

PHASE 3

PLAN ENTERPRISES FOR SUSTAINABLE DEVELOPMENT



BOOKLET E

Community-based
tree and forest
product enterprises:
**Market Analysis
and Development**

BOOKLET E

PHASE 3:
PLAN ENTERPRISES
FOR SUSTAINABLE
DEVELOPMENT

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Introduction

The primary **objective** of this phase is to formulate a plan for growth of the future enterprise, develop the strategy for the enterprise and initiate the action steps that will prepare the way for implementation.

In Phase 3, entrepreneurs are assisted in working out an enterprise development plan for their product by analysing the data obtained so far. Entrepreneurs will describe the mission of the enterprise, formulate the goals and objectives, develop the strategy of the future enterprise, draw up an action plan, assess the enterprise's profitability, determine capital start-up needs and use the plan to obtain financing. In this phase facilitators learn about tools that the entrepreneurs can use to assess changes in the business environment and to monitor the progress of their enterprise in order to adapt the plan accordingly. This will ensure that they continually identify and solve problems as they arise, so they can limit their risk and remain competitive.

The development of a plan for tree and forest product enterprises comprises eight main steps, listed in Box E.1.

BOX E.1

Phase 3: Steps in planning enterprises for sustainable development

- STEP 1** Examine the business environment of the selected product(s)/enterprise
- STEP 2** Define the enterprise mission, goals and objectives
- STEP 3** Develop strategies in each of the four areas of enterprise development
- STEP 4** Formulate the action plans to implement the strategies
- STEP 5** Calculate financial projections for the enterprise
- STEP 6** Obtain financing
- STEP 7** Initiate the pilot phase and training
- STEP 8** Monitor progress and deal with change

The outputs to be expected from this phase are:

- formulation of the enterprise strategy for selected products;
- development of an action plan;
- financing, as specified in the capital needs statement; and
- implementation of a monitoring and planning system.

Preliminary planning activities

Before starting Phase 3, it is necessary to organize a team, draw up a time schedule and plan a budget.

Organize the team

The team comprises representatives of the interest groups formed at the end of Phase 2, who are assisted by facilitators and, when required, by business analysts with experience in financial planning for small enterprises.

Draw up a time schedule

The time required for further steps involving financing of the enterprise depends on the complexity of the process. Overall, the entire process for Phase 3 can take at least two months if it involves several interest groups and formal registration.

The major activities in Phase 3 consist of workshops in which group members participate as they work out the details of their enterprise strategies and action plans. In most cases, a workshop of only three or four days is sufficient for a facilitator to assist one medium-sized producer group to develop the concept of enterprise development. However, when several interest groups are developing the same product, as in the honey producers example taken from the Quang Binh, Viet Nam, case study, representatives from all the groups need to meet and develop overall strategies for coordination. Thus the amount of time needed for this process will depend partly on the number of groups that are planning to federate, and partly on communication difficulties and the distances the representatives have to travel in order to meet.

After developing overall strategies, the representatives need to go back to their groups and go over the proposed plan in order to ensure that all members are in agreement. At the same time, the financial details of the enterprise development plan can be worked out by a team of selected group members and facilitators on the basis of the strategies proposed by the groups. Eventually, an additional workshop among representatives of the groups will have to be organized in order to finalize the details and develop the action plan.

The steps related to obtaining financing may involve formal registration of the enterprise in order to qualify for bank loans. This is a step that may be lengthy, depending on the local situation. Setting up the management systems for the enterprise will also take time. In some cases, the pilot phase in Step 7 can be utilized as a way of saving time. Some forms of financing (such as grants through a supporting organization) may simply involve initially setting up temporary systems and testing them through one season of collection and production before formalizing them in a more lengthy process.

Plan a budget

The main expenses for Phase 3 involve organizing planning workshops, and, in some cases, contracting the expertise that may also be needed to develop the financial plan. Some interviews with key direct or indirect actors may also be needed in order to confirm information obtained on the product in Phase 2.



STEP 1 | Examine the business environment of the selected product(s)/enterprise



In Phases 1 and 2, the facilitator assisted the target group in gathering information on the four areas of enterprise development at community, national and/or international levels in order to select a product initiative. This formed the basis for the analysis of the business environment for the product that takes place in Phase 3. The focus at this point will be on examining the specific factors that influence the marketing of the product, such as information on the relevant market (size, growth, consumer behaviour, trends), and on other factors, such as social, cultural and economic conditions, resource base status, and political and technological trends. This analysis enables the facilitator to assess the constraints within the sub-sector, the obstacles that need to be overcome, and the most effective strategies to enable the producers to obtain more equitable benefits from marketing the product.

The objective of this step is to assess the context within which products will be developed, with the aim of developing an enterprise strategy that addresses the opportunities and constraints identified in the business environment for that enterprise.

How to examine the enterprise environment

The enterprise environment is the interrelationship of factors in the four areas of enterprise development of tree and forest products. These factors influence the demand, production, processing and distribution of products or commodities. They are also known as critical success factors, which are the fundamental conditions that have to be satisfied if the enterprise is going to be competitive, sustainable and equitable.

The target group should examine the enterprise environment before initiating its enterprise, and on the basis of that information it should develop realistic goals and objectives to ensure the profitability of its enterprise.

Although facilitators and the target group have already gathered information on the product during Phase 2, more specific information is now needed.

Issues to be included in the analysis

The following is a checklist of issues that should be assessed during Step 1 of Phase 3.

▲ MARKET/ECONOMY ANALYSIS

- potential markets (customers) for the product (how large and how diverse are they, and where are they located?)
- competitors and their pricing policies, market strategies and relative share of the market (see competitor analysis example in Table E.1)
- constraints in marketing the product
- current market channels and proposed channels of distribution
- potential strategic alliances and partnerships

▲ RESOURCE MANAGEMENT/ENVIRONMENT ANALYSIS

- resource availability, volumes and rates of sustainable extraction
- seasonal cycles of production
- existing community management systems for the resource

▲ SOCIAL/INSTITUTIONAL ANALYSIS

- institutions that can support the enterprise
- the legislative environment for the enterprise

▲ SCIENCE AND TECHNOLOGY ANALYSIS

- appropriate technology available for adding value to the product through quality improvements that satisfy customer requirements

Competitor analysis

The competitor analysis is one of the tools that can be used in the market analysis in Step 1 to identify strengths, weaknesses, opportunities and threats (SWOT). Once the target group has gathered detailed information about the business environment for its product, it can compare its enterprise idea to existing enterprises in order to determine the nature of the challenges that it will face. The SWOT analysis identifies strengths, weaknesses, opportunities and threats. Strengths and weaknesses often address the internal factors governing an enterprise, while opportunities and threats refer to external forces in the business environment. An example of this type of analysis is given in Table E.1.

TABLE E.1 Competitor analysis using SWOT (strengths, weaknesses, opportunities, threats) in the Quang Binh, Viet Nam, case study

SWOT	THE HONEY PRODUCERS OF MINH HOA/TUYEN HOA	COMPETING COMPANY
Strengths	<p>Potential access to supplies of low-priced and high-quality raw materials</p> <p>Technical and extension aspects that can easily be solved</p> <p>Low investment, low production costs and high potential for profitability</p>	<p>Sophisticated research and development and marketing linkages, as well as strong capital base</p> <p>High-quality production</p> <p>Centrally located production units close to markets and ease of adaptation to customer preferences</p>
Weaknesses	<p>Lack of knowledge regarding marketing channels and customer preference</p> <p>Locations in rural areas distant from market centres and difficulty of obtaining packaging supplies</p> <p>Lack of processing technology</p>	<p>Inability to meet the expanding market demand</p>
Opportunities	<p>Increasing domestic and export markets, with prospects for the development of a domestic niche market for pure, natural, certified honey as a gift and also for use in the women's health care sector</p> <p>Opportunities for substitution of imports of Australian and Spanish honey into Viet Nam</p> <p>Training of small-scale beekeepers to produce export quality honey of the proper moisture content</p> <p>Possible linkages with larger wholesalers of honey in order to acquire technology and market information</p>	<p>Well-established distribution channels</p> <p>Possibility of exporting honey in bulk, giving larger manufacturers an advantage over small-scale producers</p>
Threats	<p>Requirements of foreign buyers for low moisture content, which limits growth of this market</p> <p>Difficulty of market penetration, which can only be achieved in export markets through high quality, standardization and respect of contracts</p> <p>Eventual dependence of producers on only one major buyer</p>	<p>Competition from many countries for selling honey to European markets</p>



STEP 2 | Define the enterprise mission, goals and objectives

The objective of this step is to formulate the enterprise development plan. The various elements of this plan are listed below. To formulate an enterprise development plan, the members of the interest groups combine all the information and the analysis they have done thus far on a potential product. They then organize this information to produce a summary report that briefly describes the enterprise and convincingly demonstrates that it is a good investment choice, that the product is competitive, that it fills a defined customer need, and that sustainability issues such as those of resource management and sociological aspects have been addressed. This exercise then becomes a participatory event to be repeated on a seasonal or annual basis in order to monitor the interest group's achievements, to identify problems and to plan the next steps.

First, the facilitator should organize a workshop in which the members of the target group use the information gathered thus far on their selected product to formulate the mission, goals and objectives of their enterprise. These three concepts provide an outsider with the information that clearly illustrates what the enterprise is all about.

An enterprise development plan minimizes the possibility of failure and maximizes the likelihood of success by:

- encouraging the target group to think carefully about each phase of the business;
- gathering information to make an informed estimate of the probability of success and the degree of risk;
- committing thoughts and ideas to paper so that they can be evaluated both personally and by an outsider;
- examining the strengths and weaknesses of the business relative to its competitors;
- evaluating the feasibility of the concept and identifying the specific factors that will determine success or failure;
- formulating realistic, attainable goals; and
- maintaining an ongoing process of gathering and examining information, planning objectives, implementing strategies and controlling (monitoring) progress.

