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## ABSTRACT

This instructor guide for a unit on business plans in the PACE (Program for Acquiring Competence in Entrepreneurship) curriculum includes the full text of the student module and lesson plans, instructional suggestions, and other teacher resources. The competencies that are incorporated into this module are at Level 1 of learning--understanding the creation and operation of a business. Included in the instructor's guide are the following: unit objectives, guidelines for using PACE, lists of teaching suggestions for each unit objective/subobjective, model assessment responses, and overview of the three levels of the PACE program. The following materials are contained in the student's guide: activities to be completed in preparation for the unit, unit objectives, student reading materials, individual and group learning activities, case study, discussion questions, assessment questions, and references. Among the topics discussed in the unit are the purposes of business plans, why and when they should be developed, who develops them, what they contain, and why they are important. A sample business plan that includes a description of the business and marketing, organization, operations, management, and financial plans is presented. (MN)

# INSTRUCTOR GUIDE

## Unit 5 The Business Plan Level 1

### HOW TO USE PACE

- Use the objectives as a pretest. If a student is able to meet the objectives, ask him or her to read and respond to the assessment questions in the back of the module.
- Duplicate the glossary from the *Resource Guide* to use as a handout.
- Use the teaching outlines provided in the *Instructor Guide* for assistance in focusing your teaching delivery. The left side of each outline page lists objectives with the corresponding headings (margin questions) from the unit. Space is provided for you to add your own suggestions. Try to increase student involvement in as many ways as possible to foster an interactive learning process.
- When your students are ready to do the *Activities*, assist them in selecting those that you feel would be the most beneficial to their growth in entrepreneurship.
- Assess your students on the unit content when they indicate they are ready. You may choose written or verbal assessments according to the situation. Model responses are provided for each module of each unit. While these are suggested responses, others may be equally valid.

UNIT 5  
LEVEL 1

**PACE**  
THIRD EDITION

Program for Acquiring Competence in Entrepreneurship

CENTER ON EDUCATION AND TRAINING FOR EMPLOYMENT  
COLLEGE OF EDUCATION  
THE OHIO STATE UNIVERSITY

Research & Development Series No. 301-5

### Objectives:

- List the reasons for having a business plan.
- Identify the components of a business plan.
- Discuss the importance of a business plan.

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## Objectives

## Teaching Suggestions

### 1. LIST THE REASONS FOR HAVING A BUSINESS PLAN

What is a business plan?

Explain the importance of *planning* in business. Start with a simple example to teach students how to plan for their day-to-day activities. Next, address the concept of *risk* associated with a new business venture. This will help students understand the important role that planning plays in the start up of a new business.

What should you do before writing a business plan?

Define the concept of *opportunity analysis* using simple business start-up ideas (e.g., before opening a new auto repair shop in a small town, the entrepreneur should analyze the market demand to determine if the business has a fair *opportunity* to succeed).

Why and when should you develop a business plan?

Emphasize the importance of the business plan for getting the business started as well as for future operations. Employ the term *roadmap* to suggest the guiding role of the business plan.

Who develops the business plan?

Use a chalkboard or overhead to make a list of financing sources available to the entrepreneur. Include personal savings, funds borrowed from family, friends, acquaintances, investors, banks, agencies, etc. Explain that entrepreneurs are able to borrow money only if their business plans convince the investors that the business idea is worth of taking a risk.

Introduce concepts such as entrepreneurship, goods and services, profit and loss, sales, expenses, finances, etc. Keep your explanations short, and use simple business examples to help students understand the meaning of these concepts.

### 2. IDENTIFY THE COMPONENTS OF A BUSINESS PLAN

What is in the business plan?

Describe the business idea presented in the Lemon-Aid case. Use a chart to list the six major sections of a business plan (i.e., description of the business, the marketing plan, the organization plan, etc.). Check off each section as you explain it.

What is our business?

Select volunteers to offer their understanding of the business idea behind the Lemon-Aid case.

What is our plan for marketing?

Divide the chalkboard or transparency into seven sections. In each section, include one of the questions listed in the text in the Marketing Plan section (e.g., "What is our product?" "Who will buy our product?" etc.). Divide the class into seven teams. Teams are to answer the question assigned to them. Compare the answers of your students with those presented in the text, and provide them with feedback.

## Objectives

## Teaching Suggestions

How shall we organize?

In simple terms, explain the concept of partnership. Highlight the fact that each partner is liable for the actions of all partners. Also explain how partners are liable in real-life situations, when the business is not able to meet its financial obligations.

