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Skills for the Workplace

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Managing Enterprise in the 21st Century

Complete Business Plan Handbook

**by
Michaela Schriek**

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Business Idea

Somewhere between scribbling your idea on a cocktail napkin and actually starting a business, there's a process you need to carry out that essentially determines either your success or failure in business. Oftentimes, would-be entrepreneurs get so excited about their "epiphanies"-the moments when they imagine the possibilities of a given idea-that they forget to find out whether that idea is viable.

For some entrepreneurs, getting the idea-and imagining the possibilities-is the easy part. It's the market research that doesn't come so naturally.

Market research, then, can prove invaluable in determining your idea's potential. You can gather information from industry associations, Web searches, periodicals, federal and state agencies, and so forth. A trip to the library or a few hours online can set you on your way to really understanding your market. Your aim is to gain a general sense of the type of customer your product or service will serve-or at least to being willing to find out through the research process.

The type of information you'll be gathering depends on the type of product or service you want to sell as well as your overall research goals. You can use your research to determine a potential market, to size up the competition, or to test the usefulness and positioning of your product or service.

Assuming your research process has helped you uncover your competition, you now need to find out what they're up to.

Your aim is to understand what your competition is doing so you can do it better. Maybe their service is poor. Maybe their product has some flaws-something you'll only know if you try it out yourself. Or maybe you've figured out a way to do things better, smarter, more cost-effectively. Find your selling point. It's going to be the core of your marketing program, if and when you're ready for that step. It's also going to be what sets you apart and lures customers your way.

Business Identity

A business (also called a firm or an enterprise) is a legally recognized organization designed to provide goods and/or services to consumers, governments or other businesses.

The owners and operators of a business have as one of their main objectives the receipt or generation of a financial return in exchange for work and acceptance of risk.

The private sector:

Sole trader - is a type of business entity which legally has no separate existence from its owner.

Partnership- is a type of business entity in which partners (owners) share with each other the profits or losses of the business undertaking in which all have invested.

Companies - There are two types of company:

Limited company (Ltd), which does not offer its shares to the general public, and the **Public limited company (Plc)**, shares in which are offered to the public at large through the medium of the Stock Exchange.

Mission Statements

The mission statement should be a clear and succinct representation of the enterprise's purpose for existence.

It should incorporate socially meaningful and measurable criteria addressing concepts such as the moral/ethical position of the enterprise, public image, the target market, products/services, the geographic domain and expectations of growth and profitability.

Mission Statements Examples:

Disney:

"We create happiness by providing the finest in entertainment for people of all ages, everywhere."

Sainsbury

"Our mission is to be the consumer's first choice for food, delivering products of outstanding quality and great service at a competitive cost through working 'faster, simpler and together.'"

Asda

Our aim at ASDA is simple - to continually lower our prices so we can save our customers money every day.

Environment Analysis

External and internal analysis for your business

Understanding the environment your business operates in is a key part of planning and will allow you to discern the **threats** and **opportunities** associated with your area of business.

A **PESTEL** analysis helps you to identify the main opportunities and threats in external environment;

- **P**olitical changes such as new regulations due to government changes
- **E**conomic factors such as interest rates, exchange rates and consumer confidence
- **S**ocial factors such as changing attitudes and lifestyles, and the ageing population
- **T**echnological factors such as new materials and growing use of the internet
- **E**nvironmental factors such as global warming or impact of your product on the environment and legislation covering disposal of such products
- **L**egal factors such as changes in laws and regulations,

You also need to understand your own internal **strengths** and **weaknesses**. For example, the main strengths of a new business might be an original product and enthusiastic employees. The main weaknesses might be the lack of an existing customer base and limited financial resources.

A **SWOT** analysis combines the external and internal analysis to summarise your Strengths, Weaknesses, Opportunities and Threats. You need to look for opportunities that play to your strengths. You also need to decide what to do about threats to your business and how you can overcome important weaknesses.

For example, your SWOT analysis might help you identify the most promising customers to target. You might decide to look at ways of using the internet to reach customers. And you might start to investigate ways of raising additional investment to overcome your financial weakness.

Your marketing objectives

Your marketing objectives should be based on understanding your strengths and weaknesses, and the business environment you operate in. They should also be linked to your overall business strategy.

For example, suppose your business objectives include increasing sales by 10 per cent over the next year. Your marketing objectives might include targeting a promising new market segment to help achieve this growth.

Objectives should always be **SMART**:

- **Specific** - for example, you might set an objective of getting ten new customers.
- **Measurable** - whatever your objective is, you need to be able to check whether you have reached it or not when you review your plan.
- **Achievable** - you must have the resources you need to achieve the objective. The key resources are usually people and money.
- **Realistic** - targets should stretch you, not de-motivate you because they are unreasonable.
- **Time-bound** - you should set a deadline for achieving the objective. For example, you might aim to get ten new customers within the next 12 months.

The Marketing Mix

The **marketing mix definition** is simple. It is about putting the right product or a combination thereof in the place, at the right time, and at the right price. The difficult part is doing this well, as you need to know every aspect of your business plan.

As we noted before, the marketing mix is predominately associated with the 4Ps of marketing, the 7Ps of service marketing, and the 4 Cs theories developed in the 1990s.

A marketing expert named E. Jerome McCarthy created the Marketing 4Ps in the 1960s. This classification has been used throughout the world. Business schools teach this concept in basic marketing classes.

The marketing 4Ps are also the foundation of the idea of marketing mix.



#1 Marketing Mix – Product

A product is an item that is built or produced to satisfy the needs of a certain group of people. The product can be intangible or tangible as it can be in the form of services or goods.

You must ensure to have the right type of product that is in demand for your market. So during the product development phase, the marketer must do an extensive research on the life cycle of the product that they are creating.

A product has a certain life cycle that includes the growth phase, the maturity phase, and the sales decline phase. It is important for marketers to reinvent their products to stimulate more demand once it reaches the sales decline phase.

Marketers must also create the right product mix. It may be wise to expand your current product mix by diversifying and increasing the depth of your product line.

All in all, marketers must ask themselves the question “what can I do to offer a better product to this group of people than my competitors”.