This analysis is particularly important when seeking financing, since the target group must demonstrate to the financier:

- a clearly defined business concept;
- a working knowledge of the major functions of the enterprise;
- a clear understanding of the industry, market and competitive environment in which the enterprise will operate, and a plan for exploiting the opportunities that have been identified;
- a realistic estimate of the financial needs of the venture; and
- convincing and well-documented arguments for why and how the business will succeed.

As a result of this exercise, the target group will achieve a good understanding of how the enterprise will work and of what it can expect. It provides the group with a framework within which it can:

- identify and assess changes that take place in the business environment on an annual basis;
- develop strategies for adapting to changes that affect the enterprise;
- properly manage the business by using the plan as an operating tool;
- use the enterprise plan as a reference with which to measure progress made towards objectives;
- provide an opportunity for participation by the community members on an annual basis; and
- use the plan as a tool for obtaining financing from a bank, an investor or a donor, such as a development project.



Elements of an enterprise development plan

In conventional business planning there are several models for how to convey the information about a business to an outsider. However, in order to simplify this presentation and adapt these models to the smaller scale of most tree and forest product enterprises, the following elements should be included:

- ☐ overview of the enterprise;
- ☐ business environment;
- ☐ mission statement;
- ☐ goals;
- ☐ objectives;
- ☐ strategies;
- ☐ action plans; and
- ☐ financial plan.

Overview of the enterprise

The overview of the enterprise can combine the functions of executive summary and enterprise description. It should mention everything that is important in the enterprise development plan in one or two pages. In many cases, the people who read the plan will read only this section. If they need additional information, this section shows them where to find it. The overview draws from all the other elements in the enterprise development plan in order to summarize clearly the basic nature of the enterprise. It provides a brief description of the business environment in which the enterprise will operate; it states the mission of the enterprise; it describes the opportunity that the enterprise is exploiting; it identifies the enterprise participants and describes their expectations for themselves and for the enterprise; and it answers the questions of what their stake in the enterprise is, of how they share the benefits, of how they manage the enterprise, and, finally, of what is unique about the enterprise or its products, compared to those of existing competitors.



HOW TO PREPARE AN OVERVIEW

To draft an overview at the beginning of the planning process, the facilitator should organize a workshop with the members of the interest group and list the critical issues concerning the success of the enterprise. The target group should be encouraged to review the information obtained from previous phases. Special attention should be given to the economic objectives of the target group as formulated in Phase 1, Step 2; the identification of opportunities and constraints that was made during the selection of the most promising products in Phase 2, Step 2; and the information on the business environment that was obtained in Step 1 of Phase 3.

The final version of the overview should be written when the enterprise development plan has been completed, since it is a synopsis of the entire plan. The facilitator therefore needs to organize one more session with the target group to review the entire enterprise development plan, including the financial plan, and use that to finalize the overview.



EXAMPLE

An overview of the enterprise: case study of the honey producers of Minh Hoa/Tuyen Hoa, Quang Binh, Viet Nam

The honey producers are farmers from communes in the districts of Minh Hoa and Tuyen Hoa. They are unable to produce enough grain to meet the minimal consumption needs of their families. Malnutrition and diseases associated with inadequate diet are widespread. As the possibilities of increasing staple food production are limited, the farmers expect that the additional income from this enterprise will allow them to purchase more food and eliminate their dietary deficiencies.

The group sells honey and beeswax, a by-product of beekeeping, extracted according to methods learned during technical training provided by the Integrated Food Security Project (IFSP), Quang Binh. The enterprise consists of groups of five farmers, which are later to federate into a larger marketing unit. The small-scale groups purchase the equipment that will enable them to produce high-quality honey. They target honey wholesalers in the domestic market. The honey is produced in an organic way, and no chemical pesticides are to be spread in the area where the bees collect pollen. In order to maintain quality, the number of hives per ha are to be limited so as not to exceed the absorption capacity of an area.

The honey producers are unique among honey enterprises for the following reasons.

- The honey interest groups expect to raise the economic standards of the local population and will thus be committed to conserving and protecting their forest resources. In the future they envision further benefiting the communities by federating with other groups, which will increase their scale and enable the development of a brand name for the large group of honey producers from the four communes. This will then make it profitable to invest in a refinement and packing unit.

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- The honey enterprises are expected to have a positive impact on the environment, as no chemical substance will be dispersed in the environment in order to avoid killing the bees. This will also contribute to the biological diversity of plants through increased pollination.
- Competition is seen as a positive trend that will be encouraged through this enterprise by increasing the capacity of the farmers to become real economic actors, and will result in quality improvements among them.

The goal for the first year was for the group to purchase the equipment needed for production by using some of its own share capital and by obtaining a loan for the remainder. The plan forecast that with income from the total production of the group's 35 hives, the entire loan would be paid back within the first year, while still leaving enough working capital to cover the enterprise's overhead for the following year.

The enterprise targets domestic niche markets, such as women's health and gift markets, in addition to traditional users and tourist markets, by producing natural honey that is certified as organic and is differentiated from 'industrial' honey. It will gradually also target mass markets, aiming to substitute imported honey from Australia and Spain and to identify export destinations for high-quality honey. This will become possible once the group has acquired more experience and has developed good links with buyers, and once several groups federate into larger units.

The IFSP initially gave some support in order to ensure the enterprise's long-term goals and sustainability. One member of the group is responsible for quality control and monitors adulteration. One group member was to undertake a market study tour. Institutions at the national level that can provide training, technical assistance and extension support were to be identified. Women's participation was to be encouraged by ensuring that some of the group members are female and are involved in decision-making and sharing of benefits.



Business environment

The following is an example of the business environment for honey from the Quang Binh, Viet Nam, case study.



EXAMPLE

The business environment for honey

Domestic production and market

The total production of honey in Viet Nam in 1997 was 4500 tonnes, of which 3500 tonnes were exported. Currently, domestic knowledge about the quality of honey is increasing, and people are taking an interest in the moisture content. The domestic market absorbs 1000 tonnes, a figure expected to reach 2000 tonnes in the year 2000. The main domestic market is in urban areas, such as Ho Chi Minh City, Ha Noi, Vung Tau and Dong Nai.

The export price is much lower than the domestic price. The export price ranges from US\$950 to \$1450 per tonne, while the domestic price is about \$1.54 to \$3.07 per kg. The price for some honey originating near tourist sites such as Cuc Phuong National Park reaches \$5 per kg from the farmer. This is because the local culture puts a very high value on honey as a medicine for purposes of health, and for women's health care especially. It is also considered a valuable gift for relatives at festival time. The packed and labelled type is sometimes regarded as the 'industrial' type, having lost its natural qualities. Therefore, prospects for development of a niche market of pure, natural, certified honey for the domestic market, as well as for a larger, well-packed and well-labelled production of high-quality honey, are good. The technical and extension aspects of increased production could be solved quite easily in Viet Nam, since technical, training and research institutions exist at national level. However, much support is needed for developing the marketing channels and for organizing and training producers to respect market and quality requirements. Although no records are available, a significant quantity of honey from Australia and Spain is imported into Viet Nam. These imports could easily be substituted by local production, if proper quality control and proper purification and packing operations were in place.

Foreign market

Viet Nam exported 3500 tonnes of honey in 1997. Vietnamese honey is liquid in form, and this is the form preferred in most countries. The type of honey (composition, colour, botanical source, stage and form of processing) and its price depend on the country of destination. For example, German consumers prefer dark honey, which would be used in other countries only for industrial purposes. Foreign demand is higher for single-flower honey than for wild honey. Foreign consumers accept the organoleptic qualities and flavour of honey originating in Viet Nam, but moisture content is a problem. Export-quality honey is produced only by *Apis mellifera* because it easily meets the maximum moisture content requirement for export (20 to 21 percent). The quality could be improved if small-scale beekeepers could be trained in the aspects of quality standards, since the market image of Vietnamese honey has suffered recently as a result of the production of adulterated honey. Viet Nam exports to Europe, main-

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ly Germany, France, the United Kingdom, Switzerland, the Netherlands and Italy, and to the United States of America. The demand for high-quality honey from Viet Nam could reach 10 000 tonnes per year (it is presently 3500 tonnes), less than 5 percent of European consumption, estimated at 238 709 tonnes in 1993.

From 1989 to 1993 the production of honey in the European Union (EU) averaged 100 000 metric tons per year, with Germany, Spain, France, Greece and Italy as the largest producers. At the same time, imports have increased steadily from non-EU countries that are traditional producers, such as Argentina (26 percent), China (24 percent) and Mexico (21 percent), but also from new competitors such as Cuba, Uruguay, Hungary and Poland. Most of the honey imported into Germany originates in developing countries, and part of this is exported once it is refined and retail-packed. Low-quality honey is used for industrial purposes, such as confectionery, bakery products and pharmaceuticals.

Many factors lead producing countries to export honey in bulk rather than in pre-packed form. Retail packaging of honey is not an economically viable undertaking in many developing countries, because good-quality retail packaging costs are usually lower in the importing countries. Weight and freight costs are higher, and technical problems (such as crystallization) that cannot be corrected may arise if the honey is pre-packed. Good honey may be spoiled by poor storage and transport, and the interval between production and sale should be kept to a minimum. Market penetration can be achieved only by ensuring the high quality of the product, by delivering honey of the same standard as that provided in samples, and by respecting the terms of the contract.

This enterprise is characterized by the following opportunities.

- A relatively low investment is required in order to get started.
- Production costs and labour requirements are low.
- Two products (honey and beeswax) can be derived from one production process.
- Demand is large, and the products have high market value.
- Honey production is a speciality of the district and there is existing experience among the farmers.
- The enterprise is adapted to the local ecosystem.
- There are no legal restrictions.
- Equipment is simple and the technology is appropriate, while it is also easy for the farmers to obtain from supporting institutions the technical knowledge required for extraction and processing.

Formulate the mission statement

The mission statement answers the question: What is the enterprise? It is developed in order to describe the enterprise and clarify its purpose in order to communicate it to people both inside and outside the enterprise.