How will we produce and deliver our product?

Use the above suggestion to address the production and operations plan.

What management skills will be required?

Use a chalkboard or an overhead to list the management functions in a small business (i.e., operations, marketing, general, and financial management).

Will we make a profit?

This is an opportunity to employ all of your teaching "arsenal" while assisting students in understanding the basics of the financial plan. The key is to use several simple numerical examples to help students acquaint themselves with the concepts of estimated sales, costs of goods sold, gross profit, operating expenses, etc.

Use and explain the accounting formulas presented in the text (e.g.,  $\text{Sales} - \text{Costs of Goods Sold} = \text{Gross Profit}$ ). Only after students feel comfortable with the meaning and use of these formulas, should you proceed with introducing the financials in the Lemon-Aid case.

Finally, use a chart to explain the simple income statement presented in the case. Explain the interchangeable use of the terms *profit and loss statement* and *income statement*.

### 3. DISCUSS THE IMPORTANCE OF A BUSINESS PLAN

Why is the business plan important?

Finalize the Lemon-Aid case by reviewing the questions presented in the text. Have students respond to them using the information given in the case.

### MODEL ASSESSMENT RESPONSES

1. The primary reason for developing a business plan is to create a *roadmap* for the start-up and future operations of your business. Because entrepreneurs must invest their money, energy, and time to start a business, they need to plan for it carefully. In addition, should the entrepreneur need capital, investors and lenders must see a solid business plan before they will extend loans.
2. The major sections of the business plan are the description of the business, marketing plan, operations plan, organization plan, management plan, and financial plan.

The description of the business section outlines the type of business proposed, and briefly assesses the products and services that will be provided.

The marketing plan describes in detail the product, advertising, sales methods, potential customers, location, and competition.

The operations plan details the development of the product or service, i.e., what materials are needed, sources for materials, type of manufacturing process, etc.

The organization plan refers to the legal form the business will take (e.g., sole proprietorship, partnership, or corporation).

The financial plan assesses the profitability of the business. This section should convince investors of the need for money, how you will spend the money, when the business will become profitable, etc.

3. The purpose of developing a projected income statement is to show cause to expect that the business will become profitable in the future. Conversely, the income statement could show that the business may incur losses immediately after the start-up. The word "projected" means that the entrepreneur "anticipates" the profitability of the business. This projection should be based on a thorough market analysis and not on "hunches."
4. A correct response should take the following form:

How shall we attract customers?—b)

What shall we sell?—b)

What is the competition?—b)

How much will it cost to get started?—c)

Is additional money needed?—c)

What will our expenses be?—c)

Who will buy our product or service?—b)

What will our sales volume be?—b) and c)

Where shall we locate the business?—b)

Does the business promise to be profitable?—c)

How shall we organize our business?—d)

Who will be our general manager?—e)

Shall we organize as a partnership?—d)

Who will be in charge of the finances?—e)

Who should we develop our product?—a)

**PACE**  
THIRD EDITION

## Program for Acquiring Competence in Entrepreneurship

Incorporates the needed competencies for creating and operating a small business at three levels of learning, with experiences and outcomes becoming progressively more advanced.

**Level 1** — Understanding the creation and operation of a business.

**Level 2** — Planning for a business in your future.

**Level 3** — Starting and managing your own business.

Self-contained **Student Modules** include: specific objectives, questions supporting the objectives, complete content in form of answers to the questions, case studies, individual activities, group activities, module assessment references. **Instructor Guides** include the full text of each student module and lesson plans, instructional suggestions, and other resources. **PACE, Third Edition, Resource Guide** includes teaching strategies, references, glossary of terms, and a directory of entrepreneurship assistance organizations.

For information on PACE or to order, contact the Publications Department at the  
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The  
Business Plan

Your Potential  
as an  
Entrepreneur

Nature of  
Small Business

Business  
Opportunities

Global Markets

Help for  
the  
Entrepreneur

Types of  
Ownership

Marketing  
Analysis

Location

Pricing  
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**PACE**  
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Competence in  
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CENTER ON EDUCATION  
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THE OHIO STATE UNIVERSITY

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Research & Development Series No. 301-5

# THE BUSINESS PLAN

## BEFORE YOU BEGIN . . .

1. Consult the *Resource Guide* for instructions if this is your first PACE unit.
2. Read What are the Objectives for this Unit on the following page. If you think you can meet these objectives now, consult your instructor.
3. Look for these business terms as you read this unit. If you need help with the meaning, ask your instructor for a copy of the PACE Glossary contained in the *Resource Guide*.