In developing the right product, you should answer the following questions:

- What does the client want from the service or product?
- How will the customer use it?
- Where will the client use it?
- What features must the product have to meet the client's needs?
- Are there any necessary features that you missed out?
- Are you creating features that are not needed by the client?
- What's the name of the product?
- Does it have a catchy name?
- What are the sizes or colors available?
- How is the product different from the products of your competitors?
- What does the product look like?

#2 Marketing Mix – Price

The price of the product is basically the amount that a customer pays for to enjoy it. Price is a very important component of the **marketing mix definition**.

It is also a very important component of a marketing plan as it determines your firm's profit and survival. Adjusting the price of the product has a big impact on the entire marketing strategy as well as greatly affecting the sales and demand of the product.

This is inherently a touchy area though. If a company is new to the market and has not made a name for themselves yet, it is unlikely that your target market will be willing to pay a high price.

Although they may be willing in the future to hand over large sums of money, it is inevitably harder to get them to do so during the birth of a business.

Pricing always help shape the perception of your product in consumer's eyes. Always remember that a low price usually means an inferior good in the consumer's eyes as they compare your good to a competitor.

Consequently, prices too high will make the costs outweigh the benefits in customers' eyes, and they will therefore value their money over your product. Be sure to examine competitors pricing and price accordingly.

When setting the product price, marketers should consider the perceived value that the product offers. There are three major pricing strategies, and these are:

- Market penetration pricing
- Market skimming pricing
- Neutral pricing

Here are some of the important questions that you should ask yourself when you are setting the product price:

- How much did it cost you to produce the product?
- What is the customers' perceived product value?
- Do you think that the slight price decrease could significantly increase your market share?
- Can the current price of the product keep up with the price of the product's competitors?

#3 Marketing Mix – Place

Placement or distribution is a very important part of the product mix definition. You have to position and distribute the product in a place that is accessible to potential buyers.

This comes with a deep understanding of your target market. Understand them inside out and you will discover the most efficient positioning and distribution channels that directly speak with your market.

There are many distribution strategies, including:

- Intensive distribution
- Exclusive distribution
- Selective distribution
- Franchising

Here are some of the questions that you should answer in developing your distribution strategy:

- Where do your clients look for your service or product?
- What kind of stores do potential clients go to? Do they shop in a mall, in a regular brick and mortar store, in the supermarket, or online?
- How do you access the different distribution channels?
- How is your distribution strategy different from your competitors?
- Do you need a strong sales force?
- Do you need to attend trade fairs?
- Do you need to sell in an online store?

#4 Marketing Mix – Promotion

Promotion is a very important component of marketing as it can boost brand recognition and sales. Promotion is comprised of various elements like:

- Sales Organisation
- Public Relations
- Advertising
- Sales Promotion

Advertising typically covers communication methods that are paid for like television advertisements, radio commercials, print media, and internet advertisements. In contemporary times, there seems to be a shift in focus offline to the online world.

Public relations, on the other hand, are communications that are typically not paid for. This includes press releases, exhibitions, sponsorship deals, seminars, conferences, and events.

Word of mouth is also a type of product promotion. Word of mouth is an informal communication about the benefits of the product by satisfied customers and ordinary individuals. The sales staff plays a very important role in public relations and word of mouth.

It is important not to take this literally. Word of mouth can also circulate on the internet. Harness this effectively and it has the potential to be one of the most valuable assets you have in boosting your profits online. An extremely good example of this is online social media and managing a firm's online social media presence.

In creating an effective product promotion strategy, you need to answer the following questions:

- How can you send marketing messages to your potential buyers?
- When is the best time to promote your product?
- Will you reach your potential audience and buyers through television ads?
- Is it best to use the social media in promoting the product?
- What is the promotion strategy of your competitors?

Your combination of promotional strategies and how you go about promotion will depend on your budget, the message you want to communicate, and the target market you have defined already in previous steps.

Marketing Mix 7Ps

The 7Ps model is a marketing model that modifies the 4Ps model. The 7Ps is generally used in the service industries.

Here is the expansions from the 4Ps to the 7Ps marketing model:



#5 Marketing Mix – People

Of both target market and people directly related to the business.

Thorough research is important to discover whether there are enough people in your target market that is in demand for certain types of products and services.

The company's employees are important in marketing because they are the ones who deliver the service. It is important to hire and train the right people to deliver superior service to the clients, whether they run a support desk, customer service, copywriters, programmers...etc.

When a business finds people who genuinely believe in the products or services that the particular business creates, it's highly likely that the employees will perform the best they can.

Additionally, they'll be more open to honest feedback about the business and input their own thoughts and passions which can scale and grow the business.

This is a secret, "internal" competitive advantage a business can have over other competitors which can inherently affect a business's position in the marketplace.

#6 Marketing Mix – Process

The systems and processes of the organization affect the execution of the service.

So, you have to make sure that you have a well-tailored process in place to minimize costs.

It could be your entire sales funnel, a pay system, distribution system and other systematic procedures and steps to ensure a working business that is running effectively.

Tweaking and enhancements can come later to "tighten up" a business to minimize costs and maximize profits.

#7 Marketing Mix – Physical Evidence

In the service industries, there should be physical evidence that the service was delivered. Additionally, physical evidence pertains also to how a business and its products are perceived in the marketplace.

It is the physical evidence of a business' presence and establishment. A concept of this is branding. For example, when you think of "fast food", you think of McDonalds.

When you think of sports, the names Nike and Adidas come to mind.

You immediately know exactly what their presence is in the marketplace, as they are generally market leaders and have established a physical evidence as well as psychological evidence in their marketing.

They have manipulated their consumer perception so well to the point where their brands appear first in line when an individual is asked to broadly "name a brand" in their niche or industry.

Marketing Mix 4Cs



The 4Cs marketing model was developed by Robert F. Lauterborn in 1990. It is a modification of the 4Ps model. It is not a basic part of the **marketing mix definition**, but rather an extension. Here are the components of this marketing model:

- Cost – According to Lauterborn, price is not the only cost incurred when purchasing a product. Cost of conscience or opportunity cost is also part of the cost of product ownership.
- Consumer Wants and Needs – A company should only sell a product that addresses consumer demand. So, marketers and business researchers should carefully study the consumer wants and needs.
- Communication – According to Lauterborn, “promotion” is manipulative while communication is “cooperative”. Marketers should aim to create an open dialogue with potential clients based on their needs and wants.
- Convenience – The product should be readily available to the consumers. Marketers should strategically place the products in several visible distribution points.