The mission statement uses the information obtained in Steps 1 and 2 of Phase 1 to define the target group and the economic objectives of its enterprise. It also addresses cultural, gender and sustainability issues. In addition, the mission statement points out the enterprise's main activities, the type of customer to be targeted, the kind of service that will be offered, the unique qualities of the enterprise and the customer needs that will be satisfied by the product.

HOW TO FORMULATE A MISSION STATEMENT

The facilitator should assist the interest group by using a participatory approach to help the members work together to develop the mission statement. This will ensure that they feel a sense of ownership about the mission statement because they are involved in the process of its formulation. The mission statement is a general statement that helps to provide a conceptual framework for goals, objectives and strategies.

The facilitator organizes a workshop in which all the group members are present, and asks them to make a list of the following:

- the enterprise's main activities and the kinds of products that it offers;
- the number and kind of enterprise participants and their expectations regarding the enterprise over the next few years;
- the things that the enterprise does that distinguish it from others; and
- the kinds of customers to be targeted.



If a mission statement is prepared, the enterprise participants should ensure that the objectives and strategies that they develop always conform to the mission. For example, if the participants in the enterprise agree that their honey will be organic, and that they will promote this feature in order to distinguish it from the competition, then they have to ensure, year after year, that they do not begin to use pesticides on the land in the areas where the bees collect pollen. There might be temptations in the future to use pesticide in order to increase their profits (for instance, if insects were damaging some of the flowering plants), but this strategy would not conform to their original mission statement. Instead of using pesticides, they might need to get additional technical assistance in order to explore the possibilities of integrated pest management solutions.

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The following are two versions of mission statements for a bamboo toothpick factory in Laos. In the first version, the statement is general and vague. The second version more specifically defines the enterprise and its aims both to ensure customer satisfaction and to provide income and employment to skilled local people. Unlike the vague statement in the first version, it also gives the reader the impression that strategies will actually be developed for taking into consideration natural resource management.

Version 1: To manufacture and market toothpicks in local and international markets by involving the local community in an environmentally sustainable manner.

Version 2: Through an established, reliable toothpick company in Laos, to consistently supply the requirements of its local and international buyers while helping to provide additional income and employment to skilled residents of Vientiane and of its adjacent village communities, within the context of sustainable resource management.



EXAMPLE

The mission statement in the Quang Binh, Viet Nam, case study

This enterprise, formed of small groups of farmers from Minh Hoa and Tuyen Hoa, aims to produce natural, organic honey and beeswax by using small-scale, village-based technology that ensures high quality. The enterprise is owned by all the group members and supplies its products to wholesalers, packaged in such a way that it maximizes convenience for them and addresses customer requirements. The future success and uniqueness of this enterprise are to be assured through measures aimed at maintaining a chemical-free environment in the areas where the bees collect pollen, so that flower production and biological diversity can be encouraged and quality can continually be improved.



Define goals

The goals define a particular course of action directed at reaching the destination spelled out in the mission statement. They are the general results that the enterprise expects to achieve. The facilitator can think of formulating a mission statement as being like planning a vacation and choosing the final destination, while developing the goals is like planning the itinerary to be followed in order to arrive at that destination. Goals should try to give the specific targets that the enterprise expects to achieve in a given period, in terms of sales, profits or numbers of employees. The goals should indicate the following:

- the number and kind of products and their position in relationship to those of competitors;
- the expected size, sales and target markets that the enterprise can reach; and
- the number of people who will be involved.

HOW TO DEFINE GOALS

Facilitators should ask the interest group to discuss what kind of product it wants to market. On the basis of its analysis of the business environment, its own capacity and the economic objectives it identified in Phase 1, it should make a realistic estimate of approximately what the volume of sales of that product could be within one or two years of starting the business. So that the enterprise can be worthwhile for the group, it should make sure that this volume is also enough to allow it to achieve its economic objectives. In addition, it should consider how much its volume of production and its sales could expand over the next three to five years. It will have to begin with some preliminary goals and further refine these as it goes through the successive stages in Phase 3 of strategy development and financial planning.



EXAMPLE

Goals in the Quang Binh, Viet Nam, case study

The group sells honey from beekeeping, extracted according to the methods learned during technical training and packaged in 650 cc bottles made of transparent glass. The members expected to begin with 35 hives in the first year and to produce 525 kg of honey and 175 kg of beeswax. They expected this to increase to 50 hives in the second year, producing 750 kg of honey and 250 kg of beeswax. They anticipated a return on investment at the end of the first year of 55.8 percent (net profits as a percentage of the initial assets invested).



Define objectives

Goals alone are not going to result in action. It is only through the formulation of objectives that the goals can be operationalized. Objectives provide the foundation on which the members of the target group can then prepare strategies and assign tasks. Objectives will also provide the solutions to problems and will exploit opportunities identified in previous exercises. These will ensure that the sales/profit goals are attained and will also take the mission statement into account. Again using the example of planning a vacation, the objectives are like the things that people want to see along the way at each stop on their itinerary, as they travel towards their final destination. Objectives have time limits assigned to them, so they provide a means for measuring progress.

HOW TO DEFINE OBJECTIVES

In the workshop, facilitators should encourage the members of the target group to think of specific and realistic objectives for the first year or two of the enterprise in the four areas of enterprise development. Facilitators should make sure that the objectives are linked to the goals and to the mission statement. Objectives, strategies and actions should be SMART (specific, measurable, appropriate, realistic and time-bound). The facilitator can have the workshop participants divide into four working groups, each representing one of the four areas, and ask each group to list objectives relevant to that area.



EXAMPLE

Objectives in the Quang Binh, Viet Nam, case study

▲ MARKET/ECONOMY

■ Products

Objective: In the first year, the enterprise was to develop high-quality honey for domestic markets, packaged according to the requirements of wholesale domestic and export buyers. Beeswax was also be sold as a by-product of honey production.

■ Price

Objective: To obtain a wholesale price for honey and beeswax that is competitive and aims for a break-even point of 172 bottles.

■ Place/Distribution

Objective: To develop links with buyers in targeted markets. To organize collection of the product from the five members of the interest groups. To assess possible long-term strategies for linking several honey producer groups in all four communes.

■ People

Objective: To identify the needs of the targeted buyers (wholesale distributors) and develop methods for maximizing their convenience in obtaining the product.

■ Promotion

Objective: To become recognized as a reliable supplier of quality natural and organic honey and honey by-products.

▲ **RESOURCE MANAGEMENT/ENVIRONMENT**

Objective: To supply honey without negative impact on the resource.

▲ **SOCIAL/INSTITUTIONAL**

■ **Gender issues**

Objective: To ensure that women have improved decision-making and share in the income benefits.

■ **Organizational structure for the enterprise**

Objective: To plan for an association of honey production groups from all four communes.

■ **Institutional support**

Objective: To make full use of existing support structures in order to accomplish the objectives in the enterprise development plan.

▲ **SCIENCE AND TECHNOLOGY**

■ **Research and development**

Objective: To ensure that production efficiency and quality requirements are maintained.





STEP 3 | Develop strategies in each of the four areas of enterprise development

The objective of this step is to develop specific strategies in each of the four areas of enterprise development. The product assessment that took place in Phase 2 will be taken a step further to enable the target group to take advantage of opportunities or overcome constraints in the business environment, and ensure that the business will be sustainable and equitable.

In MA&D, the enterprise strategy includes four areas of development (as outlined in Booklet B). Therefore, the market/economy strategy is supplemented by a resource management/environment strategy, a social/institutional strategy and a science and technology strategy.

- ▲ The **market/economy strategy** includes the '5 Ps' of the marketing mix: product, price, place, people and promotion. It also addresses strategic alliances that can effectively support marketing.
- ▲ The **resource management/environment strategy** includes the resource management options and the best partners for achieving them.
- ▲ The **social/institutional strategy** includes the relationships between the enterprise participants. It addresses methods for ensuring that decision-making and distribution of benefits are equitable and reach the intended target groups. It also includes the legal aspects regulating the enterprise as well as linkages with supporting institutions at all levels.
- ▲ The **science and technology strategy** includes the operational aspects linked to production and processing, in addition to the kinds of technology or research needed to add value to the products.



How can target groups formulate their enterprise strategy?

The target groups that were formed in Phase 2 will have met in a workshop to undertake Steps 1 and 2 of this phase. Step 3 can also take place in the same workshop. In Step 3, they will go over the data that was gathered and discussed during the product assessment phase. Participants should again bring up any suggestions that came up at that time for improvement in the marketing system of a product.

The group members can choose to break up into four working groups, and each group can choose to focus on one of the areas of enterprise development, as they did to formulate objectives. However, they will now try to formulate strategies for overcoming the constraints and taking advantage of the market opportunities that were previously identified for their product.

At the conclusion of their session, they should be able to make a list of their proposed strategies and of any additional information needs that they have, in order to be able to plan the methods and the cost of each strategy.

Market/economy strategy

The market/economy strategy ensures that the enterprise is taking advantage of opportunities and overcoming constraints in the business environment of a product. The two main areas to address when planning market/economy strategies are the marketing mix and strategic alliances.

The marketing mix

Also known as the '5 Ps', the marketing mix consists of the general areas of product, price, place, people and promotion. The various components of the marketing mix are used to motivate customers to purchase the product. The target group can use the marketing mix to specify how the product will be positioned in the market. During the annual planning cycle, the marketing mix becomes the basis for developing objectives and strategies that respond to changes in the business environment.

Each of the components of the marketing mix gives rise to some main issues, as follows.

PHASE 3: Plan enterprises for sustainable development
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PRODUCT

The enterprise may consider developing more than one of the product options described above, thereby creating a product mix. A well-balanced product mix ensures spreading out the risk factor over several different products and improves competitiveness by always offering new products to customers.

Product/market options There are four possibilities for a product. The facilitator can discuss these with the members of the target group and help them decide which combinations of product and market strategies are appropriate for their enterprises. Box E.2 illustrates the various possibilities for a product.

A product can be located in any of the four squares of the grid in Box E.2. Each of the four possibilities carries a different profit and risk factor, and different strategies are required in order to achieve results.