Cost of goods sold

Financial plan

Gross profit/Gross margin

Income statement/Profit and loss statement

Management plan

Marketing plan

Net profit

Operating expenses

Operations plan

Opportunity analysis

Organization plan

Profit/Loss

Target market

## THE BUSINESS PLAN

### WHAT ARE THE OBJECTIVES FOR THIS UNIT?

Upon completion of this unit you will be able to—

- list the reasons for having a business plan,
- identify the components of a business plan, and
- discuss the importance of a business plan.

### WHAT IS THIS UNIT ABOUT?

This unit introduces you to the *business plan*—a key document if you are considering entrepreneurship. A business plan is required by banks, loan agencies, or individuals who might consider lending you money for starting your business. It is absolutely necessary to help future small business owners plan on paper the course of their business.

You will learn why the business plan is so important to your business, who should develop it, and when it should be developed. Furthermore, you will examine the parts of a business plan by reviewing the activities of a group of young people as they plan their own business.

Understanding and learning how to write a business plan involves putting together all you know about running a business. Financial analysis, business financing, operations, marketing, management of human resources,

and legal issues—all have to be included in a business plan.

### WHAT IS A BUSINESS PLAN?

A *business plan* is a written statement that specifies the *goals* of the business and *how* these goals will be achieved. A complete business plan should give answers to the following questions:

- Who is the entrepreneur and what does he or she want to do?
- Who are the partners, if any?
- Where should be the business located?
- What is the product the proposed business will market?

- Why did the entrepreneur choose that product?
- Why does the entrepreneur believe the business is profitable?
- When will the business start to become profitable?
- Will the business remain profitable in the future?
- What are the costs to start the business?
- Who will be the customers?
- How will the product be promoted?
- How many employees will be needed, how will they be trained, and how will they be rewarded for their work?

### **WHAT SHOULD YOU DO BEFORE WRITING A BUSINESS PLAN?**

Developing a business plan is time consuming and, most often, requires help from professional business consultants. Before investing time and money in preparing a complete business plan, it is essential to closely study your product and customers. This step, which should always precede the business plan, is called *opportunity analysis*.

Without this study it is impossible to make a sound decision or even proceed with writing a business plan. (For more information

on business opportunities, turn to PACE Unit 3, Business Opportunities.)

### **WHY AND WHEN SHOULD YOU DEVELOP A BUSINESS PLAN?**

A business plan helps you organize your thoughts and focus your efforts and your objectives. The plan forces you to create and analyze strategies for reaching those objectives. The business planning process also helps you identify weaknesses in your ideas and plans **before** you actually commit your time and money to them.

Developing a business plan before attempting to start a business is crucial. The business plan is a roadmap to owning and operating a small business. As a future entrepreneur, you must work out the details of every part of the proposed company. You need to collect information carefully and put your findings on paper. After you have prepared the business plan, you will learn whether you will be able to make a profit, and when this is likely to happen. You will also see the need on paper for changes that can avoid costly mistakes before the business opens.

The business plan is even more important if you need to borrow money or seek investors to get your business going. Bankers, loan agencies, or individuals will want to study your plan to see if your business promises to be profitable. Only then will they consider lending you money or investing in your company.

You should understand that planning for your business is a key factor for your future business success. The business plan will give you a guide to follow even after you start the business. It is important to realize that once a business plan is written, it is not cast in stone. In fact, every business plan needs to be updated as the business moves forward. This is because no matter how well you plan, unexpected events will occur requiring you to reconsider your plan and adapt it to new situations.

## WHO DEVELOPS THE BUSINESS PLAN?

Do you remember running a lemonade stand in your neighborhood when you were a child? Most of us recall a time when we were caught up in the excitement of organizing our own little "business." Maybe your project involved joining your pl ymates and presenting a play or variety show for your parents and friends. Or perhaps you and other young friends prepared a neighborhood newsletter, or collected old clothes and had a rummage sale, or sold Girl Scout cookies. All of these "businesses" were forms of entrepreneurship. Although the "play" projects produced the side benefits of fun and learning to work together, you were probably inspired by the chance to put your talents to work to "make some money."