Whether you are using the 4Ps, the 7Ps, or the 4Cs, your marketing mix plan plays a vital role. It is important to devise a plan that balances profit, client satisfaction, brand recognition, and product availability. It is also extremely important to consider the overall “how” aspect that will ultimately determine your success or failure.

By understanding the basic concept of the marketing mix and its extensions, you will be sure to achieve financial success whether it is your own business or whether you are assisting in your workplace’s business success.

The ultimate goal of business is to make profits and this is a surefire, proven way to achieve this goal.

Marketing Strategy

One of the key elements of a successful marketing strategy is the acknowledgement that your existing and potential customers will fall into particular **groups** or **segments**, characterised by their 'needs'. Identifying these groups and their needs through market research, and then addressing them more successfully than your competitors, should be the focus of your strategy.

You can then create a marketing strategy that makes the most of your strengths and matches them to the needs of the customers you want to target. For example, if a particular group of customers is looking for quality first and foremost, then any marketing activity aimed at them should draw attention to the high quality service you can provide.

Once this has been completed, decide on the best marketing activity that will ensure your target market know about the products or services you offer, and why they meet their needs.

This could be achieved through various forms of advertising, exhibitions, public relations initiatives, Internet activity and by creating an effective 'point of sale' strategy if you rely on others to actually sell your products. Limit your activities to those methods you think will work best, avoiding spreading your budget too thinly.

A key element often overlooked is that of monitoring and evaluating how effective your strategy has been. This control element not only helps you see how the strategy is performing in practice, it can also help inform your future marketing strategy. A simple device is to ask each new customer how they heard about your business.

Once you have decided on your marketing strategy, draw up a marketing plan to set out how you plan to execute and evaluate the success of that strategy. The plan should be constantly reviewed so it can respond quickly to changes in customer needs and attitudes in your industry, and in the broader economic climate.

Finance

Cost Identification and Itemisation

The first step in setting prices is to establish your costs. This section helps you understand the different types of costs involved in setting up and running your business.

The first step in setting prices is to establish your costs. Your price has to be high enough to cover all the costs you incur and to make a profit. You need to understand the different types of costs involved in setting up and running your business.

Business costs fall into 3 main categories:

- fixed costs or overheads
- direct or variable costs
- capital costs

Fixed costs or overheads

These are the costs you have to pay no matter how much or how little you sell. For example, one of the fixed costs for a shop is the rent. This stays the same whether the shop sells one product or thousands.

Fixed costs include:

- office expenses such as supplies, utilities and telephone
- salaries and wages for you, office staff and salespeople
- marketing and sales expenses, including advertising
- insurance
- vehicle and travel costs
- professional fees
- rent

Direct or variable costs

These costs change as sales increase. For example, the costs of raw materials, packaging and delivery charges are variable costs as they change depending on the number of units you are producing.

For businesses providing a service, there are often fewer variable costs, although these may include charges for freelance support or sub-contractors.

Variable costs include:

- raw materials
- direct labour costs for staff involved in producing products or delivering services
- packaging
- delivery charges
- utilities for a manufacturing base or warehouse
- depreciation expense on production equipment and machinery

Capital costs

These are fixed costs that benefit your business for a long time. This includes items such as machinery, equipment and company vehicles. Capital costs are also known as capital assets.

Depreciation

This is the accounting term used to give a value to the amount of wear and tear on your capital assets. The value of things such as machinery, equipment and vehicles falls as they are used or wear out. Depreciation means the cost of these assets are spread and they are written off against the profits of several years rather than just the year in which they are purchased.

The general rule of thumb is that capital items depreciate by approximately 25% each year.

Talk to your accountant or business adviser for more information on how to work out depreciation and on which items.

	Direct	Indirect	Fixed	Variable	Controllable	Uncontrollable
Bought out components	X			X	X	
Sales Commission		X		X	X	
Materials for Research						
Grain for processing						
Machine operators bonus						
TV advertising						
Production Managers salary						
Advertising for staff						
Office cleaning services						
Electricity						
Overtime for production worker						
Diesel for delivery lorries						
Business rates						
Admin Managers salary						
Stamps for postage						
Professional fees						
Rep's car repairs						

Now that you've identified what it costs to start and run your business, you can work out the cost of producing your product or providing your service. This section takes you through the process of costing your product, costing your service or costing for retail.

Costing your product or service

In the previous section, you identified all the costs associated with starting and running your business. This included capital costs, as well as fixed and variable costs.

Now you are in a position to work out the cost of producing your product or providing your service.

The cost of your product is how much it costs to produce (the raw materials and packaging plus labour) plus a contribution towards the overheads of the business.

Here's how to calculate that overhead contribution:

- estimate how many products you'll sell in a year. In this example, 3,000 units.
- work out your total fixed costs - overheads plus drawings. In our example, overheads are £6,000 and drawings are £12,000, so total fixed costs are £18,000.
- divide the total fixed costs (£18,000) by the number of units you expect to sell (3,000) to calculate how much fixed costs to allocate to each unit.

$$\frac{\pounds 6,000 + \pounds 12,000}{3,000} = \pounds 6$$

Add the direct costs for that unit to calculate the total product cost per item.

In this example, the direct costs are £3.

$$\pounds 6 + \pounds 3 = \pounds 9$$

Here's the full calculation:

<u>Total Overheads + Drawings</u>	<u>£6,000 + £12,000</u>	
Total No of Units	3,000 units	=£6
+ Direct Costs (for that product)		+ £3
Product Cost		= £9

Costing your service

Costing a service works on the same principle as costing a product, but this time takes into account your hourly rate for providing the service.

Here's how to calculate your hourly cost:

Number of weeks you expect to work during the year (be realistic)46

Number of productive (chargeable) hours you expect to work per week24

Work out your total fixed costs (overheads plus drawings) £21,600

Calculate the annual total of chargeable hours 46 X 24 = 1104

Calculate the hourly charge to cover fixed costs 21600/1104 = £19.56

Remember to allocate some time to running the business – for administration, marketing, bookkeeping and planning.

This calculation gives you the basic cost per hour for providing your service. You may also need to add in costs for any materials you use or produce, for example, a trainer may produce a workbook or training notes for delegates, or a plumber may provide replacement items such as a washer or pipes.

