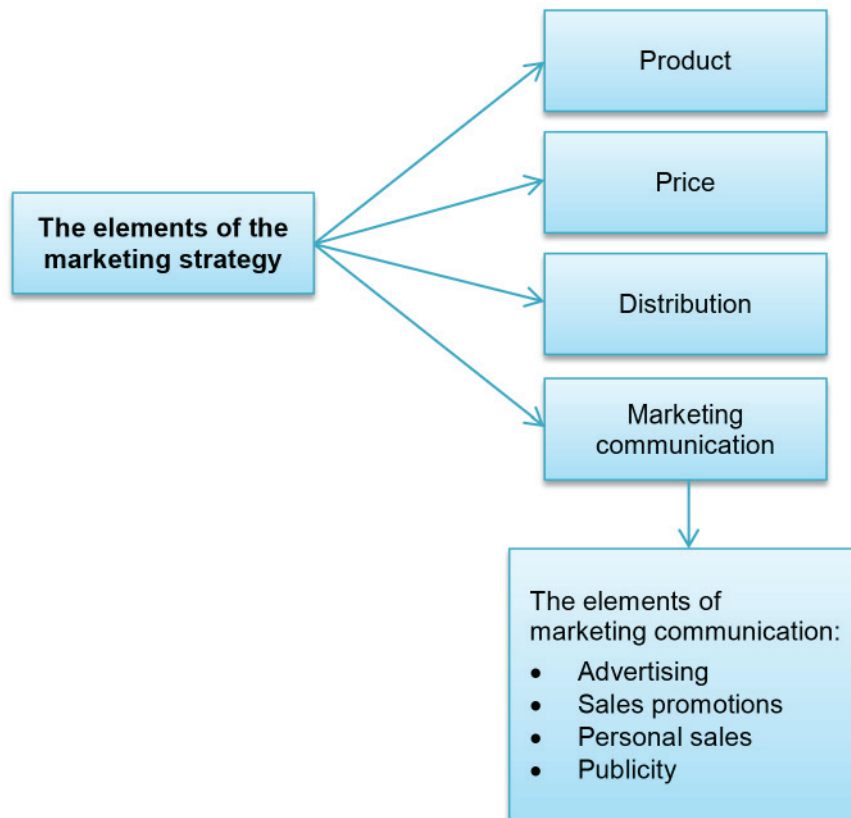
In learning unit 2 we discussed the rights of consumers. Can you still remember them?

.....



The rights of consumers are protected by legislation. Read the provisions of the Consumer Protection Act in section 6.7.1 in the prescribed textbook.

6.5.1.2 The marketing strategy



(a) The product

This represents the products or services that you are going to offer and includes the colour, size, packaging, quality, guarantees and after-sales service of the products or services.

(b) The price

This is your selling price which you have determined when you have calculated the profit potential of your idea. As we indicated in learning unit 4, the selling price should be profitable, affordable and competitive.

(c) Distribution

Distribution entails the physical transfer of the products or services to consumers, or the way in which your products or services will reach the market. If you sell the products or services directly to consumers, you will use a direct distribution channel. If you use wholesalers, retailers or agents to sell your products to consumers, you will use an indirect distribution channel.

(d) Marketing communication

This entails the methods that you are going to use to make consumers aware of your products or services. It is extremely important to keep the type of product or service, the size of the enterprise and the location of the target market in mind when you decide which method or element of marketing communication you are going to use. Marketing communication consists of four elements, namely advertising, sales promotions, personal sales and publicity.

Advertising

This includes the use of pamphlets, radio and newspaper advertisements, as well as advertisements on billboards.



Check out:

The top 10 South African TV adverts that left you with an indelible experience:
<http://buzzsouthafrica.com/top-10-south-african-tv-adverts-that-left-you-with-an-indelible-experience/>

Sales promotions

These include special offers, discounts, gifts and trade-ins.

Personal sales

These include the use of sales staff, for example telesales, door-to-door sales and catalogues.

Publicity

This includes sponsorships, donations and articles in newspapers or magazines.

6.5.2 The public relations function



Definition

The public relations or external relations function is responsible for promoting the image of the enterprise to ensure positive support from all the interest groups of the enterprise. It strives to create goodwill, cooperation, mutual understanding and acceptance from all the relevant interest groups, such as the consumers, community, capital providers, employees and authorities.

6.5.2.1 The difference between marketing and public relations

Although the public relations and marketing functions work closely together, they are not the same. The marketing function sells the products or services to consumers to make a profit for the enterprise. The public relations function sells the enterprise (making it known) to the public (interest groups) to promote the image of the enterprise.