Your fund-raising project was a business that sold *goods* (lemonade, old clothes, cookies) or *services* (delivering newspapers, carrying groceries, lawn mowing) to customers (parents, relatives, neighbors) for a *profit* (the money left after you paid your expenses). Even though you didn't know it then, you

were an *entrepreneur*—a person who invests money, energy, and time in a business in hopes of making money. As an entrepreneur, *you* are responsible for developing the business plan for the business that you want to open.

## WHAT'S IN A BUSINESS PLAN?

Let's identify the parts of a business plan by reviewing the activities involved in setting up a lemonade stand in Jonathan Spivey's front yard on a hot June day. What Jonathan and his friends did to get the business going are what every entrepreneur should do before opening a new business. The difference is that Jonathan's business is a simple one, and that fact should make the business planning process easier to understand. The activities of Jonathan and his friends show the different parts of a business plan.

On a particularly hot day three enterprising youngsters were very thirsty. They thought that other people were perhaps also thirsty for an ice-cold, refreshing glass of lemonade. Maybe the other people would be willing to buy the lemonade from them!

The three friends were Jonathan Spivey, Kathy Merritt, and Joey Wiltshire. Here is their story, told as the parts of a business plan.

## SAMPLE BUSINESS PLAN\*

### WHAT IS OUR BUSINESS?

**Part One: Description of the Business.** As Jonathan and his friends drank the lemonade that Jonathan's mother made for them, Jonathan said, "Hey, you guys, if we get some paper cups we might be able to sell this stuff out front under the big oak tree. I'll bet we could make some money."

That was the marketable idea that launched a business planning venture in Centerville, Kentucky. They decided to investigate the possibility of selling lemonade to other thirsty people.

### WHAT IS OUR PLAN FOR MARKETING?

**Part Two: The Marketing Plan.** The three young entrepreneurs probably didn't know that they were developing a marketing plan to get people to buy their product. However, that is exactly what they did as they answered the following questions:

- **What is our product?**

All the hot, thirsty people who see our business will buy the lemonade. They will remember their own lemonade stand and will want to give us kids a boost. We're going to offer a cold, refreshing drink—lemonade—under a cool shade tree!

This is how our product will benefit the customers. By selling our lemonade, we will satisfy their thirst and offer a cool, relaxing spot to rest for a few minutes.

- **Who will buy our product?**

Whom are you trying to attract and serve? That is, who is our *target market*? All the hot, thirsty people who see our business under a cool shade tree. All the passersby who remember their own lemonade stands and want to give us kids a boost.

- **Where should we locate our business?**

We need to pick a spot that makes it easy for people to buy our product. The large oak tree stands near a busy intersection, so traffic from two directions will see our stand. There is plenty of parking space on both streets for customers to stop without danger. The nice shade will be inviting on a hot day.

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\* To obtain additional sample business plans, contact the Distributive Education Clubs of America (DECA) at 1908 Association Drive, Reston, VA 22091-1594.

- **How can we attract customers?**

We've got to think of a way to letting people know we're in business and what we can do for them. Therefore, we'll need a name for our company. Why don't we call it "Lemon-Aid?" We know how to spell lemonade, but we want to catch the customer's eye. We need a sign on both streets. We need a sign high enough on the oak tree to be seen over traffic. We need chairs for customers to sit in while they drink.

We also need a sign on the lemonade stand. Then we need to get a large box and paint it yellow and pink. This will be our building. Our advertising signs will say:

1. BUY YELLOW AND PINK "LEMON-AID" FROM THE KIDS
2. TAKE HOME A GALLON OF "LEMON-AID" FOR THE FAMILY

- **What is our competition?**

It is important to know who else is offering people a product to meet the same need that we are trying to meet and how their offer compares to ours. The nearest soft drink place is the gas station four blocks down Faulkner Avenue. They don't have any shade, or any homemade lemonade in two colors, or any cute kids selling it. The drug store is situated 10 minutes away from your location at a busy intersection.

- **How much should we charge for our product?**

We have to consider how much people might be willing to pay for our product, how much our competition charges for their product, and what it costs us to provide our product.

The gas station charges 55 cent for a can of soda pop. The drug store charges 89 cents for an 12-ounce glass of lemonade. We probably can't charge more than 35 cents for a 6-ounce cup of lemonade if we expect to attract customers. We'll have to figure out how much it will cost us to make our lemonade and serve it.

- **What advice do we need?**

We should not open a business without seeking advice from experienced people who can help us make good decisions. Let's talk to our parents and ask their opinions about our plans.