Here's the full calculation -

<u>Total Overheads + Drawings</u>	<u>£6,000 + £12,000</u>
Productive Hours	1104 Hours
=Hourly Cost	£19.56

Costing for Retail

If your business is involved in buying items to re-sell, you need to establish how much to add to the price you bought the unit for, so that you cover all your costs and make a profit. This is your retail mark-up.

Here's how to work it out:

In this example, overheads are £9,600, drawings are £12,000 and direct costs are £45,000

Total Overheads + Drawings	£9,600 + £12,000
Direct Costs	£45,000
x100	x100
= Retail mark-up %	= Retail mark up of 48%

This means you would increase the amount you paid for the item by 48% to cover your costs and make a profit. If you paid £1 for the item, you would sell it for £1.48.

Break-even point

The break-even point is the point at which your costs and your income are equal. Anything you sell above break-even generates profit for you. In your calculations, make sure the figures you estimate for the number of units you will sell, or the number of productive hours you will work, are realistic.

Break-even can be used to help you see the relationship between your price and the number of units sold, as well as the effect of different prices on the business.

Calculating your Break-even point

To calculate your break-even point, you need to know:

- total fixed costs/overheads for the year

- direct costs per unit, and
- expected selling price

For example:

Total Fixed Costs - £10,000

Direct Costs per unit - £2

Unit Selling Price - £6

Work out the contribution each unit makes to the total fixed costs by subtracting the direct costs per unit (£2) from the selling price (£6).

Selling Price – Direct Costs per unit £6 - £2 = £4

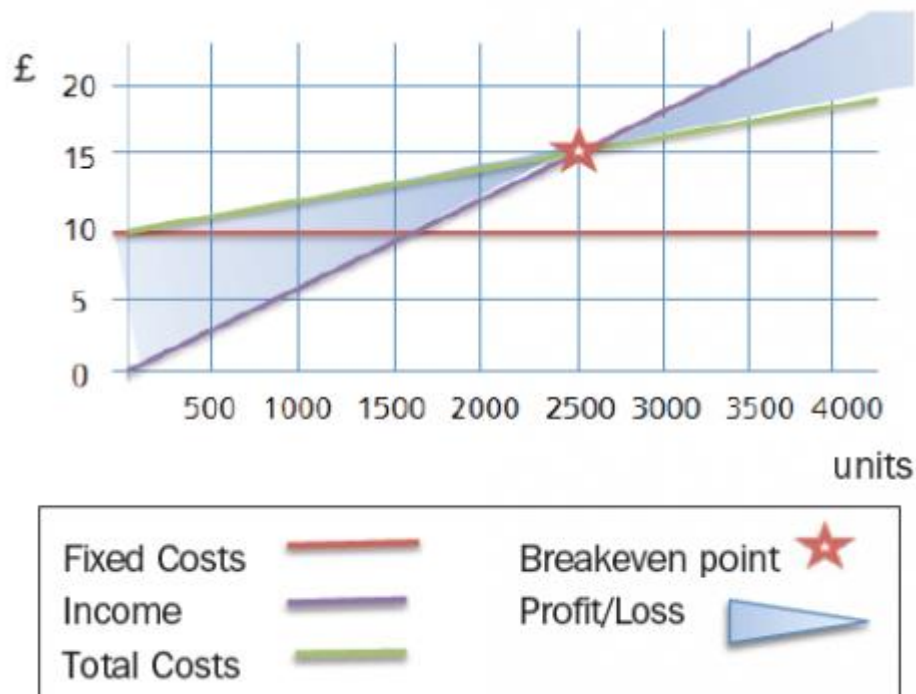
Now divide the total fixed costs (£10,000) by the contribution (£4). This gives you the number of units you have to sell to break-even.

Fixed Costs = Break-even point : £10,000 = 2,500 units

Unit contribution £4

Calculating your Break-even point

In our example, the business needs to sell 2,500 units to break-even. If they produce more than 2,500 units, they make a profit, less than 2,500 units and they make a loss. The sales forecast needs to be higher than 2,500 units to make a profit.



Break-even Point and Pricing

Using this example, let's look at how different price points affect the amount of product you need to sell to break-even.

If the selling price is £8 instead of £6 the contribution per unit is now £6 and the break-even point is 1,667 units

£10,000 = 1,667 units

£6

If the selling price is £4 instead of £6

£10,000 = 5,000 units

£2

From this example, you can see how price and sales are linked:

- selling price of £6 means selling 2,500 units to break-even
- selling price of £8 means selling 1,667 units to break-even
- selling price of £4 means selling 5,000 units to break-even

Make sure that if you adjust your selling price, you understand how much you need to sell to break-even.

Pricing

Pricing is a complex area. Set your prices too high and you may lose the sale. Set them too low, and you leave money on the table. This section looks at the different ways to arrive at your price and the different pricing tactics you may consider.

As we have discussed, pricing is one of the biggest decisions you need to make about your business. To a great extent, the prices you charge determine the amount of profit you make, so getting the price right is vital to your business success.

There are two ways to arrive at your prices:

- cost plus
- market-based price

Cost plus

In this method, you add together all the costs to produce your products or services. This includes materials, labour, packaging, etc. You then add a percentage on top of this cost as profit for you.

In this method of price setting, you add together all the costs to produce your products or services. This includes materials, labour, packaging, etc. You then add a percentage on top of this cost to represent your profit.

Many start-up businesses focus on cost-plus pricing. It is relatively simple to calculate and profit margins are constant.

However, as we have discussed, a number of other factors affect pricing decisions. Here are some disadvantages of cost-plus pricing:

- it ignores the level of demand for your product or service
- it does not take into account how price sensitive your market is – and the customers' willingness to potentially pay more
- if your costs are high relative to competitors, you may find your price is also uncompetitive
- allocation of overheads is often arbitrary and may distort prices
- it takes no account of the image and market position you are aiming for

Market-based price

In this method, (also known as value-based pricing) you estimate what the customer is likely to pay for your product or service based on competitors' prices.

The alternative to cost-plus pricing focuses on what customers are willing to pay. This means you have to understand how much value customers attach to your product or service. You also need to understand your market and the economic conditions.