6.5.2.2 The use of public relations

As an entrepreneur, you can use public relations successfully to make the public aware of your new enterprise.

The following methods (or hints) can be used to promote public relations:

- Use your network of friends and acquaintances to make your business known or join organisations and associations such as the local Chamber of Commerce. This is known as networking.
- Invite journalists from the local newspaper to the opening of your business.
- Write an article yourself and send photographs with it for publication.
- Ask for an article to be written about your enterprise when you place advertisements.
- Testimonials from satisfied customers are also an excellent form of public relations.



Read Example 6.8 on the successful use of public relations in the prescribed textbook.



Did you know:

Public relations (PR) do not always go well?

Here's what we can learn from the PR disasters of 2015:

<http://www.mediaupdate.co.za/publicity/83222/heres-what-we-can-learn-from-the-pr-disasters-of-2015>

6.5.3 The information management function



Definition

The information management function (or the information and record systems function) is responsible for collecting, processing, storing and distributing information, as well as developing record-keeping and filing systems. This function enables management to make informed decisions.

The following record-keeping systems must be developed for the new enterprise:

- a system for keeping information on customers
- an accounting system that is simple and effective
- a stock control system
- a system for the control of cash
- a system for keeping records of marketing, enquiries and sales
- a system for keeping record of turnover and profit for tax purposes and levies to local authorities



Read the discussion in section 6.7.3 in the prescribed textbook on how the kind of information you must record will determine which filing system you must use.

6.5.4 The financial function



Definition

The financial function is responsible for determining the capital need of the enterprise and for deciding how the capital need will be financed. This includes decisions on the effective application of funds and the best possible use of the sources of finance, as well as the development of a basic accounting system.

6.5.4.1 Financing your enterprise

The capital need of your enterprise can be financed by means of internal and external capital sources. Although we have already discussed the importance of own capital in learning unit 5, the importance of investing your own funds in the enterprise cannot be overemphasised. Financing institutions generally require a certain amount of own capital to show that you, as the entrepreneur, are committed to the enterprise.

6.5.4.2 Financing of different financial requirements

As an entrepreneur, it is important to know how to obtain the right finance for your different capital requirements.

- To buy property, you will need a large amount and have to apply for long-term financing.
- To buy expensive machinery and equipment, you have to apply for medium-term financing.
- To buy computer equipment or raw materials, you have to apply for short-term financing.

6.5.4.3 Managing your finances



Study the information on managing your finances in section 6.7.4 in the prescribed textbook.

6.5.5 The human resources function



Definition

The human resources function is responsible for the effective use of a competent, motivated labour force. The activities of this function include compiling job descriptions and job specifications, as well as the recruitment, selection, employment, induction, training and development of personnel.

Steps to plan your staff requirements and to ensure the right appointments:

- **Draw up a list of all the tasks** that must be performed in the enterprise.
- **Compile a job description** by grouping the tasks so that tasks that can be performed by a specific person can be combined.
- **Compile a job specification** by determining what qualifications and skills the person must have to perform the tasks.
- **Recruit the right people.** Since you do not have any employees yet, you will have to use external recruitment sources, such as placing advertisements, using recruitment agencies or approaching training institutions.
- From the applicants, you then have to **select the best candidate.**
- An **employment contract** must be signed and a written job description must be given to the new employee.
- The **training and development needs** of the employees must be addressed regularly.



Read the discussion on appointing family members or friends and the complications arising from this in section 6.7.5 in the prescribed textbook.

6.5.6 The purchasing function



Definition

The purchasing function is responsible for ensuring that production means of the right quality are supplied to the enterprise in the right quantities, at the right time, to the right place, from the right supplier, at the right price.

In learning unit 4 we explained how to calculate the cost per unit for the different types of enterprise and how the cost per unit influences the selling price and profit of the enterprise. The price of production means, such as raw materials or stock, plays an extremely important role in the profitability of the enterprise. Therefore, it is of the utmost importance that from the start, you find the right supplier that can deliver the right quality production means at the right price.

To start the purchasing function:

- Find suitable suppliers of raw materials or stock.
- Negotiate with suppliers for better prices for cash payments.
- Compare suppliers in terms of prices, quality and the services they provide.
- Find alternative suppliers so that you are not dependent on one supplier.
- Maintain good relations with suppliers.
- Maintain good relations with other functions of the enterprise.
- Exercise effective stock control.
- Exercise quality control.