## HOW SHALL WE ORGANIZE?

**Part Three: The Organization Plan.** We will organize our business as a partnership. All three of us will contribute money from our personal savings and we will all work. We will make decisions together and we will split the profits at the end. We will also be responsible for any losses.

## HOW WILL WE PRODUCE AND DELIVER OUR PRODUCT?

**Part Four: The Operations Plan.** We need to consider what will be required to produce and provide the product to our customer. We need to know how we will make the lemonade and what will be needed to serve it to the customer.

We also need to get Jonathan's mom's lemonade recipe and decide what ingredients we should buy, how much of them to buy, how to make the lemonade, and who will make it. Finally, we will buy the cups in which to serve the lemonade and we will set up a stand from where we will do business.

## WHAT MANAGEMENT SKILLS WILL BE REQUIRED?

**Part Five: The Management Plan.** Even though we did not realize it right away, we understand now that a good management team is the key to our business success. Common sense tells us there are certain responsibilities that have to be taken care of if we want to succeed.

We will need to figure out what tasks we entrepreneurs need to perform. We need someone to oversee buying the lemons, sugar, ice, and water, as well as making the lemonade. Jonathan said he'd been helping his mom make lemonade for 3 years now. He knows where to get the ingredients at good prices. Jonathan will be our *operations manager*.

We also need someone to be responsible for figuring out how much lemonade we can sell, at what price, and how we will attract customers. Kathy has a flare for selling and had been marketing director for her 4-H club's fair project. We'll have her be our *marketing manager*.

Another need is for someone to make sure all managers are working together toward common goals. This task requires good organization skills. Joey is our class leader and he is a member of the school counsel. He is very good at helping and leading people. He will be our *general manager*.

Finally, we need someone to handle our finances. But none of us knows anything about finance.

(Having found an area of responsibility where none of them had any knowledge, they decided to ask one of their parents for help. Kathy's father works for an accounting firm in downtown. He offered to help the kids develop the *financial plan*.)

## WILL WE MAKE A PROFIT?

**Part Six: The Financial Plan.** Their kids' parents were interested in learning more about the lemon-aid project. Kathy's parents offered to lend them folding chairs. Jonathan's parents offered space in the refrigerator to store a gallon jug of lemonade. They also offered a styrofoam chest for storing ice and lemonade near the stand. However, the parents wanted more information about the company's finances. They realized that they would probably be asked to become investors, and they wanted their children to learn from the experience.

A financial plan would help them determine in advance how much *net profit* (money left over after all expenses have been paid) they would have at the end of the summer. With Mr. Merritt as financial consultant, they estimated how much profit the business might be able to make.

Investors in a business want to know the answers to two major questions answered in the financial section:

- How much profit can the business make?
- How much money do you need to get the business started and to keep it going until you make a profit?

Decisions about the first question are made by studying a *projected income statement* for the business. An *income statement* shows the results of your business operations. More precisely, the income statement includes *sales* (i.e., how much money you earn from selling your product) and *expenses* (i.e., how much money you spend to keep your business going). The final result on the income statement shows the company's profit (or loss) during the period (i.e., whether money was made or lost from selling the product). A *projected income statement* guesses at sales and expenses for a future period, or how profitable a business will be.

Kathy's father shared the formulas below to help the lemon-aid entrepreneurs estimate their profit (or loss) for the 2 months that the business would operate:

$$\begin{array}{r} \text{Estimated Sales} \\ - \text{Cost of Goods Sold} \\ = \text{Gross Profit} \end{array}$$

$$\begin{array}{r} \text{Gross Profit} \\ - \text{Operating Expenses} \\ = \text{Net Profit} \end{array}$$

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Mr. Merritt guided the lemon-aid partners through each step of the formulas. His method was to ask them questions about their plans. The following sections show the process used to determine how much profit the business would make.

**Estimated Sales.** The *sales* figure is all the money that customers are expected to spend on your product and services during the period covered by the income statement.

**Question:** How many customers do you expect to attract during the 2 months? How much will they buy?

**Answer:** We will count on an average of five customers an hour. We will be open 6 hours a day for 2 months (60 days). Therefore, we can expect 1,800 customers over a 2-month period (5 customers an hour x 6 hours a day x 60 days = 1,800 customers). If we serve 6-ounce cups, the customers will buy approximately 1.41 gallons of lemonade a day (5 customers an hour x 6 hours a day x 6 oz. a customer = 180 oz). Since there are 128 ounces per gallon, and the kids will sell 180 ounces of lemonade a day, they will sell approximately 1.41 gallons a day (180 oz./128 = 1.41 gallons).

