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Some essentials for startups relating to finance and cost management

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Abstract
There has been a paradigm shift in doing business because of the coronavirus epidemic, and the war between Ukraine and Russia. War-like tensions are persisting and germinating among other countries. Besides initiatives like Standup India, Make in India, Vocal for local and global, One District One Product, Skill India, Ease of living, etc., have given impetus to youth and other industrialists to start their own. All these, taken together, have given birth to various start-ups, and some have become unicorns. This paper aims to provide critical points that may be useful to venture capitalists, researchers, and academicians. The paper focuses on the finance area, more specifically on cash inflows and outflows, raising the finance and explaining some tools and techniques relating to the cost management relevant to the startups (namely Activity-based costing, Zero-based budgeting, the importance of classification of cost, and Break-even point. The paper provides some suggestions on the relevance of proper budgeting, the relevance of cash inflows and outflows, and emphasis on using these costing techniques by the owners of the start-ups, Proper classification of costs between fixed and variable costs, and using the break-even analysis for effective management of startups.

Keywords: Startups relating, finance, cost management

Introduction
Startups and new business ideas always play an important role in the growth and development of the country. Its importance increases many folds in a highly populated country like India. For the success and sustainability of a startup, cost, and finance is one of the important aspects that must be analyzed in detail by the start-up owners. In a country like India, where there is always a scarcity of resources, the founders, (Along with details of the product, feasibility of the product, market analysis, challenges of ever-changing demand and supply dynamics, and competitors challenges) must make a thorough study about the cost and financial dynamics for the startups to sustain. Along with business ideas, startups need money to remain in the business for a longer period of time.

Startups are business ventures started by startup founders and/or venture capitalists to fulfill a marketplace need by providing an innovative product/process/service or combining these three. Startups have gained faster growth in the last ten years, especially in India. Many of them have achieved the title of unicorns in India.

Startups are ventures that disrupt (Or are a big threat to) existing similar types of industries because they come out with new innovative products/processes/services by introducing them at a large scale, hence changing the world. If they are successful, their valuations go up to the sky. Investors (Venture capitalists) in these startups look for heavy returns to get back the capital invested and make huge profits either by sale or by initial public offering (IPO).

Objectives of writing this paper
The objective of writing this paper is to provide critical points for sustaining startups for a longer period by thoroughly analyzing critical reasons that may become reasons for the discontinuation or shutdown of business. It will not only be valuable for founders but also academicians, researchers, and venture capitalists.

Scope
The scope of this article is to stick to the finance area, more specifically to cash inflows and outflows, raising the finance and explaining some tools and techniques relating to the cost

management relevant to the startups (namely Activity-based costing, zero-based budgeting and the importance of classification of cost, Break-even point).

Activity Based Costing

Profit can be increased either by having higher revenue or by reducing the cost. Increasing revenue depends on increasing price per unit or increasing sales. Both are external factors that are not under the control of the company. Another facet of increasing profit is the reduction in cost. Proper cost determination helps in price fixation. This is a big riddle for the startup founders to fix the proper price of the products or services they offer. In this regard, Activity-based costing can be helpful. The cost of the product can be reduced by eliminating unproductive activities. Activity-based costing helps in identifying relevant cost drivers which help in reducing the cost of cost object. Various examples of unproductive activities can be 1) hiring a celebrity for advertisement 2) high cost of selling personnel 3) extravagant decoration in the shop, and 4) costly and big space for display. Initially, startups have a cash crunch therefore, it becomes all the more important to identify unproductive activities involving cash outflows. The startup founders should give special emphasis on identifying these activities from the beginning.