6.5.7 The operations function

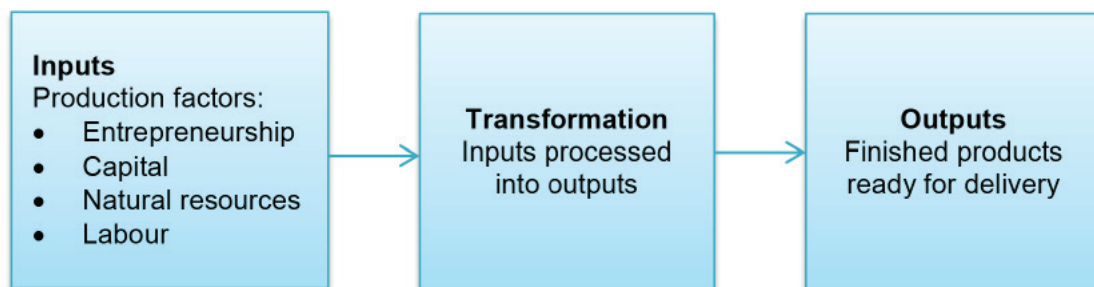


Definition

The operations function is responsible for transforming inputs (raw materials) into outputs (final products) by using the four factors of production to manufacture products or to provide services.

It is important to remember that all types of enterprise (manufacturing, commercial and service) have operations functions. In a manufacturing enterprise, the operations function is the place where the products are manufactured. Commercial and service enterprises also need inputs that must undergo some kind of transformation in order to deliver an output.

The transformation process for the manufacturing of a product can be illustrated as follows:



An example of the transformation process for the manufacturing of wooden furniture:



Read the information that should be considered by the operations function of a manufacturing enterprise in section 6.7.7 in the prescribed textbook.

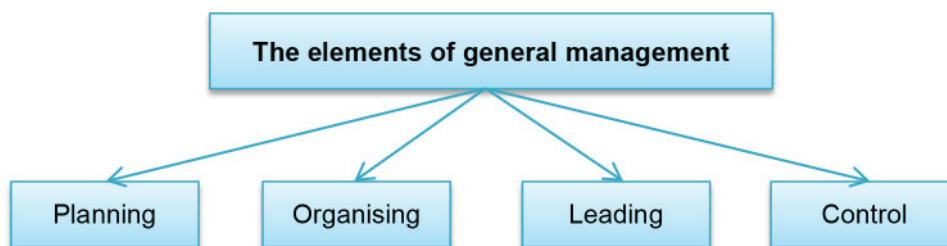
6.5.8 The general management function



Definition

The general management function is responsible for the overall management of the enterprise. This includes all the activities (planning, organising, leading and control) that are performed in the enterprise to enable the enterprise to achieve its goals. The general management function is found in all the other functions of the enterprise.

Below is an illustration of the general management function:



As an entrepreneur, you will act as the manager of your enterprise. You will thus be responsible for the planning, organising, leading and control of all the activities of the enterprise.

Planning

Planning involves formulating objectives for the enterprise and working out a systematic plan to achieve these objectives. Management should determine in advance what the enterprise wants to achieve and how these objectives can be attained.



Check out:

How business planning leads to better management:
<http://www.entrepreneur.com/article/219424>

Organising

Organising entails grouping and coordinating activities, creating posts and allocating duties, authority and responsibilities to subordinates. Organising includes providing resources such as labour, capital and raw materials (or stock) and dividing and distributing tasks. It means that you must determine in advance how, where, by whom, when and with what resources jobs must be carried out.

Leading

Leading refers to the way in which a manager motivates subordinates to work together voluntarily to achieve the objectives of the enterprise.



Check out:

How managers can be true leaders, not just taskmasters:
<http://www.entrepreneur.com/article/235929>

Control

Control means determining realistic standards against which the actual performance of the employees and the enterprise can be measured so that deviations can be identified

and corrective steps taken. The manager ensures that employees carry out instructions according to plan so that the objectives of the enterprise can be achieved.



Read the discussion on general management in section 6.7.8 in the prescribed textbook.



You have now reached the end of learning unit 6.

SUMMARY

The setting-up and establishment factors are not equal for all businesses. It is vital that you, as the entrepreneur, realise this important fact in order to determine which factors are critical for the success of your enterprise. The emphasis of the enterprise often shifts and growth makes different demands on the enterprise. Where you may have started with a few or no staff members, you have to appoint more staff members as the need grows. You must take note of the critical success factors in the implementation stage, but must also be aware that the situation is not static. To ensure competitiveness and survival, provision for change must be made in time.