Over two months, we expect to sell 84.6 gallons of lemonade in cups (1.41 gallons a day x 60 days = 84.6 gallons). We also expect to sell 5 gallons in bulk (whole gallons at one time) during the 2 months. Therefore, we expect a total of 89.6 gallons over 2 months (84.6 gallons in cups + 5 gallons in bulk = 89.6 gallons).

**Question:** How much will it cost to make that amount of lemonade?

**Answer:** We asked Jonathan's mother for the lemonade recipe. We shopped around at grocery stores for the best prices. We found it will cost \$7.39 to make and serve a gallon of lemonade.

24 lemons @ \$0.25 each	\$6.00
1 lb. sugar @ \$0.40	.40
21 6-oz. cups @ \$0.04 each	.84
food coloring and napkins	.10
<u>1/2 lb. ice @ \$0.10 lb.</u>	<u>.05</u>
Total cost per gallon	\$7.39

**Question:** How much will you need to charge for lemonade?

**Answer:** With 1 gallon of lemonade, we can fill 21 6-ounce cups (128 oz/6 oz a cup = 21.3 cups). It will cost \$.352 to make a 6-ounce cup of lemonade (\$7.39/21 cups per gallon = \$.352 per cup).

We have already checked our competitors' prices. Remember that the gas station charges 50 cents for a 12-ounce soft drink and the local drug store fountain charges 89 cents for a 12-ounce lemonade.

We had hoped to charge 35 cents for a 6-ounce cup. Obviously, if it costs approximately 35 cents to make a cup, then we will have to add enough to cover expenses and make a profit. We really doubt if 60 cents per cup is enough to produce a profit, but our advisors think that most customers will not pay more.

**Question:** What will your sales volume be at a selling price of 60 cents per cup?

**Answer:** We estimate our total sales volume for the 2 months to be \$1,120.00.

30 cups per day x 60 days x \$0.60 per cup	=	\$1080.00
<u>5 gallon @ \$8.00</u>	=	<u>40.00</u>
Estimated Sales	=	\$1120.00

**Cost of Goods Sold.** Mr. Merritt explained that *cost of goods sold* is the value of raw materials and other products that are actually used in producing the finished products. In this case, the costs of goods sold include the cost of sugar, lemons, food coloring, napkins, ice, and cups that are actually used for producing the lemonade over 2 months. The calculation is made as follows:

Beginning Inventory	
+ Purchases	
- <u>Ending Inventory</u>	
= <b>Cost of Goods Sold</b>	

*Inventory* refers to the raw materials (in our case the lemonade ingredients and cups) purchased by a business to produce goods or services. Inventory might also include the finished goods purchased for resale to customers (e.g., snicker bars, if the kids also sold snickers along with the lemonade). The kids do not have any *inventory at the beginning*. They will purchase the necessary lemonade ingredients and other items (cups, ice, and napkins) which make up the *purchases* in our formula. We will assume that the kids will sell all the lemonade they produce and use all their inventory by the end of the second month, so they will have no *ending inventory*.

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**Question:** How much will the lemonade ingredients and other items cost?

**Answer:** The kids will need to spend \$662.14 for the lemons, sugar, food coloring, napkins, and ice. This is the total dollar amount of the goods sold.

$$\begin{aligned} 89.6 \text{ gallons} \times \$7.39 \text{ per gallon} &= \$662.14 \\ \text{Cost of goods sold} &= \$662.14 \end{aligned}$$

**Gross Profit.** *Gross profit* is also called *gross margin*. This is all the money you make from sales before you subtract any operating expenses. Mr. Merritt explained that gross profit is figured by subtracting the value of the cost of goods from the estimated sales. Lemon-aid is planning to sell 89.6 gallons of lemonade for a total amount of \$1,120.

**Question:** What is your gross profit?

**Answer:** Our gross profit will be \$457.86.

Estimated sales	\$1120.00
- <u>Cost of goods sold</u>	- <u>662.14</u>
= <b>Gross profit</b>	= <b>\$ 457.86</b>

At this point, the lemon-aid partners became worried about whether it was worth continuing with the project. Mr. Merritt insisted that they complete the *projected income statement* before deciding, so they continued.