Here are some examples of market-based pricing:

- someone may pay more for a carton of milk from a small local shop late at night than they would for the same product in a large supermarket because it is more convenient at that time of night
- a brand name product may be considerably more expensive than an unbranded equivalent because people want to own or be associated with the brand
- some people pay a premium price for the latest fashion or gadget because they want to be amongst the first to have it
- this may be on a worldwide basis, but could also be in a local context, for example, "the only supplier of x in Carmarthen"
- the price of a painting by a major artist depends completely on how much someone values that artist's work and how many others may also want the same picture – again a local connection may have a big influence in this situation
- tickets for a sports event or pop concert can be at a high price if there are more potential customers than seats available

- if your business is in a city, you may be able to set prices higher than if you are based in a rural location. This is because potential customers in the city may have higher rates of pay and, therefore, greater spending power

However, if there is a great deal of competition for your product in the city, you may have to set prices lower, whilst a rural-based business with little competition can charge more.

Here's how to set your prices using market-based pricing:

1. Check out competitors' prices. You want to understand what their selling strategy is, so find out what promotions they offer, if they use seasonal discounts or if they keep some prices low to attract sales on other lines.
2. Understand your customers. Review your market research and establish where, when, why, how and how many they buy. Which products or services do your customers think are the best value and why?
3. Combine the information you've gathered about competitors' products and your customers' views and establish a benchmark for your product or service.

Differential pricing

Although you've now set your price, you may decide that it is beneficial to adjust your prices for different customers and different circumstances. This is called differential pricing.

Here are some examples of differential pricing that you may consider using:

- seasonal demand: holidays are more expensive in the summer or during public holidays when demand is higher
- distribution channel: you may have different prices for products sold online against those sold through distributors or through department stores
- products in a farm shop may be a different price from those sold through the local supermarket
- key accounts: you may negotiate a different price with a national account such as a major supermarket chain
- regional variations: prices in a small seaside town may be different from those in large cities
- volume: you may offer a discount to customers buying a large volume
- timing: a plumber can charge a higher price for an emergency call-out and a printer may charge a premium for a fast turnaround.

Whenever you use differential pricing, remember, there must be a justifiable reason for the price difference.

Different pricing tactics

There may be times when pricing is influenced by factors other than costs or perceived value. Tactical pricing can be used to achieve specific objectives.

Consider some of these pricing tactics – each one has a different impact on how many sales you make and on your profit:

- **odd value** - popular in retail, this is when a product is priced at £9.99 instead of £10 with the intention of creating a favourable impression for cost-conscious customers
- **loss leaders** - this is when you sell some products at a loss, so that you can win new customers. Supermarkets use this tactic on frequently purchased products such as bread or baked beans with the aim of getting people to come into the store. You may choose to offer a product at a loss for first-time buyers, increasing the price for subsequent purchases
- **price skimming** - this is when you sell a new product at a high price to customers who “must have it” right at the start. The price is then dropped once the initial demand has been satisfied
- **penetration pricing** - this is the opposite of price skimming and involved introducing a product at a low price and getting as many customers as possible before the competition catches up. This helps to create market share and can also build brand loyalty
- **discounting** - a dangerous tactic to use too often, but one that can be effective if you want to increase sales in the short term or reward loyal customers
- **bundling** - this involves offering a number of products together as a bundle, usually at a lower price than if they were purchased individually. For example, a computer, printer and software bundle, or a surfboard and wetsuit package. This is useful for extending the purchase to complementary or linked products, and can be used for overstocks or slow-moving items

If you provide a service, bundling can be a useful tool as it prevents the customer from negotiating an hourly rate. You can bundle several services together, for example, consultancy and mentoring, or offer a combination of service and product, for example, a complete kitchen bundle – planning and layout, selling the kitchen units and installation and fitting.

Payment terms

Payment terms and payment options are important parts of your pricing strategy. There can be big benefits to both you and the customer, but be sure you understand how much the various options cost you in terms of administration.

Depending on the nature of your business, you may consider:

- asking for payment up-front, either part-payment or full payment

- asking for a deposit followed by staged payments
- requesting payment on completion

Value Added Tax (VAT)

If you are a VAT-registered business, you must charge VAT at the appropriate rate on the goods and services you supply. Remember to include VAT in your pricing calculations. Make it clear to your customers whether your prices include or exclude VAT.

Full details of current VAT thresholds are available on the HMRC website.

Balance Sheet Essentials

The *Accounting Equation*: **Assets = Liabilities + Owner's Equity**

Current Assets

The term *current* in a balance sheet generally means "short-term" which is usually one year or less. Common current assets include **cash** (cash, coin, balances in checking and savings accounts), **accounts receivable** (amounts owed to your business by your customers usually within 10-60 days), **inventory** (goods for sale), and **prepaid expenses** (e.g. insurance and rent).

Long-Term Assets

These assets include **long-term investments**, cost of **property and equipment** (e.g. land, buildings, equipment, tools, furniture, computers, vehicles, etc.) offset by accumulated depreciation, **intangible assets** (e.g. patents, contracts, trademarks, copyrights, and goodwill), and other assets (like *deferred income tax* arising from the loss of value of property that cannot be reported as a tax deduction until the property is sold).

Current Liabilities

These include the obligations to be paid within one year, including **accounts payable**, short-term loans, income taxes payable, wages, unearned revenue (e.g. service contracts), and the current portion of long-term debt (e.g. mortgage payments payable within 12 months).

Long-Term Liabilities

These include **long-term debt** (e.g. notes, mortgages), **capital lease obligations** (e.g. leases structured as loans), and **deferred income tax** (e.g. the tax due on the increase in value of an investment security that isn't paid until the security is sold).

Owner's Equity (or Stockholders' Equity for corporations)

This is basically the amount left over when you subtract Total Liabilities from Total Assets. It includes the **owner's investment(s)** and **retained earnings** (the portion of the profits reinvested in the business).