We have now covered all the stages in the creation of an enterprise. We trust that you have learned how to come up with creative ideas, how to test the feasibility and viability of your idea, how to compile a business plan and how to implement your idea to start a real enterprise.



SELF-ASSESSMENT

To test and assess your knowledge of this learning unit, you can now do the following activities:

- (i) *Complete the self-assessment questions on learning unit 6 below. Remember: The only way you can test your knowledge is by answering the questions without looking at the solutions contained in Appendix A.*
- (ii) *Do the self-assessment questions in the prescribed textbook at the end of chapter 6.*

Read the case study below and answer all the questions that follow.

Case study: Leather for Africa

Oudtshoorn is a town in the Little Karoo that is well known for its ostrich farms. Freddy Fredericks was the owner of a small sole proprietorship that manufactured purses and handbags from ostrich leather. Freddy bought the leather from a local tannery, manufactured the products with the help of his two employees, Tom and Jerry, and sold them to local shops and hawkers. Freddy experienced a serious cash flow problem, because he sold his products on credit to the local shops, while he had to pay his supplier in cash. To

make matters worse, the price of leather also increased owing to a drought in the area and the outbreak of bird flu. His sales figures started to show a drastic decline, as he had to compete with several bigger enterprises that manufactured the same types of product in bulk at lower costs and therefore could afford to sell them at lower prices. Freddy decided to retire and asked his son, Leon, to take over the business.

Leon took over the business, realising that the business would not survive unless he made some drastic changes. He decided to involve six of his friends in the enterprise to accumulate more capital and expertise. The new owners registered the enterprise, Leather for Africa, as a private company with Leon as the director. Leon invested R40 000 of his savings in the business and his friends each contributed R10 000. However, they still had to apply for financing of R150 000 to purchase more industrial sewing machines, cutters, workbenches and office equipment.

The new owners decided to add more products to the existing range. They included a bigger variety of purses and handbags, as well as belts, cell phone covers, book covers and attaché cases of various shapes and sizes for men and women. They also decided to rent a larger factory in an industrial area to increase the capacity of the enterprise. They employed more staff to manufacture the products and Tom and Jerry were promoted to supervisors of the manufacturing division. Heidi was appointed to handle the administration of the new enterprise.

Leon and the other owners realised that they would not survive if they concentrated only on the local market and tourists. They decided to launch a marketing campaign, starting off with personal visits to owners of clothing shops in George and Mossel Bay, showing them samples of their products. Three of these shop owners agreed to sell the products. Leather for Africa also advertised their products in a regional newspaper, offering to sell them to the public on an order basis.

Leather for Africa could now also afford to sell their products at more competitive prices. Since they were now buying the leather in bulk, they qualified for discount prices. The supplier also agreed to sell the leather on credit to them, which resulted in a tremendous difference in their cash flow figures.

Multiple-choice questions

- (1) One of the factors that Leon and the other owners had to keep in mind when they had to choose a form of enterprise is **legal personality**. They decided to register the enterprise as a **private company**, which means that Leather for Africa _____.
 - (a) can exist independently of Leon and the other shareholders
 - (b) cannot exist independently of Leon and the other shareholders
 - (c) can act in its own name
 - (d) can own its own assets

Choose correct option:

- (1) a, b
- (2) a, b, c, d

- (3) b, c, d
 - (4) a, c, d
- (2) Because Leon and the other owners have registered the enterprise as a private company, their **liability** would be _____ .
- (1) unlimited, which means that they could lose their private assets if the enterprise goes bankrupt
 - (2) limited to their own personal debts
 - (3) limited to the debts of the enterprise
 - (4) limited to the capital they have invested in the enterprise
- (3) Leon and the other owners also had to keep the **continuity** of the enterprise in mind. Leather for Africa would _____ .
- (1) have limited continuity
 - (2) have an indefinite lifespan
 - (3) cease to exist if one of the shareholders withdrew from the enterprise
 - (4) cease to exist if they decided to involve more shareholders
- (4) Because Leather for Africa is a private company, the **prospects of financing** would be _____ .
- (1) limited to Leon's creditworthiness
 - (2) worse than that of a sole proprietorship
 - (3) limited to the enterprise's creditworthiness
 - (4) limited to the shareholders' creditworthiness
- (5) To be allowed to set up a business, Leon and the other owners should have **full legal capacity**. This means that they _____ .
- (1) may be insolvent
 - (2) have to comply with the rules and regulations of the local authorities
 - (3) may not be under judicial management
 - (4) do not need to have the capacity to pay their bills
- (6) Working with industrial sewing machines and cutters could be dangerous. Therefore Leather for Africa had to take out insurance for their employees before they could start to work. **If an accident takes place, the employees can claim compensation** from the _____ .
- (1) local authorities
 - (2) South African Revenue Service
 - (3) Unemployment Insurance Fund
 - (4) Compensation Commissioner
- (7) The owners of Leather for Africa decided to rent a larger factory to increase the capacity of the enterprise. The **most important establishment factors** that Leather for Africa had to consider were _____ .
- (a) the availability of raw materials
 - (b) the market