**Operating Expenses.** *Operating expenses* summarize the amounts paid out to keep the business running. The operating expenses usually are rent, repairs, salaries, telephone, electricity, and other expenses that a business must pay for to be able to produce goods and services. We should note that the operating expenses are another type of expenses *different* from costs of goods sold. In our case, the operating expenses the kids have are their salary and advertising expenses.

**Question:** How much will your operating expenses be?

**Answer:** We planned to pay a small wage to the person working the stand (50 cents per hour). We will need to replace our advertising posters once during the two months.

Salaries and wages (360 hours @ \$.50 an hour) (60 days x 6 hours x \$.50 per hour = \$180.00)	\$180.00
Advertising and promotion (4 sheets poster board @ \$1.00 = \$4.00)	<u>4.00</u>
Total Operating Expenses	\$184.00

**Net Profit.** Now the lemon-aid entrepreneurs had arrived at the bottom line of the income statement. The *net profit* is the difference between the gross profit and the operating expenses. It tells you whether our business shows a profit or a loss. This explains why the income statement is also called a *profit and loss statement*.

**Question:** How much is your net profit?

**Answer:** After subtracting the operating expenses from the gross profit, we have \$273.86 net profit to divide among the three of us.

Gross profit	\$457.86
<u>Operating expenses</u>	<u>184.00</u>
Net profit	\$273.86

The projected income statement that Jonathan, Kathy, and Joey prepared for their parents is shown below.

<b>PROJECTED INCOME STATEMENT</b>		
<b>for "LEMON-AID"</b>		
(Jonathan Spivey, Kathy Merritt, Joey Wiltshire)		
July 15, 1993 through September 15, 1993		
Sales		\$1120.00
<u>Less: Cost of goods sold</u>		<u>662.14</u>
Gross profit		\$ 457.86
<u>Less: Operating expenses</u>		
Salaries	\$ 180.00	
Advertising	<u>4.00</u>	
Total operating expenses		\$ <u>184.00</u>
Net profit		\$ 273.86

## WHY IS THE BUSINESS PLAN IMPORTANT?

The would-be lemon-aid owners saw that the business appeared to offer enough potential profit to make further steps worth the effort.

The business planning experience was helpful for Jonathan, Kathy, and Joey; they learned an important lesson in entrepreneurship. The lesson taught them that no matter how good an entrepreneur's idea might be, you need to plan to see if it will be profitable. Now, the three entrepreneurs are able to correctly respond to the questions?

- What is your business?
- What are you able to do by yourselves to start and keep the business running?
- What are the responsibilities of each one of the three young entrepreneurs?
- What kind of assistance do you need and how will you obtain it?
- How much money do you need to spend to make and sell the lemonade?
- How should you price the lemonade?
- How should the lemonade be advertised?
- Who will be the customers?
- How profitable will the business be at the end of three months?

An important conclusion should follow the lemon-aid business plan. The business plan is a tool designed to help you find and explore opportunities. It also provides you with a way to analyze *potential* opportunities continuously. A business plan is *personal* and should never be "canned" or prepared professionally. No one knows you or your ideas better than you do. It is the *process* of seeking the answers to important questions about your enterprise that are important as you try to realize the dream of owning your own business.



## ACTIVITIES

The following activities are designed to help you apply what you have learned in this unit.

### INDIVIDUAL ACTIVITIES

#### A.

On a separate sheet of paper, identify and briefly describe a business that you know about. Correctly identify the product or service that is sold. Try to explain what unmet needs the product or service satisfies. Next, specify the market the product/service serves (i.e., who are the customers). Finally, discuss how the product/service competes in the market (i.e., by quality, price, location, selection, novelty, innovation, etc.).

#### B.

Choose a business idea similar to the lemonade stand in the text (e.g., selling old clothes or cookies, delivering newspapers, lawn mowing, etc.). Try to come up with a projected income statement following the lemon-aid model in the text. Use a step-by-step approach to calculate your gross profit, cost of goods sold, and net profit. Does your business idea appear to be profitable?

## GROUP ACTIVITIES

#### A.

For a small business to be successful, the owner must know the market. Analyzing the market is a way to gather facts about potential customers and to determine the demand for your products or services. The following questions will help collect the information necessary to analyze the market and determine if the product or service will sell. Divide the class into groups of four to six. First, groups are to choose a business they are familiar with (e.g., a bakery store, a computer service shop, etc.). Next, each group should answer the following questions:

1. Do you know who their customers are?
2. Do you understand their needs and desires?
3. Do you know where they live?
4. Does the business offer the kind of products or services that they will buy?
5. Are the prices competitive in quality and value?