Product/market options		
Products	Markets and means of marketing	
	Existing	New
Existing	1 Existing/Existing	2 Existing/New
New	3 New/Existing	4 New/New

Marketing strategy decisions will vary according to which of the four options is chosen.

1 To continue making existing products for existing markets

To expand sales in the existing markets with the same product, the target group must:

- attract new customers;
- convince present customers to increase purchase (to 'increase orders');
- improve existing products;
- intensify promotion or information about the product (this is why companies have a sales force, why they advertise, and why they are concerned about 'brand recognition');
- improve quality; and
- adjust prices.

2 To continue making existing products and add new markets

New markets may be developed by:

- conducting a market study to discover new markets;
- studying new trends to identify emerging markets;
- searching for market niches (place);
- focusing on serving customers in a section of the market more efficiently or effectively than competitors; and
- investigating the export market.

3 To introduce new products to sell to existing markets or market channels

Sales of new products can be increased with an established customer base by:

- conducting a market study among established customers to find out their needs;
- conducting research and development to create new products; and
- conducting promotion targeted to the established client base.

4 To introduce new products to sell to new markets

New markets can be targeted with new products by:

- identifying a new product and the proper niche (clientele);
- conducting thorough research and development and pilot testing;
- conducting aggressive and well-designed promotion to enter a new market; and
- setting up strategic partnerships with distributors with networks in the targeted market.

**EXAMPLE****Risk options**

The option of **lowest risk** is to continue making the existing product and target existing markets. The means of marketing are improved, which results in **expanded sales of the product**. For example, in Nepal, options for the producers of medicinal plants were to continue selling dried plants to the district collector or to organize the storage of dried plants in a village store-room in order to improve the quantity and quality of supply and to overcome the seasonal production limitation.

An option of **moderate risk** is to continue making the existing product and **expand to new markets**. An example of this option would be for the producers of medicinal plants not only to sell their products to the district collector but also to expand the sales of the product by selling them to the national herbal processing company in the capital town.

Another option of **moderate risk** is to **introduce new products to existing markets**. A company that already has a well-established market will often use this option to convince its existing customers to try new products. In an example of this option, the factory that manufactured ten herbal medicines would produce new medicinal preparations for curing additional diseases and distribute them to the same customers.

PHASE 3: Plan enterprises for sustainable development

STEP 3: Develop strategies in each of the four areas of enterprise development

The market option of **highest risk**, but with the greatest potential profits, is the market strategy of **new products and new markets**. Successful green marketing is an example of a market strategy that offers new environment-friendly products to a new or emerging market niche. In an example of this option, the factory manufacturing herbal medicines would produce a new product, such as a herbal tea, for export to customers who are sensitive to environmental issues.

HOW TO DEVELOP A MARKET/ECONOMY STRATEGY

Facilitators will work with the following information gathered on the products in Phase 2:

- the cost of production of the goods and their shipping;
- the raw materials, skills and equipment necessary to produce the product or service according to what the consumers are buying;
- the designs, labels and packaging for the product or service that the target audience finds most appealing;
- the standards of quality in packaging and design that the market and government regulations require;
- stages of the product's life cycle (introduction, growth, maturity, saturation and decline); and
- the market testing strategy and the results of focus groups that have been communicated to the manufacturers (many new products fail in the marketplace because solutions to the problems are not found before the product is offered to customers).



EXAMPLE

Producer groups of medicinal plants in Nepal had the option of generating income from medicinal plants they collected from the forest (an example of the option of existing product to existing market) and, at the same time, they had the option of planting some other species (the option of new product to a new market) that would not yield income for several years but were needed by the district factory.



PRICE

It is often said that in a free market system the customer determines the value of the product. Therefore, to a great extent, price objectives are determined by the type of enterprise, its location, the target customers and the expenses of the enterprise. Before choosing a pricing strategy, the target group must be aware of the perception of the customer and the potential market values for the product. The data gathered using the market information system described in Phase 2 is therefore critically needed by the target group to make decisions on pricing.



Price determines how much profit is made. If prices are too low, the enterprise cannot cover costs; if prices are too high, there are not enough sales.

HOW TO DETERMINE PRICES

Facilitators will work with the following information from Phase 2:

- the prices that other businesses charge for the same or similar products or services;
- the price potentially paid by target customers for this product;
- total production, management and marketing costs; and
- the amount of profit needed from the business (after paying for production, management and marketing costs, how much additional money is wanted for distribution to business owners or re-investment in the business?).

FACTORS THAT INFLUENCE THE SETTING OF PRICES

The exercises in the financial plan in Step 5 show how to assess whether the profit margin is sufficient for a healthy business. If it is not, the target group either has to raise its prices or lower its costs. However, in addition to the profit margin, other factors that influence prices must be considered, such as customers, the prices set by the competition and the state of the economy.



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How to determine the profit margin

The price of a product should cover the following and still provide a profit margin:

- the cost of production of the goods and their shipping;
- the overhead costs of the business (including depreciation and financing charges);
- the salary of the members of the target group and staff; and
- the repayments to investors.

If the price does not accomplish these functions the business cannot survive.



EXAMPLE

The Praja Cooperative in Chitwan district, Nepal, is included as an example in Step 5. During the preparation of the financial plan for this enterprise, prices were compared between those offered by the road-head buyer and the processor in the adjoining district. The target group was able to obtain a higher price from the processor, although it also had to factor in additional costs, such as storage, transportation and management.

Customers

It is important to know the customers and what price they are willing to pay for what level of quality. Customers are influenced by seasonal changes in price, which are based on the supply of and demand for a product.



EXAMPLE

A high-quality product, such as a packaged herbal tea with a well-designed label, may appeal to wealthier customers, who are willing to pay more for the presentation of a product. Similarly, some buyers of forest products, such as medicinal herbs, will pay more for the product sold to them in bulk, since it is more convenient for them to buy it that way than to send their own agents to collect from a number of villages.

On the other hand, a herbal medicine production group selling to a local alternative health clinic targets low-income customers who are not concerned with packaging and who are mainly interested in saving money. However, if the same production group targets a new market of urban buyers, it will have to research quality and packaging that will attract those wealthier customers, and it will be able to charge more for the product.

Many pricing strategies take advantage of the psychology of buyers. Some buyers are concerned only about the brand name and the image of the product, rather than about the price. This is an important link to the mission statement of the enterprise. Many buyers will pay more for honey that is guaranteed to come from pesticide-free flowers and to be produced by an enterprise that is environmentally sustainable and ensures equitable distribution of profits.

The following are some of the typical issues and questions facing target groups when they try to set prices based on the information known about the potential customers.

- **Volume.** Is the target market mass market or elite?
- **Image.** Does the target group want to be known for quality or for bargain prices (prestige pricing rather than leader pricing)?
- **Customer psychology.** \$9.95 sells better than \$10!
- **Product lifespan.** Is it a fad item that will go out of style? If so, the target group needs to make profits quickly and charge higher prices.
- **Seasonality.** Is the product available? A characteristic of non-timber forest products (NTFP) is that many are only available for short seasons. If there are several buyers at a road-head, they may all be offering different prices or different paying conditions. A cost/benefit analysis is needed to be able to evaluate the different price offers versus the higher costs of storage for longer periods and then to decide how long to store and when to sell the product.

The following are examples of profit objectives with respect to customers that can also help in determining pricing strategies.

- **Leader pricing, loss leader.** By taking a loss on one product, the target group can stimulate sales on another.
- **Market penetration.** An initial low price can be offered to gain the attention of the market.
- **Price skimming.** The target group can start with high-end prices to see what the market will bear.
- **Price lining.** Several items can be grouped under one price.
- **Status quo.** Prices can be set according to those of the competitors.



PRICING METHODS

Industrial pricing

This method can be used in a manufacturing situation. The target group needs to know the variable costs and fixed costs to work out cost-plus pricing.

- ☐ **Variable costs** are associated with each unit of production. They vary according to sales and they include:
 - materials for production;
 - labour in production; and
 - a percentage of the overhead allocated to sales of a unit.
- ☐ **Fixed costs** are costs that remain constant no matter how many units are sold, such as rent, water, electricity and management wages.
- ☐ **Cost-plus pricing.** In cost-plus pricing, the fixed and variable costs per unit are worked out and a margin for profit is added.

Retail pricing

If the target group is distributing ready-made goods, the price can be determined by using the cost of the goods based on the supplier's invoice and by using competition as a precedent. Under retail pricing, any one of the following three strategies can be used.

- ☐ **Standard mark-up pricing.** The standard mark-up is computed and then added to the cost of the goods. Cost and profit are all built into a standard mark-up figure. This method is useful for businesses with large inventories.
- ☐ **Cost-oriented pricing.** Prices are set individually, on the basis of the cost of the goods, the overhead and the desired profit. This is the most accurate pricing method but also the most time consuming, since the product is evaluated separately.
- ☐ **Competitive pricing.** This is the simplest method of all, since prices are pre-set by the industry. To work out the price of a product, the target group works backwards from the competitor's price to calculate the mark-up.



PLACE/DISTRIBUTION

In many instances, tree and forest products are gathered in remote areas, and getting the product from the village to the buyer requires a carefully planned distribution system. In the existing market channel, transactions usually take place between village traders and agents who buy for processing firms.

HOW TO SET UP A MARKETING INFORMATION SYSTEM (MIS), CONTROL PRICES AND SET UP LINKAGES

Facilitators should guide the target group to assess whether it can take over some of the functions of the intermediary trader in order to increase its share of profits. It has to develop a system for obtaining increased access to market information and more control over prices, and it also has to devise a strategy that includes setting up a sustainable link between the group and its final customer.

Marketing information systems

The target group makes a list of the information that it wants to receive, how often it wants to receive it, and where it is available. A system is worked out for obtaining the price data and for disseminating it. Gathering information can include sending a member of the group to collect information on a regular basis, or developing a communication arrangement with partners living close to markets for the product, as in urban areas and near borders.



EXAMPLE

The Praja Cooperative in Nepal decided that it was critical for its members to be in touch directly with buyers outside the area in order to get up-to-date information on the distribution channel for products, on prices and on trends in demand. Therefore, its marketing strategy involved setting up an office with a storage room in the district market town.