- (c) cumulative attraction
- (d) energy and water

Choose the correct option:

- (1) a, c
 - (2) b, d
 - (3) a, b, c
 - (4) a, d
- (8) To manufacture the leather products without interruptions, the operations function should determine how much leather they would need and notify the _____ function in advance so that **the leather can be bought in time from the local tannery.**
- (1) marketing
 - (2) public relations
 - (3) purchasing
 - (4) information management
- (9) **Showing samples of their products** to the clothing shops in George and Mossel Bay and **placing advertisements in the regional newspaper** is the responsibility of the _____ function of Leather for Africa.
- (1) marketing
 - (2) public relations
 - (3) operations
 - (4) information management
- (10) Leather for Africa employed more staff to manufacture the products and Tom and Jerry were promoted to supervisors of the manufacturing division. The **division of tasks** forms part of the _____ element of the general management function of Leather for Africa.
- (1) planning
 - (2) organising
 - (3) leading
 - (4) control



SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS

Please refer to Appendix A for the suggested solutions to the self-assessment questions.

APPENDIX A

CHAPTER 1



SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS

Case study: New Romantics

1. 3

An entrepreneur takes the risk to start his or her own enterprise and is creative, innovative and responsible for the growth of the enterprise. Options a and c relate to the characteristics of a small business manager. Therefore, only option 3 can be correct.

2. 1

An intrapreneur is creative and innovative and contributes towards the growth of the enterprise, but is not willing to take the risk of starting his or her own enterprise. Nicky is an employee with entrepreneurial abilities. Option 2 is incorrect, because an entrepreneur takes the risk to start his or her own enterprise. Option 3 is incorrect, because a small business manager is the owner of the business and does not display any creativity and innovation. Option 4 is incorrect, as a franchisor is an entrepreneur and New Romantics is not a franchise.

3. 4

Options 1 and 2 are advantages of an informal enterprise. Option 3 is a disadvantage of a formal enterprise. A formal enterprise has easier access to external finance than an informal enterprise.

4. 2

Commitment refers to the owner's willingness to dedicate his or her money, skills and expertise to establish and build the enterprise. Option 1 refers to the owner's willingness to perform tasks himself or herself, option 3 refers to the owner's ability to learn from setbacks and failures and option 4 refers to the owner's ability to carry on, despite setbacks and difficult situations.

5. 1

Involvement refers to the owner's willingness to work in the enterprise himself or herself. Nadene is personally involved in the enterprise and is aware of everything that is happening at all levels and in all the divisions of New Romantics.

6. 4

If the enterprise fails, the owner would not only lose his or her own capital, but would also be liable for paying back the borrowed capital. Option 1 refers to the owner's ability

to identify and implement opportunities, option 2 refers to the owner's ability to carry on, despite setbacks and difficult situations and option 3 refers to the owner's ability to learn from setbacks and failures.

7. 1

Creativity refers to the ability to identify new ideas and opportunities, and innovation refers to the ability to implement or apply these ideas and opportunities. Nadene identified and implemented the opportunity to open the shop.

8. 2

Option 1 refers to the owner's overall knowledge of the enterprise. Option 3 refers to the continued existence of the enterprise. Option 4 refers to the ability of the owner to distinguish between income and profit. Growth refers to the expansion of the enterprise.

9. 1

If New Romantics does not maintain sound human relations with their consumers, the consumers will not refer other customers to them. Option 2 refers to perseverance. Options 3 and 4 refer to the owner's willingness to risk investing own capital in the enterprise.

10. 3

Option a is incorrect, since profit is the amount that is left after she has bought more fabric and paid the seamstresses' salaries and all her other expenses. Income is the amount she gets from the sales of the wedding gowns and must first be used to purchase more stock and to pay operating expenses. Therefore, only option 3 can be correct.

CHAPTER 2



SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS

Case study: Lazy to Cook

1. 3

By acting as a wedding planner and coordinator, Zanele provides a service. Therefore options 1 and 4 are incorrect. Option 2 is also incorrect, as this answer relates to the branch of industry, not the production branch.