Zero Base Budgeting

Zero-base budgeting is a tool that can be very useful to startups. It is an approach where resources are allocated based on a zero base to the particular division/product or process. It takes into account that every rupee invested is based on the company's priority, hence ensuring the effective utilization of resources. In a way, it is equivalent to having a clean slate and writing on it fresh. The founders should be very clear with respect to the identification and sharpening of objectives, critical examination of various alternative ways of attaining these objectives, and selecting the best alternatives through cost-benefit analysis. Had it not been a case of a startup, the founders would have had an opportunity to challenge all historical data and create a budget based on the current future projections for sales and fixed and variable expenses. It is the zero-base budgeting tool that helps the founders draft a realistic budget with a fresh start.

Classification of Costs

The owners of start-ups need to understand the behavior of various costs. These costs may be classified as fixed and variable costs. The classification is paramount to comprehend the firm's financial flexibility. Some of the fixed or overhead costs remain static, such as rent and employees' salaries over a period of time, while other costs vary based on the business activity, such as material, labor cost, and marketing expenses. Founders need to minimize fixed costs to the minimum as it lowers the Break-even point (BEP) and also the cash break-even point. The founders should strive to achieve BEP as early as possible to have financial flexibility. Both types of these break-even points generate information for decision-making, especially financial planning and budgeting.

Deeply understanding the inflow and outflow of cash

A proper understanding of the inflow and outflow of cash is highly significant to ensure that the financial health of a startup remains sound over a long period. This requires framing of budgeting to pinpoint its short-term needs. Proper liquidity is necessary all the time to meet short-term requirements like salaries, rent, interest payments, and instalments of loans taken. Founders are required to understand the cash management techniques to develop accurate budgets. There are some specific ways to keep intact the inflow and outflow of cash listed below:

1. Minimum cash reserves should be maintained. It is suggested to keep a minimum cash balance for at least for few months to meet urgencies like, a slowdown in operation, hurried borrowings, and unexpected contingencies like lockdowns, floods, hurricanes, strikes, and supply chain logistic delays.
2. High risk is associated with high rewards. But startups start fresh and have a shortage of available cash most of the time. To meet this requirement interest debt is high leading to high risk. Research has shown approximately 50% of small businesses meet their financing needs, while about 30% fail on account of paucity of money. Therefore, it is imperative on the part of founders to opt for the lowest interest rate and keep an open eye on restructuring debt leading to a lower rate of interest and increasing the duration of interest, which should free up the organization's cash flows.
3. It is highly recommended to keep the reserves for the provision of contingencies. Startups dealing with Information technology that are likely to have foreign exchange transactions with foreign-based clients must secure themselves from the fluctuations of foreign exchange.
4. Small businesses and startups do face the challenge of invoicing and collection of payment from their clients making availability of cash difficult. Therefore, it is essential for startups to have high efficiency by sending invoices timely and initiating a rapid collection process. An aggressive policy should be followed in the recovery of late payments.
5. Another way to increase the availability of cash is to negotiate and renegotiate payment terms with suppliers and creditors to extend the duration of the payments.
6. Better cost management is a crux for startups. Founders should consistently strive to identify the areas where costs can be effectively and efficiently managed, thereby improving the cash position. For example, reduce the size of the place. Cost reduction brings down the per-unit cost.
7. Precise financial projections and planning are called for better cash flow management. If possible, they should be compared with actuals to find out the deviations and prompt corrective action to be taken by the managers of the startups.
8. Constant efforts are required to tap the other market rather than depending upon a single customer or market, this will reduce the risk associated with cash inflows.
9. Startup managers should keep abreast of the latest changes in the market and try to predict the likely changes to determine the significant impact on the startup and in case it is materially affecting them, contingencies provision should be made. For example, floods, road closures, earthquakes, lockdown-like extremities and recession in the economy, Political instability, Procedural delays, etc.

10. Start-ups must make provisions or some mechanism to reinvest some portion of the profit into the expansion of the business so that the financial position of the business will become strong as early as possible. This will help them to face the adversities, if any, in a better way. Moreover, this policy will help in reducing the burden of interest on debt over a period of time. As a result, the financial position of the business remains sound and it will help in the long-term stability of the start-ups.
11. Slow moving and dormant stock must be disposed of early so that space will be available for new stocks.