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Control over prices

Prices of tree and forest products can undergo wide fluctuations from season to season. The reasons for these price changes are mainly beyond the control of the producers. Therefore, the only way to exert control is through storage of a product until a good opportunity to sell presents itself. This requires regular updates on prices, good storage facilities and capital to pay collectors for the product and to avoid cash flow problems while waiting to sell.



EXAMPLE

The Praja Cooperative enterprise development plan (see p. 83) shows that a strategy of at least four months of storage was planned in order to avoid selling during the harvest season. This strategy was devised by examining the market channel and by looking at the annual trends in price for that product. Buyers commonly store this product because there are price fluctuations every year, with low prices during harvest season and higher prices four months later.

Linkages with distributors

The target group should prepare pricing information that is more convenient for the shopkeepers who are distributing the product. Good accounting and record-keeping and frequent communication to clarify misunderstandings are essential.

When there is an attempt to increase market share and compete with other, similar products, the relationship with the wholesale or retail distributors becomes very important. Distributors expect terms of payment that compare favourably with those for competitors.

WHAT INFORMATION ABOUT DISTRIBUTION SHOULD BE ASSESSED FROM PHASE 2?

The information that will help to plan a distribution system is about:

- the type of transportation required to get the product or service to the public;
- the distributors of the product (which ones are useful and which ones are useless?);
- the time and costs involved in getting the product or service to the market; and
- promotion strategies that include distribution networks.



EXAMPLE

If an enterprise producing honey wants to penetrate an urban market, it will have to compete with other established brands of honey. These brands might be giving distributors 30 days to pay their bills to the honey company, and a new brand will not be successful unless it can offer similar (or better) terms of payment.

PEOPLE

The essence of marketing is finding out the interests and needs of prospective buyers of a product. This can be a major challenge for target groups in remote areas.

HOW TO DEVELOP A MARKET STRATEGY

Information that is needed from Phase 2 includes:

- a list of types of buyers and market segments; and
- the pattern of trends in the target markets, and of changing interests or needs.

Facilitators need to devise strategies that establish links with end users of a product. The target group needs to visit the market place where its products are sold on a regular basis, compare its product to that of competitors, and get customer response and feedback. Alternatively, the group needs to be in touch with retail distributors who sell the product to the end user (the final recipient of the product) in order to communicate information about the product needs to these retailers and to receive feedback from the customer, in order to improve the product or adjust prices.



EXAMPLE

The members of the target group in the Praja Cooperative, who live in a remote area, needed to have regular contact with the buyer of their product. A market study visit to the buyer's processing factory was organized for representatives of all the potential entrepreneurs. They obtained information from the buyer about demand, quality and packaging preferences that the road-head trader had never shared with them. The buyer was willing to pay almost double the road-head price for the product if those requirements were met.



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PROMOTION

There are many options for promotion, depending on the product and the means available to the target group.

To develop a strategy for promotion, the following information from Phase 2 should be assessed:

- features of the product that help people recognize the product as distinctive and that encourage them to buy it;
- forms and costs of promotion that can be used to reach the greatest number of people; and
- different target market segments (niche markets), and consequent effects on promotion and packaging.

Facilitators need to ensure that the mission and values of the enterprise are features of the promotional package for the product, and these need to be communicated to the distributors and end users. The strategy for promotion will depend on the objectives for gaining market share. Brand name recognition in an environment of competing companies is an important objective to strive for. Simple and cost-effective promotion includes attractive and informative labels and packaging. Promotional events include trade fairs; promotional strategies can include distribution of free samples. More sophisticated (and expensive) forms of promotion include advertising in print media, on billboards, and on radio and television. In all cases, the promotional strategies need to be assessed in view of the expected returns.



EXAMPLE

The facilitators supporting the Praja Cooperative wanted to pilot test a fruit juice concentrate made from a very common fruit found on trees in the project area. Since they had linkages with international organizations working in development, they distributed the product on a complimentary basis to some of the offices. These organizations were interested in supporting international market linkages and in buying the product for use among their staff. In this way, the producers obtained useful customer information and good linkages with new markets in exchange for the cost of the complimentary bottles of fruit juice.



Strategic alliances for marketing

Strategic alliances for marketing are a frequent feature of tree and forest products market development because:

- product development requires an extremely diverse range of skills and orientations in the economic, financial, legal, institutional and technological areas; and
- one enterprise usually cannot afford to maintain the required broad-based expertise of staff or to hire adequate technical consultants.

HOW TO DEVELOP STRATEGIC ALLIANCES FOR MARKETING

During the study of the business environment, facilitators helped the members of the target group identify both direct actors (such as producers, processors, middlepersons and consumers) and indirect actors (such as research institutions, product associations and government agencies) involved in the production, transportation, manufacturing and trade of a product. The members of the interest group can form work groups for each area of enterprise development, and discuss which kinds of partnerships could help them overcome some of the constraints in that area. Non-financial partnerships for marketing include an association formed of several production groups to promote trade linkages and standardize product quality. Other actors or stakeholders in the area may also want to be involved in the organization in some way; they may include local traders, the chamber of commerce and local non-governmental organizations.

Partners in an alliance need to have the following characteristics in order for the alliance to be effective:

- they should be organized around a well-defined joint aspect of the enterprise that is beneficial to both partners;
- they should have similar values and discuss these before making commitments in the partnership;
- there should be good communication links;
- a core decision-making group should be identified and maintained; and
- good boundaries and distinctive roles should be maintained.



Resource management/environment strategy

During Phase 2, the target group assessed the capacity of the resource to regenerate itself and to be harvested sustainably. Using the information gathered during that phase, group members should choose management regimes and identify training needs and partners that can provide technical expertise.

The resource management strategy is critical for:

- choosing the product (only products with a sustainable raw materials stock will be promoted);
- contributing to the decision of the maximum scale of the proposed enterprise (an available and reproduced resource allows a larger scale than a resource that needs a strict management);
- deciding the alternative ways of getting the resource, such as cultivation and changing the area of supply;
- developing a protection plan for the species, since it is likely that marketing efforts, if successful, will contribute to greater pressure on the survival of the plants; and
- supporting the marketing strategy (products contributing to the conservation of the environment and produced in an eco-friendly manner, such as those free of chemicals, gain an environmental added value that can be recognized by consumers interested in environmentally and socially sustainable products and can be integrated in the production costs).

How to develop a resource management strategy

Potential strategies differ according to the current status of the resource base and according to whether or not there is a clear understanding of the production yield cycle and regeneration potential of the resource. The conclusions can be summarized as follows.

- Even if the resource base status is large, and the production yield cycle and regeneration potential is not difficult to understand if proper study is conducted, the option of lowest risk is to allow access to the wild resource and encourage interest groups to organize themselves and issue harvesting management rules (such as regulation of harvesting season, regulation of the minimum size and grade of harvested resource, restrictions regarding the zone for regeneration, and regulation of proper harvesting techniques) that all local users have to respect. This has then to be supported with the parallel social organization of the producers' groups (see Social/institutional strategy, p. 35).

- The risk of decreasing the stock of resource is greater for species of medicinal plants with a moderate resource base. Assuming that the production cycle and regeneration potential can be surveyed, the option of lowest risk is for the interest groups not only to issue harvesting management rules and enforce them internally, but also to request legal support from the government. The local rules recognized and enforced by the governmental institutions will then keep other outsiders from depleting the resource and will discourage local illegal harvesting.
- Domestication of species, where possible, can be initiated on trial plots on common property or on private lands in either of the options mentioned above.

RESOURCE MANAGEMENT STRATEGIC ALLIANCES AND PARTNERS

Alliances with specific partners are necessary in order to provide expertise for skills training. Interest group members should have access to forest land for cultivation and for managed extraction of various species; the forest land allocation process should be a priority for these groups. Training should be included for the land management of these plots.

As regards the policy aspect, producers' groups formalize co-management partnerships with the commune and the district's forest protection authorities; facilitators should assist producers' groups so that they will be involved in designing and in negotiating the terms of the forest management agreements with the local authorities. (Most of the time harvesters do not know the best harvesting period of the resources.) In the future, producers may benefit from alliance with a research institute that can help provide this information, which enables the producer to obtain a product of better quality, and can also provide information on the way to domesticate it according to the consumer's preferences. If the marketing of the products is enhanced by the eco-friendly quality of their exploitation, an alliance with a certification agency will be necessary.



EXAMPLE

In Nepal, one of the biggest threats to the sustainability of tree and forest products, especially high-altitude, high-value medicinal plants, is early harvesting by villagers who need cash before the important holidays every year. Talking to them about improving harvesting methods has no effect, since they have no control over the plots and therefore no incentive to leave a part of the plant in the ground for regeneration, since someone else will probably come along and harvest it. There are two very effective strategies for assuring sustainable resources. The first is to set up mechanisms so that collectors can get advance payment before the holidays for the product that is harvested later, when the seeds have matured. The second is to give communities greater control over the resource, so as to protect it from others.

Social/institutional strategy

Disadvantaged community members and gender issues

If the steps in Phases 1 and 2 have been conducted in a thorough manner, the successful marketing of the product should not lead to any negative impacts. The social/institutional strategy needs to predict possible impacts, including greater pressure on resources and changes in land use and the possible impacts on all users in the community.



As a result of the new activities, it may become more difficult for other members of the community to have access to resources they usually obtained from the land used by the new enterprise. Also, for example, they may affect the availability of water for the other community members. Women's workloads may increase as a result of the enterprise, yet they may not share in the decision-making or in the benefits.

DEVELOP A STRATEGY FOR PARTICIPATION OF DISADVANTAGED COMMUNITY MEMBERS

The target group should try to identify current users of a resource and then include a social strategy that makes provisions to avoid these potential social impacts. An important element of this strategy should be the participation of disadvantaged members of the community in the planning activities. Therefore, the facilitator should build the capacity of the interest groups, ensuring that all those members of a community who are interested have a chance to participate in the decision-making. This will be very important if the community decides to use some of the profits from the enterprise to respond to some of the community's needs.