Example of the first 6 months on a balance sheet (yours needs to show 12 months)

Company Name		Balance Sheet Date					
		Month 1	Month 2	Month 3	Month 4	Month 5	Month 6
Assets							
Current Assets							
Cash	£	400,000.00	£ 320,000.00	£ 320,000.00	£ 320,000.00	£ 320,000.00	£ 320,000.00
Accounts Receivable	£	200,000.00	£ 160,000.00	£ 160,000.00	£ 160,000.00	£ 160,000.00	£ 160,000.00
Inventory (Stock)	£	1,500,000.00	£ 1,200,000.00	£ 1,200,000.00	£ 1,200,000.00	£ 1,200,000.00	£ 1,200,000.00
Prepaid Expenses	£	5,000.00	£ 4,000.00	£ 4,000.00	£ 4,000.00	£ 4,000.00	£ 4,000.00
<Other Current Asset>	£	-	£ -	£ -	£ -	£ -	£ -
Total Current Assets	£	2,105,000.00	£ 1,684,000.00	£ 1,684,000.00	£ 1,684,000.00	£ 1,684,000.00	£ 1,684,000.00
Fixed Assets							
Land	£	150,000.00	£ 120,000.00	£ 120,000.00	£ 120,000.00	£ 120,000.00	£ 120,000.00
Equipment	£	100,000.00	£ 80,000.00	£ 80,000.00	£ 80,000.00	£ 80,000.00	£ 80,000.00
Accumulated Depreciation - Equipment	£	75,000.00	£ 60,000.00	£ 60,000.00	£ 60,000.00	£ 60,000.00	£ 60,000.00
<Other Fixed Asset>	£	-	£ -	£ -	£ -	£ -	£ -
Total Fixed Assets	£	325,000.00	£ 260,000.00	£ 260,000.00	£ 260,000.00	£ 260,000.00	£ 260,000.00
Total Assets	£	2,430,000.00	£ 1,944,000.00	£ 1,944,000.00	£ 1,944,000.00	£ 1,944,000.00	£ 1,944,000.00
Liabilities & Equity							
Current Liabilities							
Accounts Payable	£	60,000.00	£ 48,000.00	£ 48,000.00	£ 48,000.00	£ 48,000.00	£ 48,000.00
Accrued Liabilities	£	300,000.00	£ 240,000.00	£ 240,000.00	£ 240,000.00	£ 240,000.00	£ 240,000.00
<Other Current Liability>	£	-	£ -	£ -	£ -	£ -	£ -
Total Current Liabilities	£	360,000.00	£ 288,000.00	£ 288,000.00	£ 288,000.00	£ 288,000.00	£ 288,000.00
Long Term Liabilities							
Long term loans	£	125,000.00	£ 100,000.00	£ 100,000.00	£ 100,000.00	£ 100,000.00	£ 100,000.00
<Other Long Term Liability>	£	-	£ -	£ -	£ -	£ -	£ -
Total Long Term Liabilities	£	125,000.00	£ 100,000.00	£ 100,000.00	£ 100,000.00	£ 100,000.00	£ 100,000.00
Total Liabilities	£	485,000.00	£ 388,000.00	£ 388,000.00	£ 388,000.00	£ 388,000.00	£ 388,000.00
Equity							
Paid-In Capital	£	500,000.00	£ 400,000.00	£ 400,000.00	£ 400,000.00	£ 400,000.00	£ 400,000.00
<Other Equity>	£	-	£ -	£ -	£ -	£ -	£ -
Retained Earnings	£	1,340,000.00	£ 1,072,000.00	£ 1,072,000.00	£ 1,072,000.00	£ 1,072,000.00	£ 1,072,000.00
Current Year Earnings	£	80,000.00	£ 64,000.00	£ 64,000.00	£ 64,000.00	£ 64,000.00	£ 64,000.00
Total Equity	£	1,920,000.00	£ 1,536,000.00	£ 1,536,000.00	£ 1,536,000.00	£ 1,536,000.00	£ 1,536,000.00
Total Liabilities & Equity	£	2,405,000.00	£ 1,924,000.00	£ 1,924,000.00	£ 1,924,000.00	£ 1,924,000.00	£ 1,924,000.00

A Profit and Loss statement

A profit and loss statement is required for all companies registered at Companies House by law as part of the financial accounts. If you are self-employed then the information which is required to complete your self-assessment return is the basics of a profit and loss account. The report may also be required by management on a monthly basis to assist in business decisions.

A profit and loss account is useful tool for management decisions, as it looks at the costs which relate to sales during the period. It may be that you are selling your goods at 50% higher than you are buying them, but when taking into account all the overheads you are actually making a loss. The pricing, sales and costs can then be reviewed to see how future figures can be improved.

The figures to be posted to the profit and loss account may not be the same as the transactions in your bank account. Instead they are the figures that relate to the month in connection with the sale.

An example of this: during a month a business made sales of £1000, but no goods were purchased, instead existing stock of £500 was sold. This figure of £500 would need to be posted as a cost of sale on the profit and loss account.

There are several other differences between the bank account and the profit and loss account:

- Sales - Include the sales when they take place, this may not be the same month as when you are paid.
- Cost of Sales - Include the cost that relates to the sales which have taken place.
- Accruals - Include any expense which relates to the month for which no invoice has been received.
- Prepayments - You may receive an invoice for a period of time or a future date, post the correct amount in the month it relates to.
- Depreciation - If you own fixed assets they are depreciated over a period of time, a monthly figure will need to be included.

The account is basically made up of sales or turnover, less cost of sales which will give you a gross profit figure. All overheads and dividend payments are then deducted to give you a Profit or Loss figure.