To make the journey of a startup successful, founders must use the right tools, techniques, and strategies of financial management thereby reducing the impact of challenges.

Financial management is concerned with the procurement and effective utilization of funds. One of the techniques of financial management is to have a business line of credit. The line of credit is actually a floating borrowing limit that one can obtain and repay flexibly at any time. Adopting this technique is effective utilization and procurement of funds, whenever, there is a need. Ways to ease the financial burden of starting the business

Let us discuss the various funding options available to start-up owners:

1. By the owners themselves and obtaining funds via credit lines.
2. Friends and family – the advantage is that they lower interest rates as compared to banks; the disadvantage is the chances of having conflict with them.
3. Small business loans can obtained from banks/online lenders/Non-profit lenders etc. You must know your credit history. One needs to be fully organized, and transparent and must have an answer as to why the loan is needed and plans to use it i.e., for expenses or business infrastructure. One needs to develop the startup business report based on financial numbers, growth, the company's leadership and services, details of products and services, and mission statement.
4. Angel investing – refers to private investors going for financing small business ventures in exchange for equity.
5. Crowd funding refers to raising a small amount of money from a large number of people. The essentials of crowd funding are promoting the startup plan at the right place with the right audience and creating marketing materials.
6. Startup incubators are places that offer facilities, expertise (Legal and accounting), mentorship, and tools to support early-stage companies.
7. Government grants and subsidies can be obtained. The owners of startups must be aware of the schemes that the government comes out with to promote innovations on a commercial scale.

Founders may consider buying the used equipment to fulfil initial requirements from the market for old devices. For example, they may prefer a one or two-year-old item depending on the quality of the item and its sustainability.

One should opt for leasing rather than buying an expensive plant, or machinery, which is likely to save money in the short term. Cost cost-benefit analysis of buying equipment etc., vs. lease should be done.

In the fast-changing world, do not be over-enthusiastic to quickly build your team. Start from the beginning by hiring the right people for the required place. The ultimate aim should be to trim the labour cost so that the finances can be controlled.

Startup managers should consider forming partnerships with other persons, especially entrepreneurs in the same area and if possible look for bartering or trading to each other's requirements. This is a win-win situation and the right approach for all the parties in the situation.

Insurance is one the important expenses in every business be it a start-up or small or big business. It provides financial protection in a number of areas. Managers should decide what kind of insurance is needed and for whom it is needed.

Manage your time carefully – one must learn to appreciate the value of his time. Partners of startups may spend countless hours to save a little money and end up hurting themselves in the end.

Ways to leading to reduction of cost

- Establish a Budget – Make short-term and long-term plans to identify the likely shortages of cash flows also the possibility of saving.
- Reduce rent – of workspace size or having a remote team to reduce the cost.
- Create a paperless work environment- this will reduce the paper cost, printing, digital documentation, digital bills, and correspondences, etc. are needed.
- Outsourcing multiple tasks as an alternative – to integrating with other businesses, data preservation, and analysis, etc.
- Use of trial periods before purchasing software which will reduce the cost.

Suggestions

- Activity Based Costing becomes an important tool for start-ups to decide which activity to add from the beginning so that costs can be reduced especially when there is a dearth of funds.
- Founders of startups must take a challenge in preparation of a budget which should take into consideration the company's priority so that the finances available be used effectively and efficiently. A deep understanding of specific ways to keep cash inflows and outflows intact is essential.
- Every cost should be identified and classified as fixed and variable cost. Proper classification is essential to calculate Simple BEP, Cash BEP, and Financial BEP.
- All funding options available must be explored and analysed.
- Hiring only the right and required people is of utmost importance. Insurance if needed be done for important assets (Plant and machinery etc.). Emphasis should be given to reduce the cost from the beginning.

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