Some specific strategies may be needed in order to ensure that certain users are targeted in a community. There is always a risk that the new initiatives will result in the alienation of the more disadvantaged groups in the community. The target group should devise ways of ensuring the representation of those individuals in the decision-making bodies of the enterprise and in the community's management of natural resources. For instance, it may be necessary to include provisions in the organizational structure for the participation of a minimum number of women or disadvantaged members of the community in the decision-making committees. There should always be more than only one or two women on such a committee, so that they can support one another and feel comfortable about sharing their views during meetings.

As part of its enterprise development plan, the target group may decide to begin some kind of processing. The acquisition of equipment by the group has implications for all of the households. The location of a processing enterprise in the community should be considered carefully. If the users of the equipment are going to include women, the facilitator should encourage the group to consider ways of reducing their workload through choice of a good, nearby location.



EXAMPLE

The organizational structure for the Praja Cooperative shows how an attempt has been made to include all disadvantaged members of the community in the decision-making structures of the enterprise.

Once marketing of a product begins, the product will increase in value and the community has a different perception of its product. The facilitator should encourage the interest group to devise means of ensuring that the very poor members of the community still have access to the product. Similarly, other neighbouring communities may collect the product for household use. In order to avoid conflicts, it is necessary to facilitate discussions between these users and develop a strategy that takes into account their traditional use of the product.

ORGANIZATIONAL STRUCTURES FOR ENTERPRISES

The choice of a type of organizational structure is dictated mainly by financing needs, marketing support requirements, technical assistance requirements and objectives for distributing profits to participants and for sharing decision-making. The facilitator needs to encourage discussions between the members of the group in which those issues are examined. If the need for a partnership is still felt, the outcome of that analysis is the basis for a strategic decision that can be made by the enterprise participants about the function of the partnership and what opportunities for partnership should be explored.



CHOOSING A TYPE OF ORGANIZATIONAL STRUCTURE

In choosing a type of organizational structure, both advantages and disadvantages should be examined.

SOLE PROPRIETORSHIP

Advantages

- The business owner is totally responsible for all business transactions.
- He/she has total control of and responsibility for the enterprise and has the rights to all profits.
- Decision-making is simple, since there are no partners to dispute the chosen course of action.

Disadvantages

- There is no shared expertise.
- Funding comes from a sole source.
- Loan collateral consists of the assets of a sole individual.
- The enterprise ceases in the event of death or disability of the sole owner.
- The owner is personally liable for any adverse business transactions that expose the individual and his/her personal assets to great risk.

PARTNERSHIPS

A general partnership consists of two or more individuals joining together to conduct business and share proportionately in the responsibilities, risks, liabilities and profits and losses incurred.

Advantages

- There is additional technical competence.
- There is additional capital.
- There is protection from dissolution of the enterprise in the event that one of the partners becomes incapacitated or dies.

Disadvantages

- Partnerships spread control, which can create problems through disagreements.

A limited partner is strictly an investor in a partnership and has limited liability as well as a limited role in the management of the enterprise. This type of partnership is, therefore, a way of raising capital without losing control of the business. Joint ventures are examples of this type of partnership, in which technology may be shared, together with certain areas of financing and strategic interests, such as distribution networks.

INCORPORATION

A corporation is a separate entity from its owner(s), who therefore are not personally liable for its decisions or actions. A corporation can attract capital by selling stock at the market value. Management control is maintained by retaining a majority of the stock. Prospective investors can be outsiders, but they can also be staff of the enterprise. Many successful enterprises attribute their growth to the fact that they are owned by staff. Staff ownership is not usually a source for start-up capital needs but can be an effective management and capital tool after the business has become operational.

COOPERATIVE

This form of enterprise structure implies ownership by those who use the services and entitles the owners to a share in any profits that the cooperative makes. There are four basic principles in which cooperatives differ from corporations.

- 1) Benefits are derived in proportion to the member's use, rather than to the amount of investment (this differs from investor-owned corporations).
- 2) There is democratic management by the owners and an elected committee; each member has one vote regardless of the amount of stock owned or the volume of business conducted.
- 3) Services are provided to user-owners at cost.
- 4) There are limited returns on equity capital, and limited ownership of shares, in order to discourage investor-oriented decision-making.

The disadvantages of cooperatives lie in their complex management and the fact that they have often been used as conduits for government support. As a result, members are not encouraged to become self-reliant. In addition, the cost of the overhead of the cooperative can become too high in relation to the perceived value of the service being offered.



Science and technology strategy

Research and development

During the study of the business environment, existing institutions that could provide technical expertise to the enterprise in the areas of science and technology were identified. The facilitator also assessed the skills of the members of the target group and the options for upgrading their skills. An overview of the existing technical resources (such as equipment, and research and development) and of the infrastructure in place (such as communications networks and road access) was also obtained. The facilitator should now help group members choose the production technology, processing methods, equipment and packing methods and materials.

HOW TO USE RESEARCH AND DEVELOPMENT IN THE SCIENCE AND TECHNOLOGY STRATEGY

The target group needs to assess the need for technical training and the infrastructure that it will require to produce and market its products. Facilitators will assist the group in selecting the technological options that will best integrate the values and concerns of the ecological, social, market and economic areas of development defined in the enterprise strategy. On the basis of the outcome of these exercises, facilitators should recommend partners that can help bring about these results.

In the MA&D process, technological options are chosen because they contribute not only to improving production but also to integrating environment-friendly methods in the production process. Production strategies and their associated costs should ensure that the market price for a product includes a good profit margin. Various technology options can be selected, according to expenses associated with making improvements in environment-friendly technological equipment and process.



**EXAMPLE****Market strategy in the Quang Binh, Viet Nam, case study****▲ MARKET/ECONOMY****■ Products**

Strategy: To maintain a product mix consisting of a honey-to-beeswax ratio of 4:8. Target domestic niche markets such as women's health, gift markets, traditional users and tourists by producing natural honey that is certified as organic and is differentiated from 'industrial' honey. Also target the mass market, aiming to substitute imported honey from Australia and Spain, and identifying export destinations for high-quality honey. Investigate labelling and packaging requirements for those markets. Develop the production plan, purchase equipment and organize the support and training needed for the producers to achieve and respect market and quality requirements. Name one member of the group to be responsible for quality control and to monitor adulteration.

■ Price

Strategy: Sell most of the honey at a relatively high price in niche markets and also sell some of the product at lower prices to mass market buyers, in both domestic and export markets. Obtain up-to-date information from the market place on a regular basis.

■ Place/distribution

Strategy: Identify the distribution channels for the targeted niche market and for the mass domestic and export markets, as in existing market channels (including Dong Le, Quy Dat and Ba Don) and new markets (such as Hanoi, Vung Tau, Dong Nai and Cuc Phuong National Park). Identify buyers who are particularly receptive, and if they want to see hives, organize a way to show these to them. Choose the buyers and sign a buying contract with the processor in order to guarantee their interest. Organize collection and delivery from all the villages and rent a storage space in the main market town from which the processor can pick up the aggregated quantity of product. Consult with a business analyst in order to assess options and develop financial plans for the future organizational structure and legal status needed to link up several honey production groups. Hire permanent management staff to coordinate production, packaging, quality control, accounting and marketing. Identify the training needs for group members in order to organize such an association. Identify potential partners and their roles, including the IFSP, the National Center for Research and Development of Honey and the Vinapi Company.

■ People

Strategy: Conduct a study tour to initiate linkages with potential buyers and emphasize the interest in a long-term relationship that provides quality products.

■ Promotion

Strategy: Design a brand name for the future association of several groups.

PHASE 3: Plan enterprises for sustainable development

STEP 3: Develop strategies in each of the four areas of enterprise development

▲ RESOURCE MANAGEMENT/ENVIRONMENT

Strategy: No chemical substances will be used for the raising, extraction or refinement of the honey, so as to avoid killing the bees and to keep the honey organic so that certification can eventually be obtained. Only seven beehives will be placed in 1 ha at a minimum distance of 1 km from each other with a maximum of no more than 10 hives per 1.3 ha in order to ensure enough flower resource. A committee will be planned to coordinate the producers from the four communes for the planning, management and control of the resource. This will be supported by part of the fees paid by the groups for management salaries. Additional multipurpose flower trees may also be planted. There are no wastes anticipated that would have a potential negative impact on the environment.

▲ SOCIAL/INSTITUTIONAL

■ Gender issues

Strategy: Ensure women's participation by including a minimum number of females in each group.

■ Organizational structure for the enterprises

Strategy: Initially the groups will be informal, but as production increases they will start to coordinate planning for aggregating production and joint marketing. They will also have to select the legal status that is the most appropriate for their association.

■ Institutional support

Strategy: Identify the most useful institutions and initiate linkages with them.

▲ SCIENCE AND TECHNOLOGY

■ Research and development

Strategy: Each group will purchase a centrifuge in order to produce its own high-quality honey and reduce moisture content. The financial plan will include the costs of sugar and medicine in order to ensure that production is at its maximum. Linkages will be established with national institutions in order to obtain assistance on technology.



Planning for worst-case scenarios

Unpredictable events can seriously damage the enterprise and the faith of investors. Good planning minimizes these risks.

How to anticipate risks

Brainstorm with the group about all of the things that could go wrong, no matter how unlikely they seem. Then try to come up with strategies that would prevent or at least minimize the damage.



EXAMPLE

Among the risks that can be anticipated are that the product might be damaged during storage or during transportation to the processor, or that the buyer might break the contract and refuse to purchase the product. Strategies can be devised to attempt to ensure that none of these risks become reality.

The following are worst-case scenarios in which the enterprise has some possibility of developing mitigating strategies:

▲ MARKET/ECONOMY

- The national/global economy goes into a slump.
- Prices drop in the targeted market.
- Buyers cancel orders.
- A sample in the shipment is found to be contaminated.
- The truck transporting products has an accident.
- Funds for paying collectors are stolen.