Example of a P&L template

PROFIT & LOSS													
Profit and Loss for the YEAR 2015	Mth 1	Mth 2	Mth 3	Mth 4	Mth 5	Mth 6	Mth 7	Mth 8	Mth 9	Mth 10	Mth 11	Mth 12	YTD
	£	£	£	£	£	£	£	£	£	£	£	£	
Sales	£750.00	£6,500.00	£1,000.00	£200.00	£400.00	£800.00	£350.00	£400.00	£780.00	£5,000.00	£600.00	£450.00	17,230.00
Other business income	£20.00	£20.00	£20.00	£20.00	£20.00	£20.00	£20.00	£20.00	£20.00	£20.00	£20.00	£20.00	240.00
Total turnover	£670.00	£6,520.00	£1,020.00	£220.00	£420.00	£820.00	£370.00	£420.00	£800.00	£5,020.00	£620.00	£470.00	17,370.00
Cost of goods bought for resale or goods used	£300.00	£200.00	£400.00	£300.00	£500.00	£600.00	£700.00	£800.00	£900.00	£400.00	£200.00	£200.00	5,500.00
Total cost of sales	£300.00	£200.00	£400.00	£300.00	£500.00	£600.00	£700.00	£800.00	£900.00	£400.00	£200.00	£200.00	5,500.00
Gross Profit	£370.00	£6,320.00	£620.00	£-80.00	£-80.00	£220.00	£-330.00	£-380.00	£-100.00	£4,620.00	£420.00	£270.00	11,870.00
Car, van and travel expense	£400.00	£400.00	£400.00	£400.00	£400.00	£400.00	£400.00	£400.00	£400.00	£400.00	£400.00	£400.00	4,800.00
Wages, salaries and other staff costs	£120.00	£120.00	£120.00	£120.00	£120.00	£120.00	£120.00	£120.00	£120.00	£120.00	£120.00	£120.00	1,440.00
Rent, rates, power and insurance costs	£240.00	£240.00	£240.00	£240.00	£240.00	£240.00	£240.00	£240.00	£240.00	£240.00	£240.00	£240.00	2,880.00
Repairs and renewals of property and equipment	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	1,200.00
Accountancy, legal and other professional fees	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	£100.00	1,200.00
Interest and bank and credit card etc. financial charges	£10.00	£10.00	£10.00	£10.00	£10.00	£10.00	£10.00	£10.00	£10.00	£10.00	£10.00	£10.00	120.00
Phone, fax, stationery and other office costs	£3.00	£3.00	£3.00	£3.00	£3.00	£3.00	£3.00	£3.00	£3.00	£3.00	£3.00	£3.00	36.00
Total allowable expenses	£973.00	£973.00	£973.00	£973.00	£973.00	£973.00	£973.00	£973.00	£973.00	£973.00	£973.00	£973.00	£11,676.00
Net profit/(loss)	£-603.00	£5,347.00	£-353.00	£-1,053.00	£-1,053.00	£-753.00	£-1,303.00	£-1,353.00	£-1,073.00	£3,647.00	£-553.00	£-703.00	£194.00

Or a different example:

Profit and Loss for the year ended 31st March

	£	£
Sales		
Hardware	100 000	
Consultancy	20 000	
Total sales		<u>120 000</u>
Cost of Sales		
Cost of Goods sold	50 000	
Direct labour	10 000	
Total cost of sales		<u>60 000</u>
Gross Profit		<u>60 000</u>
Overheads		
Salaries	30 000	
Car and Travel	1 200	
rent, rates, power and insurance	3 000	
Telephone and stationery	2 000	
Advertising	500	
Business Entertainment	100	
Bank interest and loans	100	
Bank charges	200	
Legal fees	500	
Depreciation	200	
Corporation Tax	5 000	
Total Overheads		<u>42 800</u>
Profit/Loss		<u><u>17 200</u></u>

Business Plan

It is essential to have a realistic, working business plan when you're starting up a business.

A business plan is a written document that describes a business, its objectives, its strategies, the market it is in and its financial forecasts. It has many functions, from securing external funding to measuring success within your business.

The audience for your business plan

There are many benefits to creating and managing a realistic business plan. Even if you just use it in-house, it can:

- help you spot potential pitfalls before they happen
- structure the financial side of your business efficiently
- focus your development efforts
- work as a measure of your success

Many people think of a business plan as a document used to secure external funding. This is important because potential investors, including banks, may invest in your idea, work with you or lend you money as a result of the strength of your plan.

The following people or institutions may request to see your business plan at some stage:

- banks
- external investors - whether this is a friend, a venture capitalist firm or a business angel
- grant providers
- anyone interested in buying your business
- potential partners

You should also bear in mind that a business plan is a living document that will need updating and changing as your business grows. Regardless of whether you intend to use your plan internally, or as a document for external people, it should still take an objective and honest look at your business. Failing to do this could mean that you and others have unrealistic expectations of what can be achieved and when.

What the plan should include

Your business plan should provide details of how you are going to develop your business, when you are going to do it, who's going to play a part and how you will manage the money.

Clarity on these issues is particularly important if you're looking for finance or investment. The process of building your plan will also focus your mind on how your new business will need to operate to give it the best chance of success.

Your plan should include:

- **An executive summary** - this is an overview of the business you want to start. It's vital. Many lenders and investors make judgments about your business based on this section of the plan alone.
- **A short description of the business opportunity** - who you are, what you plan to sell or offer, why and to whom.
- **Your marketing and sales strategy** - why you think people will buy what you want to sell and how you plan to sell to them.
- **Your management team and personnel** - your credentials and the people you plan to recruit to work with you.
- **Your operations** - your premises, production facilities, your management information systems and IT.
- **Financial forecasts** - this section translates everything you have said in the previous sections into numbers.

The executive summary

The executive summary is often the most important part of your business plan. Positioned at the front of the document, it is the first part to be read. However, as a summary it makes sense to write it last.

It may be the only part that will be read. Faced with a large pile of funding requests, venture capitalists and banks have been known to separate business plans into 'worth considering' and 'discard' piles based on this section alone.

What is it?

The executive summary is a synopsis of the **key points** of your entire plan. It should include highlights from each section of the rest of the document - from the key features of the business opportunity through to the elements of the financial forecasts.

Its purpose is to explain the basics of your business in a way that both informs and interests the reader. If, after reading the executive summary, an investor or manager understands what the business is about and is keen to know more, it has done its job.

It should be concise - no longer than two pages at most - and interesting. It's advisable to write this section of your plan after you have completed the rest.

What is it not?

- A brief description of the business and its products. It's a synopsis of the entire plan.
- An extended table of contents. This makes for very dull reading. You should ensure it shows the highlights of the plan, rather than restating the details the plan contains.
- Hype. While the executive summary should excite the reader enough to read the entire plan, an experienced investor or businessperson will recognise hype and this will undermine the plan's credibility.

Your business, its products and services

If you want other people to invest in your business or if you're writing your plan to focus your existing business activities, you must be able to clearly convey what your business does.

This part of the plan sets out your **vision** for your new business and includes who you are, what you do, what you have to offer and the market you want to address.