2. 2

Zanele prepares the food, which indicates that she transforms the ingredients into a meal. This activity falls under the secondary sector. She also provides a service by acting as a wedding planner and coordinator, which means that the enterprise can also be classified under the tertiary sector. Option a is incorrect because Zanele is not involved in the exploitation of natural resources. Option d is also incorrect because she does not sell products to consumers and the commercial activity falls under the tertiary sector.

3. 1

An entrepreneur starts an enterprise with the primary (main) objective of making a profit. Options 2, 3 and 4 are examples of secondary objectives. Secondary objectives are additional objectives that are set to support the achievement of the primary objective.

4. 1

Zanele needs ingredients (raw materials) to prepare the food. Option 2 refers to the employees of the enterprise, option 3 refers to Zanele's ability to take the risk to start her own enterprise and option 4 refers to the money she uses in the enterprise.

5. 1

Option 2 is incorrect, as it refers to the right of consumers to decide what products they want to buy. Option 3 is incorrect, as it refers to the right of consumers to complain about the quality of products or services. Option 4 is also incorrect, as it refers to the right of consumers to be protected against harmful products. Although options 1 and 4 are closely related, Zanele does not sell unsafe products and therefore does not have to warn her consumers against the use of her catering services.

6. 3

Option 1 refers to the fact that the bridal couple has to choose, for example, whether they want to spend their limited budget on a wedding reception or on their honeymoon.

If they decide on a reception, they have to decide what type of reception they want – a morning tea, a lunch or a formal evening reception. This refers to option 2. As soon as they have decided on the type of reception, they have to decide on the details of the reception, which includes the type of food they want to serve. This refers to option 3. Then they have to decide who will be doing the catering, which refers to option 4.

7. 2

The market is made up of different ethnic groups and each group has a distinctive culture and lifestyle, which will obviously influence the type of reception they would prefer. The economic environment relates to inflation and interest rates, the political environment relates to legislation and the influence of government, and the physical environment relates to natural resources and pollution.

8. 3

The petrol price relates directly to the economic environment, as it has a direct influence on the prices of products and services. Although the international environment determines the oil prices and exchange rates, petrol prices are classified under the economic environment.

9. 4

The physical environment relates to natural resources and pollution and includes weather conditions and natural disasters. Therefore, only option 4 can be correct.

10. 1

The political environment relates to legislation which determines that formal businesses must register a specific form of enterprise. It also relates to the influence of local authorities which specifies that businesses that are involved in the food industry must comply with municipal health requirements.

CHAPTER 3



SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS

Case study: Power for the Nation

1. 1

During the idea stage the entrepreneur identifies, develops and tests the feasibility of business ideas. Option 2 refers to testing the viability of the idea and drawing up the business plan, option 3 forms part of option 2 and option 4 refers to the actions that the entrepreneur has to take to convert the idea into an enterprise.

2. 4

During the implementation stage the entrepreneur takes all the actions to convert the idea into an enterprise. Option 1 refers to identifying and testing the feasibility of ideas, option 2 refers to testing the viability of the idea and drawing up the business plan and option 3 forms part of option 2.

3. 3

The planning stage represents the decision-making stage. During this stage, the entrepreneur has to make all the decisions concerning the proposed enterprise and also has to decide whether the idea is viable. Option 1 refers to identifying and testing the feasibility of ideas, option 2 forms part of option 1 and option 4 refers to the actions that the entrepreneur has to take to convert the idea into an enterprise.

4. 2

Divergent thinking entails the ability of the entrepreneur to think of many original, diverse and elaborate ideas. This is essential to the novelty of creative products. Options a and d refer to convergent thinking. Therefore, only option 2 can be correct.

5. 1

When applying this method, entrepreneurs learn to judge everything that they read or observe on the strength of the ideas they can develop from it. Option 2 relates to putting the ideas on paper, option 3 relates to getting a better understanding of other people's perspectives and option 4 relates to exploring the grey areas between right and wrong.

6. 4

Option d is incorrect, because it relates to another method of cultivating a creative attitude. Option 1 is incorrect, because it does not include option c which is also an example of breaking your routine. Therefore, only option 4 can be correct.

7. 1

Skills can be learned and can also be obtained from formal training. Martin studied to become a qualified electrician. Option 2 refers to experience. Options 3 and 4 are actually the same, as aptitudes refer to inborn talents.

8. 3

Option 1 refers to the fact that Martin and Jessica have to be aware of their daily routines. Option 2 refers to their qualifications, experience and natural talents. Option 4 refers to the use of other sources, such as the Yellow Pages, business publications and expired patents. Martin and Jessica listened to their customers and identified that all of them experienced a need for generators.