Finally, groups should to share their findings.

#### B.

Divide the class into groups of four to six. Each group should record methods that businesses in your community use to attract customers. In their discussion, students should include items such as price, quality, selection, location, technical features, design, packaging, services, etc.

## CASE STUDY

Marlin O'Brian has always loved tailoring. As a little girl, she used to visit the dry cleaner across the street almost every day. The dry cleaner was owned by Marlin's neighbor, Ms. Smith. Ms. Smith was surprised to see how interested Marlin appeared to be in watching the two employees make minor repairs and adjustments to the clients' clothes. As Marlin grew older, Ms. Smith started to teach her how to use the sewing machine in the dry cleaner store.

While in high school, Marlin proved herself to be a fast learner. She majored in clothing and participated in several fashion design competitions organized by high schools in the community. Marlin won awards on sev-

eral occasions surprising her parents and teachers with her talent and hard work. Marlin's clothing instructor encouraged her to participate in other fashion design shows organized in surrounding towns.

Marlin will graduate from high school next month. She has already talked to her parents about opening a small fashion store in the neighborhood. Her parents appeared to be supportive of Marlin's plans. However, they suggested she continue her education in a fashion academy and maybe go to college to specialize in fashion design. Marlin would like to start using her talents to make money, but she realizes there is so much more she needs to learn.

## DISCUSSION QUESTIONS

1. What would you recommend Marlin do after her graduation?
2. What are some skills Marlin exhibited throughout her life? Do you believe these skills are enough for her to open a fashion design business?
3. What kind of training do you think Marlin still needs?
4. How would you explain to Marlin the importance of a business plan?

## ASSESSMENT

Read the following questions to check your knowledge of the topics presented in this unit. When you feel prepared, ask your instructor to assess your competency on them.

1. Explain the primary reason for developing a business plan.
2. Enumerate and briefly explain the major sections of the business plan.
3. What is the purpose of developing a projected income statement?
4. Identify the parts of a business plan by matching the parts in the right-hand column below with the questions in the left-hand column. Place the correct letter from the right column on your sheet. The parts may apply to several questions.

- |  |                      |
|--|----------------------|
| <input type="checkbox"/> How shall we attract customers?             | a. Operations Plan   |
| <input type="checkbox"/> What shall we sell?                         | b. Marketing plan    |
| <input type="checkbox"/> What is the competition?                    | c. Financial plan    |
| <input type="checkbox"/> How much will it cost to get started?       | d. Organization plan |
| <input type="checkbox"/> Is additional money needed?                 | e. Management plan   |
| <input type="checkbox"/> What will our expenses be?                  |                      |
| <input type="checkbox"/> Who will buy our product or service?        |                      |
| <input type="checkbox"/> What will our sales volume be?              |                      |
| <input type="checkbox"/> Where shall we locate the business?         |                      |
| <input type="checkbox"/> Does the business promise to be profitable? |                      |
| <input type="checkbox"/> How shall we organize our business?         |                      |
| <input type="checkbox"/> Who will be our general manager?            |                      |
| <input type="checkbox"/> Shall we organize as a partnership?         |                      |
| <input type="checkbox"/> Who will be in charge of the finances?      |                      |
| <input type="checkbox"/> How should we develop our product?          |                      |

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## PACE

	Unit 1.	Your Potential as An Entrepreneur
	Unit 2.	The Nature of the Small Business
	Unit 3.	Business Opportunities
	Unit 4.	Global Markets
⇒	Unit 5.	The Business Plan
	Unit 6.	Help for the Entrepreneur
	Unit 7.	Types of Ownership
	Unit 8.	Marketing Analysis
	Unit 9.	Location
	Unit 10.	Pricing Strategy
	Unit 11.	Financing the Business
	Unit 12.	Legal Issues
	Unit 13.	Business Management
	Unit 14.	Human Resources
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	Unit 16.	Selling
	Unit 17.	Record Keeping
	Unit 18.	Financial Analysis
	Unit 19.	Customer Credit
	Unit 20.	Risk Management
	Unit 21.	Operations
		Resource Guide
		Instructor's Guide

Units on the above entrepreneurship topics are available at the following levels:

- \* Level 1 helps you understand the creation and operation of a business
- \* Level 2 prepares you to plan for a business in your future
- \* Level 3 guides you in starting and managing your own business