Start with an overview of your business:

- when you started or intend to start trading and the progress you have made to date
- the type of business and the sector it is in
- any relevant history - for example, if you acquired the business, who owned it originally and what they achieved with it
- the current legal structure
- your vision for the future

Then describe your products or services as simply as possible, defining:

- what makes it different
- what benefits it offers
- why customers would buy it
- how you plan to develop your products or services
- whether you hold any patents, trademarks or design rights
- the key features of your industry or sector

Remember that the person reading the plan may not understand your business and its products, services or processes as well as you do, so try to avoid jargon. It's a good idea to get someone who isn't involved in the business - a friend or family member perhaps - to read this section of your plan and make sure they can understand it.

Your markets and competitors

In this section you should define your market, your position in it and outline who your competitors are. In order to do this you should refer to any market research you have carried out. You need to demonstrate that you're fully aware of the marketplace you're planning to operate in and that you understand any important trends and drivers.

You should also be able to show that your business will be able to attract customers in a growing market despite the competition.

Key areas to cover include:

- **your market** - its size, historical data about its development and key current issues
- **your target customer base** - who they are and how you know they will be interested in your products or services
- **your competitors** - who they are, how they work and the share of the market they hold
- **the future** - anticipated changes in the market and how you expect your business and your competitors to react to them

It is important to know your competitors' strengths and weaknesses as compared to your own - and it is good practice to do a competitor analysis of each one. Remember that the market is not static - your customers' needs and your competitors can change. So, as well as showing the competitor analyses you have undertaken, you should also demonstrate that you have considered and drawn up contingency plans to cover alternative scenarios.

Marketing and sales

This section should describe the specific activities you intend to use to promote and sell your products and services. It's often the weak link in business plans so it's worth spending time on it to make sure it's both realistic and achievable.

A strong sales and marketing section means you have a clear idea of how you will get your products and services to market.

Your plan will need to provide answers to these questions:

How do you plan to position your product or service in the market place?

Who are your customers? Include details of customers who have shown an interest in your product or service and explain how you plan to go about attracting new customers.

What is your pricing policy? How much will you charge for different customer segments, quantities, etc?

How will you promote your product or service? Identify your sales methods, eg direct marketing, advertising, PR, email, e-sales.

How will you reach your customers? What channels will you use? Which partners will be needed in your distribution channels?

How will you do your selling? Do you have a sales plan? Have you considered which sales method will be the most effective and most appropriate for your market, such as selling by phone, over the internet, face-to-face or through retail outlets? Are your proposed sales methods consistent with your marketing plan? And do you have the right skills to secure the sales you need?

Your people

Give details of your workforce in terms of total numbers and by department. Spell out what work you plan to do internally and if you plan to outsource any work. Other useful figures might be sales or profit per employee, average salaries, employee retention rates and productivity.

Your plan should also outline any recruitment or training plans, including timescales and costs.

It's vital to be realistic about the commitment and motivation of your people and spell out any plans to improve or maintain staff morale.

Your operations

Your business plan also needs to outline your operational capabilities and any planned improvements. There are certain areas you should focus on.

Location

- Do you have any business property?
- What are your long-term commitments to the property?
- Do you own or rent it?
- What are the advantages and disadvantages of your current location?

Production facilities

- Do you need your own production facilities or would it be cheaper to outsource any manufacturing processes?
- If you do have your own facilities, how modern are they?
- What is the capacity compared with existing and forecasted demand?
- Will any investment be needed?

Management-information systems

- Have you got established procedures for stock control, management accounts and quality control?
- Can they cope with any proposed expansion?

Information technology (IT)

- IT is a key factor in most businesses, so include your strengths and weaknesses in this area.
- Outline the reliability and the planned development of your systems.

Financial forecasts

As part of your plan you will need to provide a set of financial projections which translate what you have said about your business into numbers.

You will need to look carefully at:

- how much capital you need if you are seeking external funding
- the security you can offer lenders
- how you plan to repay any borrowings
- sources of revenue and income

You may also want to include your personal finances as part of the plan at this stage.

Financial planning

Your forecasts should run for the next three (or even five) years and their level of sophistication should reflect the sophistication of your business. However, the first 12 months' forecasts should have the most detail associated with them.

Include the assumptions behind your projection with your figures, both in terms of costs and revenues so investors can clearly see the thinking behind the numbers.

What your forecasts should include

Cashflow statements - your cash balance and monthly cashflow patterns for at least the first 12 to 18 months. The aim is to show that your business will have enough working capital to survive so make sure you have considered the key factors such as the timing of sales and salaries.

Profit and loss forecast - a statement of the trading position of the business: the level of profit you expect to make, given your projected sales and the costs of providing goods and services and your overheads.

Sales forecast - the amount of money you expect to raise from sales.

Your forecasts should cover a range of scenarios. New businesses often forecast over-optimistic sales and most external readers will take this into account. It is sensible to include subsidiary forecasts based on sales being significantly slower than you are actually predicting, with one for sales starting three months later expected, and another forecasting a 20 per cent lower level of sales.

Risk analysis

Alongside your financial forecasts it is good practice to show that you have reviewed the risks your business could be faced with, and that you have looked at contingencies and insurance to cover these. Risks can include:

- competitor action
- commercial issues - sales, prices, deliveries
- operations - IT, technology or production failure
- staff - skills, availability and costs
- acts of God - fire or flood

Presenting your business plan

To make sure your business plan has maximum impact, there are a number of points to observe.

Keep the plan **short** - it's more likely to be read if it's a manageable length. Think about the **presentation** and keep it professional - even if you only intend to use the plan in-house. Remember, a well presented plan will reinforce the positive impression you want to create of your business.

Tips for presenting your plan

- Include a cover or binding and a contents page with page and section numbering.
- Start with the executive summary.
- Ensure it is legible - make sure the font is ten point or above.
- You may want to email it, so ensure you use email-friendly formatting.
- Even if it is for internal use only, write the plan as if it is intended for an external audience.
- Edit the plan carefully - get at least two people to read it and check that it makes sense.
- Show the plan to expert advisers - such as your accountant - and ask for feedback. Redraft sections they say are difficult to understand.

- Avoid jargon and put detailed information - such as market research data or balance sheets - in an appendix at the back.

Make sure your plan is **realistic**. Once you have prepared your plan, use it. If you update it regularly, it will help you keep track of your business' development.

Suggested Reading List

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