9. 1

A bow-tie diagram is used to develop ideas in terms of the essence of the idea, the possible combination of ideas and the possibility of taking a new direction with the idea. Option 2 refers to the profit potential of the idea and forms part of option 4, option 3 refers to the potential of the idea to be converted into an enterprise and option 4 refers to the market and profit analysis of the idea.

10. 1

A feasibility study is a general examination of the potential of the idea to be converted into an enterprise. This study focuses on the ability of the entrepreneur to put the idea into practice. Options c and d form part of the viability study which focuses on the market and profit potential of the idea. Therefore, only option 1 can be correct.

CHAPTER 4



SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS

Case study: The Feather Dusters

1. 3

The market analysis consists of three steps. The first step entails determining and analysing the total potential market, the second step entails determining the target market and the third step entails determining the expected market share. Options a and b form part of determining the profit potential of the idea. Therefore, only option 3 can be correct.

2. 3

The psychographic segment represents the lifestyle of the consumers, which determines the types of cleaning services they would prefer. Option 1 relates to where the consumers live, option 2 relates to who the consumers are and option 4 relates to when and how often the consumers would use the cleaning services.

3. 4

The behaviouristic segment represents the buying pattern of the consumers, which determines when and how often they would use the cleaning services. Option 1 relates to where the consumers live, option 2 relates to who the consumers are and option 3 relates to which types of services the consumers prefer.

4. 3

The psychographic segment represents the lifestyle of the consumers, which includes whether or not they work full-time. Option 1 relates to where the consumers live, option 2 relates to who the consumers are and option 4 relates to when and how often the consumers would use the cleaning services.

5. 4

Opportunities and threats come from the market and macro-environments. Power cuts can be classified as an example of the physical environment (a variable in the macro-environment). Option 3 is incorrect, as power cuts could delay the execution of the cleaning services and can therefore be regarded as a threat. Options 1 and 2 are also incorrect, because strengths and weaknesses come from the micro-environment.

6. 3

Opportunities and threats come from the market and macro-environments. The legislation on the employment of domestic workers can be classified under the political environ-

ment (a variable in the macro-environment). Option 4 is incorrect, because the legislation persuaded people to rather use cleaning services, which could definitely not be regarded as a threat for The Feather Dusters. Options 1 and 2 are also incorrect, because strengths and weaknesses come from the micro-environment.

7. 1

The capacity of an enterprise refers to the maximum number of products the enterprise can manufacture, or the maximum number of services the enterprise can provide, within a certain period. Wendy had only six employees and one vehicle, therefore The Feather Dusters' capacity restricted the number of services they could provide per day. Option 2 refers to the influence that the economic situation has on the disposable income of consumers. Option 3 refers to the consumers' ability to pay for the cleaning services. Option 4 refers to the number of consumers that would use the cleaning services.

8. 2

Variable costs would increase proportionally with the number of services provided – the more houses they have to clean, the more they have to travel from one destination to another. Option 1 refers to costs that remain the same, regardless of the number of services provided, such as the rent of the new premises. Options 3 and 4 are the same – costs that cannot be allocated directly to the manufacturing of a product.

9. 3

The Feather Dusters provides cleaning services and can therefore be classified as a service enterprise. To calculate the total cost per unit, they have to divide the total costs per month by the hours worked per month. The total costs per month would include the salaries of the cleaning ladies, the rent of the premises and the overheads per month.

10. 4

The formula for calculating the break-even point in units states that fixed costs should be divided by (price per unit minus variable costs per unit). Therefore, only option 4 can be correct.

CHAPTER 5



SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS

Case study: Tony's Garden Services

1. 4

The principles of a business plan state that it should serve as a blueprint of the business by including all the facets of the proposed business and that it should be a flexible planning document that makes provision for future changes in the business environment. Although the business plan can be compiled by external consultants, the entrepreneur should be personally involved in the development of the business plan. Because option c is incorrect, only option 4 can be correct.

2. 4

Option 1 refers to the fact that the business plan should act as a checklist of all sets of information, option 2 refers to the fact that the information in the business plan should correspond in order to make business sense and option 3 refers to the fact that the business plan should contain valuable information.

3. 1

Direct distribution means that the service is provided directly to the clients. Options 3 and 4 refer to the use of intermediaries, such as wholesalers, retailers or agents, to transfer the product or service to the consumers. Option 2 is totally incorrect – no distribution implies that no sales transaction has taken place.

4. 3

Option 1 refers to the use of newspapers or magazines to advertise products or services, option 2 refers to special offers for a limited period and option 4 refers to sponsorships or articles in newspapers or magazines.