▲ RESOURCE MANAGEMENT/ENVIRONMENT

- Collectors do not respect harvesting rules.
- Outsiders continue illegal harvesting.
- There is unpredictable weather during drying seasons.

▲ SOCIAL/INSTITUTIONAL

- Unforeseen conflicts occur between forest users.

▲ SCIENCE AND TECHNOLOGY

- Machine or equipment breaks down during processing.



STEP 4 | Formulate the action plans to implement the strategies

Once strategies for the enterprise have been developed, action plans then have to be built on the product assessment and the enterprise mission statement and goals, and assigned to each strategy in order to ensure their implementation. The objective of Step 4 is the formulation of such an action plan. Facilitators should encourage the members of the target group to think through every strategy and to plan in detail all the steps necessary in order to get the enterprise started.

Develop an action plan

Now that the interest groups have formulated the enterprise strategy in the four areas of enterprise development, they need to operationalize these strategies by working out the sequence of activities necessary to bring about the intended results.

Build on the product assessment and enterprise mission statement and goals

The working groups formed in previous steps can continue to meet and to plan ways of implementing the strategies that they have developed. Within each of the four strategies, there are a number of components, such as those described in Step 3, which need to be addressed with precise action planning. Those components should all present solutions to overcome constraints detected in the product assessment that took place in Phase 2 and in the analysis of the enterprise environment in Step 1 of this phase. The solutions should also be in accordance with the mission statement and goals developed for the enterprise.

Action planning

A critical aspect of action planning is assigning responsibility for completion of each of the tasks.

Develop an action plan

The interest groups need to discuss who will do what, and what kind of capacity-building or assistance will be needed in order for the individual to be able to carry out the activities in each of the strategies. The timing of the beginning and end of each task also needs to be

determined. The determining factors in making decisions about the timing of activities are often the harvesting season for the product and the availability of enterprise participants' time.



EXAMPLE

Development of an action plan in the Quang Binh, Viet Nam, case study

The case study gives an example of how an action plan was developed by assigning activities and a time reference to each of the objectives and strategies developed in Steps 2 and 3.

▲ MARKET/ECONOMY

■ Products

Action. One member of each interest group was to be assigned to form a market study team for that product and to visit the potential buyers and market places (including Ho Chi Minh City, Hanoi, Vung Tau, Dong Nai and Cuc Phuong National Park). The study tour was to be organized with the assistance of the facilitator and the IFSP. Quality requirements, such as acceptable moisture content, were to be determined, and suppliers of equipment for production and for monitoring quality were to be found. Possible trainers from extension departments and funding to organize training were to be identified. Suppliers of bottling and packaging materials were to be investigated. Institutions at the national level that can provide training, technical assistance and extension support were to be identified. Potential graphic artists for labelling were to be identified. The target export markets and the type of honey they are interested in (dark or light, single-flower or wild honey, and moisture content), in addition to their packaging requirements, were to be identified. A strategy for building up the image of the producers with export buyers was to be developed. The weaknesses and strengths of honey from other countries also exporting to European buyers were to be assessed.

Time. Representatives were to be selected following this workshop, and the study tour was to be completed within two months.

■ Price

Action. The market study team was to gather information on existing prices in the retail/wholesale domestic and export honey markets. The team was to be assisted in planning their information gathering with the help of a marketing consultant, and in identifying ways of developing a market information system. A break-even analysis was to be done with the help of a business analyst in order to evaluate the pricing strategy.

Time: The study tour was to be completed within two months.

■ Place/distribution

Action. Representatives of the interest groups, with the assistance of the facilitator, were to visit the buyer and draw up the contract, to organize a storage and management unit in the market town and to arrange financing in order to buy the product from all the interest groups.

Time. This was to be done two months before the harvest season began.

■ People

Action. The strategy for interviews with buyers was to be planned before the study tour representatives had their meetings, and during the meetings the representatives were to try to obtain as much information from buyers as possible regarding their needs and interests.

Time. This was to be completed within two months.

■ Promotion

Action. The process of designing and printing a promotional leaflet with the assistance of the IFSP facilitator and a graphic artist was to be planned for the following year.

Time. This was to be completed within a year.

▲ RESOURCE MANAGEMENT/ENVIRONMENT

Action. Institutions and the support services that they can provide were to be identified, and surveys of the resource and interviews with local villagers were to be organized. This was done by the interest group, with the support of the facilitator.

Time. This was to begin immediately.

▲ SOCIAL/INSTITUTIONAL

■ Gender issues

Action. The identification of women who could join each interest group was to be initiated, with the support of the facilitator.

Time. This was to begin as soon as possible.

■ Organizational structure for the enterprise

Action. The relevant formal structures were to be determined, and that information was to be shared with all members. The enterprise plan was to be finalized. The kind of structure that would serve the purpose of marketing the products was to be decided, then the implications of the choice were to be discussed with all interest groups. An executive committee was to be formed and applications were to be submitted to the government officials concerned. This was to be done with support of the facilitator and one representative from each interest group for a product in each village.

Time: This was to begin as soon as pilot marketing had taken place successfully.

■ Institutional support

Action. The group members were to be assisted by a facilitator from the IFSP in identifying and contacting potential supporting institutions and sending a delegate to obtain information about them.

Time. This was to be done as soon as possible.

▲ SCIENCE AND TECHNOLOGY

■ Research and development

Action: The IFSP facilitator was to assist the group in identifying suppliers of equipment and in linking up with national institutions.

Time: This was to be completed within the following three months.



STEP 5 | Calculate financial projections for the enterprise

The objective of this step is to ensure that the proposed strategies are realistic and cost-effective and that the enterprise will be profitable. Through financial planning before starting an enterprise, it is possible to ensure that strategies are realistic by working out a budget for the activities proposed in Step 4 and assessing if they are cost-effective. When presented with the detailed planning required by budgeting, facilitators can assist the interest group in making decisions about how to divide up limited resources in the most effective way. This process then becomes another opportunity to increase the capacity of the group to reduce risk and improve its enterprise planning and management skills.

What kind of financial planning is necessary?

In most forest products, increased revenue to collectors can be obtained by value-adding. This may be a simple activity, such as better cleaning and grading. Collectors may continue to sell existing products to existing buyers, but the strategy may enable them to set higher prices. Very little may be needed in the way of capital investments, since mainly labour-intensive methods, carried out by individuals, will be used. Simple financial plans will be sufficient, and they will focus mainly on assessing profitability and showing the opportunity costs of the strategy.

However, if collectors want to increase the price that they are obtaining for products through strategies that require more intensive capital investment, then a financial plan becomes more important. For instance, this could include purchasing equipment, or collecting a product from several small collectors and storing it until the price increases. These strategies usually imply that instead of using an existing product and an existing buyer, the interest group decides it is worthwhile either to invest in improving the product in some way or to develop a new product and sell to new buyers.

For example, the Quang Binh, Viet Nam, case study illustrates a situation in which a group of farmers realized that in order to find markets for their honey they needed to buy a centrifuge machine, and in order for that to be possible, they had to form a group and put their collective finances together, and also obtain a group loan. Similarly, the example of the Praja Cooperative in Nepal illustrates a situation in which the main strategy for obtaining higher prices was to aggregate small quantities of product from all the collectors, to store the product at a road-head collection centre and to sell it directly to an urban buyer. In both of these examples, the strategies needed for accomplishing the objectives required some kind of group formation and thorough financial planning.

Interest groups who own their own enterprises on private lands may also decide to increase value or improve marketing strategies, but in their case they may be able to do so without any group mechanisms. However, this is more likely to be the case with cultivated products in which the scale of production is higher than that of collection from the wild and in which the production period is of longer term. For example, in the case of cardamom growers, individual farmers tend private land or community forestry land and have to wait two to three years before there are any returns from selling the product. Capital investments, therefore, have to be assessed in terms of opportunity costs based on the long-term profitability and viability of the enterprise.

How is a financial plan developed?

The financial projections for the planned enterprise should be done while the interest groups are meeting to discuss the strategies and their related activities. This will ensure that the group understands the financial implication of the actions that it is proposing. As a result of this planning the group might decide that it is not possible to carry out certain actions within the scope of the planned enterprise unless it can work out other ways to finance them until the enterprise grows to a point where it can support such activities.

To prepare the financial plan, a range of tools are available to help the interest group demonstrate the profitability of the enterprise and develop the financial projections. These include:

- calculating the break-even point;
- working out the start-up costs and capital need;
- calculating the payback period for investment;
- forecasting profit and losses;
- making a cash flow analysis;
- preparing a balance sheet; and
- calculating financial ratios.



In Step 5, three examples are used to give different perspectives on scale and types of enterprise. The case study of the honey producers of Quang Binh, Viet Nam, illustrates a small enterprise with five members. The example of the Praja Cooperative in Chitwan district, Nepal, is a larger organization that federates several hundred collectors. The example of the bamboo basket maker gives an idea of a microenterprise and of how, even on such a small scale, financial planning is still a useful tool.

Calculating the break-even point

The break-even point can be used as a guide to determine if the sales price used in the enterprise is high enough to generate sufficient profit to meet the goals of the enterprise.

The objective of calculating the break-even point is to use the sales price of a product to assess the level of sales, where revenues from sales equal total expenses (fixed costs and variable costs) of producing those sales.

- ▣ **Fixed costs** are part of the overhead of the enterprise, and they remain unchanged with the number of units sold; they include such costs as rent, utilities, insurance and staff salaries. Fixed costs are present even if nothing is produced.
- ▣ **Variable costs** are associated with each unit of production. Variable costs vary directly with the number of units sold; they include materials plus labour plus a percentage of overhead directly allocated to the sale of a given number of units.
- ▣ **Total expenses** are the sum of fixed costs plus variable costs.

In other words, at the break-even point, profit is equal to zero. Once revenues above that point are obtained, only the variable costs of production and not the fixed costs of overhead (since they have already been covered by sales leading up to the break-even point) have to be deducted from the sales price in order to calculate the profits. On the other hand, revenues below the break-even point constitute losses.