5. 3

The management plan includes topics such as the organisational structure, the form of enterprise, the ownership structure and the human resources plan. Option 1 includes a general description of the enterprise and information on the branch of industry and the objectives of the enterprise. Option 2 includes information on the target market, market share and marketing strategy. Option 4 includes the financial forecasts, as well as all the financial statements and budgets.

6. 4

When we add all their capital contributions, the own capital equals R100 000. Tony contributed R70 000 and therefore owns 70% of Tony's Garden Services. Paul, John and Sharon each contributed R10 000 and therefore each of them owns 10% of the enterprise.

7. 1

When an entrepreneur applies for a loan, the financial institutions would insist on some kind of collateral, such as fixed assets, property or policies, which they can repossess if the entrepreneur fails to repay the loan. Option 2 is incorrect, as current assets are not regarded as collateral. Options 3 and 4 are totally incorrect, as liabilities refer to the debts that the enterprise has to repay.

8. 1

Only option 1 can be correct. To calculate the net profit, the expenses should be deducted from the gross profit.

9. 2

Only option 2 can be correct. To calculate the closing cash balance, the opening cash balance should be added to the net cash balance.

10. 3

Capital employed reflects own capital, long-term liabilities and current liabilities. This indicates how much capital is available to the enterprise. Options b and c are examples of the employment of capital. This indicates how the capital was invested, or what assets were bought with the available capital. Therefore, only option 3 can be correct.

CHAPTER 6



SUGGESTED SOLUTIONS TO THE SELF-ASSESSMENT QUESTIONS

Case study: Leather for Africa

1. 4

Legal personality means that the enterprise is regarded as an entity on its own. This implies that the enterprise exists independently of its owners and can act in its own name. The assets and liabilities of the enterprise are completely separate from those of the owners. Option b is incorrect, as it refers to an enterprise without legal personality.

2. 4

If an enterprise has legal personality, the enterprise is liable for its own debts and the owners can lose only the capital they have invested in the enterprise. Option 1 is incorrect, as this refers to an enterprise without legal personality. Option 2 is incorrect, because the personal debts of the owners do not form part of the debts of the enterprise. Option 3 is also incorrect – if the amount of debt exceeds the capital contribution of the owners, their private assets cannot be attached to settle the debts of the enterprise.

3. 2

Because a private company has legal personality, its existence is not dependent on its members. This means that a private company has unlimited continuity or an indefinite lifespan. Options 1, 3 and 4 relate to an enterprise without legal personality.

4. 3

Options 1 and 4 are incorrect, because a private company is regarded as a legal person on its own. The owners apply for a business loan in the name of the enterprise, not in their personal capacity. Option 2 is incorrect, as a sole proprietorship can only have one owner and the enterprise cannot exist independently of its owner. This means that the prospect of financing is limited to one person's ability to accumulate capital.

5. 3

Full legal capacity means that an insolvent person or a person under judicial management may not start an enterprise. Therefore, options 1 and 4 are incorrect. Option 2 is also incorrect, as this relates to registration with the local authorities.

6. 4

Option 1 is incorrect, as this relates to the payment of service and turnover levies to the local authorities. Option 2 is incorrect, as this relates to the fact that all enterprises must

register with SARS as taxpayers, as employers, as well as for VAT. Option 3 is also incorrect, as this relates to the compensation of employees in the lower income groups if they are dismissed or have to take maternity leave.

7. 4

Leather for Africa is a manufacturing enterprise because they do not sell the leather products directly to consumers. They would therefore establish near the source of raw materials (the local tannery) to save transport costs and they would also need energy and water to manufacture their products. Options b and c relate to establishment factors for commercial enterprises and they cannot be classified as a commercial enterprise.

8. 3

The purchasing function is responsible for buying production means of the right quality, in the right quantities, at the right time, so that the operations function can continue its activities without interruptions. The marketing function is responsible for selling the products to consumers, the public relations function is responsible for improving the image of the enterprise and the information management function is responsible for distributing information.

9. 1

The marketing function is responsible for selling the products of the enterprise and includes activities such as personal sales and advertising. The public relations function is responsible for improving the image of the enterprise, the operations function is responsible for transforming inputs into outputs and the information management function is responsible for distributing information.

10. 2

Organising entails the provision of capital, resources and labour, as well as the division of tasks. Option 1 relates to setting objectives, option 3 relates to motivating employees so that they will perform their tasks willingly and option 4 relates to setting performance and quality standards and ensuring that employees comply with these standards.