Finding the fixed and the variable costs of production

Once the interest group has estimated a production and sales goal, it needs to work out both fixed and variable costs of production. The facilitator needs to assist the group in working out how to calculate the cost of its own labour, including collecting raw materials from the wild and processing.

The first step is to use the number of units from the sales target estimated in the goals in Step 2 to calculate the fixed costs and the variable costs involved in generating those sales. These cost calculations will be used again in the profit and loss and cash flow exercises in this step. Then the group has to estimate the price at which it thinks it can realistically sell the product. It is then ready to calculate the break-even point, as shown in the following example.

Once the break-even point is known for a particular price, the facilitator should encourage the group members to analyse these results and assess whether the price set for a product ensures that there is enough margin for profit. If it does not, then a higher price should be estimated and a new break-even point should be worked out. On the other hand, if the price the group is charging for the product is high enough to leave a comfortable margin, then the facilitator can have the group work out a discount strategy and check it with the break-even analysis.



EXAMPLE

How to calculate the break-even point - Quang Binh, Viet Nam, case study

First, the fixed and variable costs of a product (see Tables E.2, E.3, E.4, E.5) have to be calculated. In the activity of the honey producers of Quang Binh, Viet Nam, both honey and beeswax are produced. Therefore, the first step is to calculate the proportion of costs that can be attributed directly to honey production and not to beeswax production. One way to do this is to use the percentage of total honey sales as compared to the total sales of honey and beeswax together, and use the same percentage to work out the proportion of fixed and variable costs that are attributed only to honey.

For example, among the variable costs are those for ingredients such as sugar and medicine, which contribute to production of both honey and beeswax. In order to obtain an approximate estimate of how much of these costs can be attributed solely to honey, the total cost of these ingredients is multiplied by the percentage of sales that can be attributed to honey. However, bottles are purchased only for honey packaging and therefore the costs of bottles attributed to honey is 100 percent. Similarly, with fixed costs, most of the costs, such as those for stationery or equipment, can be divided proportionally between honey and beeswax, using the percentage of sales as an approximate guideline.

TABLE E.2 Method for calculating the fixed and variable costs directly associated with the manufacture of 1050 bottles of honey in year 1 - Quang Binh, Viet Nam, case study

Honey sales as a percentage of total sales (year 1)	=	$\frac{\text{Total sales of honey}}{\text{Total sales of honey and beeswax}} \times 100$	
Total sales of honey:	29 400 000 d	$\frac{29\,400\,000\text{ d}}{35\,525\,000\text{ d}}$	= 0.83 x 100 = 83%
Total sales of honey and beeswax:	35 525 000 d		
Honey sales as a percentage of total sales in year 1 = 83 %			

US\$1 = 13 000 dong(d)

**TABLE E.3 Variable costs of honey production (not including beeswax)
Quang Binh, Viet Nam, case study**

RAW MATERIALS	PRICE /UNIT	QUANTITY	TOTAL COST OF SALES	PERCENT	COST ATTRIBUTED TO HONEY
Sugar = 5 kg /hive	7 000 d/kg	175 kg	1 225 000	x 83%	1 016 750
Medicine = 12000 d/hive	12 000 d/hive	35 hives	420 000	x 83%	348 600
Bottles (650cc bottle = 500 g honey)	1 500 d/bottle	1 050 bottles	1 575 000	x 100%	1 575 000
Labour: 15 days per hive per year	10 000 d/day	525 days	5 250 000	x 83%	4 357 500
Total variable costs			8 470 000 d		7 297 850 d

US\$1 = 13 000 dong(d)

TABLE E.4 Variable costs of honey production - Quang Binh, Viet Nam, case study

Average variable costs per unit	=	$\frac{\text{Total variable costs of honey production}}{\text{number of bottles}}$	=
		$\frac{8\,470\,000\text{ d}}{1\,050\text{ bottles}}$	= 8 067 d/bottle

US\$1 = 13 000 dong(d)

**TABLE E.5 Fixed costs of honey production (not including beeswax)
 Quang Binh, Viet Nam, case study**

Indirect labour/management contribution		120 000 d	x 83%	99 600 d
Repair and maintenance		50 000	x 83%	41 500
Stationery, communications		60000	x 83%	49800
Depreciation of equipment over 3 years	9 620 000	3 175 000	x 83%	2 634 918
Interest (18%)	959 499	959 499	x 83%	796 384
Total fixed costs		4 364 099 d		3 622 202 d

US\$1 = 13 000 dong(d)

TABLE E.6 Break-even point in units (bottles) - Quang Binh, Viet Nam, case study

$\text{Break-even point in units (bottles)} = \frac{\text{total fixed costs for honey}}{\text{selling price (per bottle)} - \text{variable cost (per bottle)}} =$ $\frac{4\,364\,099\text{ d}}{28\,000\text{ d} - 8\,067\text{ d}} = \mathbf{171\text{ bottles}}$				
$\text{Break-even point in revenue} = \text{break-even point (per bottle)} \times \text{selling price (per bottle)} =$ $171 \times 28\,000 = \mathbf{4\,782\,400\text{ d}}$				

US\$1 = 13 000 dong(d)

The example from Viet Nam shows that once 171 bottles have been sold, out of a total of 1050 bottles projected for the year, the fixed costs have been covered, as well as the variable costs of producing 171 bottles (see Table E.6). Beyond that volume, i.e. for the remaining 879 bottles, the only cost is the variable cost of producing and selling the product. There is therefore a comfortable margin within which to make a profit. Alternatively, it can be seen that once the enterprise has brought in 4 782 400 dong (US\$370) in revenue from sales, the fixed costs have been covered for the season and, for any future sales, only the variable costs have to be deducted in order to see how much profit the enterprise is making. This is a comfortable margin, since the total sales projected for honey and beeswax come to 35 525 000 dong (\$2733).

The interest group can also use the break-even point to determine its promotion strategy. For example, if the enterprise has already sold at least 171 bottles at 28 000 dong per bottle (\$2.10) and a customer offers to buy a large volume but wants a discount, the group should realize that it needs to get at least 8067 dong (\$0.62) per bottle (the variable cost), but that it doesn't need to worry about the fixed cost anymore, therefore it can afford to offer a discount (the impact that this might have on cash flow will be discussed below in this step).

Working out the start-up costs and capital needs

The estimates of start-up costs and capital needs will enable the interest groups to answer three questions.

- 1 How much should be spent to get the business opened, on the basis of the sales projection made by the group?
- 2 How much should be set aside to cover initial operating expenses? Depending on the situation, the group might need to calculate the need for at least three to four months of operating cash in reserve, although for many microenterprises longer periods might be necessary. This can be determined by using the cash flow method illustrated below in this step.
- 3 How much of that capital does the interest group have and how much does it need to find from other sources?

HOW TO CALCULATE START-UP COSTS

To work out the start-up costs, the interest group should begin with the first year's sales projection for the business, which it worked out to state the goals of the enterprise. Then it should use the break-even analysis to assess if the price is realistic. Next, it should calculate the start-up costs of attaining those sales. Financing can usually come from several different sources. The group should make a list of all the possible sources of funding, such as district-level funds for infrastructure development, community funds, grant funds, and loans from

PHASE 3: Plan enterprises for sustainable development
STEP 5: Calculate financial projections for the enterprise

community organizations. At this point it needs to decide whether it can invest some of its money in starting the enterprise or whether it needs to take on partners for financing and perhaps also get loans from a bank.

EXAMPLE

In the Quang Binh, Viet Nam, case study (see Table E.7), start-up needs for capital for the first four months of the enterprise are 12 671 000 d (US\$975). The five members of the interest group each provided 566 000 d (\$43.50), or a total of 2 830 000 (\$218), as a contribution. A loan was obtained from the bank for the remainder, 9 841 000 d (\$757), with a one-year pay-back period and annual interest of 18 percent.

TABLE E.7 Start-up costs for 4 months (350 bottles of honey) - Quang Binh, Viet Nam, case study

	QUANTITY	UNIT PRICE	TOTAL AMOUNT
EQUIPMENT			
Boxes and frames	35	50 000 d	1 750 000 d
Bee colonies	35	190 000	6 650 000
Frames (6 frames per hive)	210	3 000	630 000
Knives and other small tools	5	18 000	90 000
Mask and nets for extraction operation	5	40 000	200 000
Centrifuge machine	1	300 000	300 000
Total			9 620 000
Indirect labour/management contribution		120 000	120 000
Repair and maintenance		50 000	50 000
Stationery, communications		60 000	60 000
Total			230 000
MATERIALS			
Sugar (175 kg/3 times per year)	58	7 000	406 000
Medicines (420 000/3 times per year)			140 000
Bottles	350	1 500	525 000
Total			1 071 000
Direct labour (5 250 000/3 times per year)			1 750 000
Total start-up costs for 4 months			12 671 000
Less member's own capital (566 000 d each x 5)			2 830 000
Remainder to be financed			9 841 000 d

US\$1 = 13 000 dong(d)

Calculate the payback period for investment

The size of the investment must be in relation to the projected return on investment. The original investment should be returned over a period of time to the owner, plus any salary for work. In industry, most business plans should allow a payback period over a five to seven year period. However, because of the relatively high cost of interest, the small-scale loans required for the working capital of tree and forest enterprises should be considered mostly short-term loans, and the aim should be to pay them back within one or two years. In some cases, loans for equipment may be stretched out over longer periods.

HOW TO CALCULATE THE PAYBACK PERIOD FOR INVESTMENT

In order to calculate the payback period for the investment, the interest group needs to make profit and loss and cash flow projections for at least two years, and perhaps more (see the following sections). That way it will be able to see at what point it will be possible to pay back the original investment without hurting the cash flow of the enterprise.



EXAMPLE

The example of the Quang Binh, Viet Nam, case study shows that the loan principal will be paid back in the first year and that the enterprise will be making a profit by that time, with enough capital reserves to be able to operate in the second year without another loan. Instead, the Praja Cooperative expects to pay back the principal on the loan after the second year.



Forecast profit and losses

This is a summary of the income and expenses for the enterprise for a specific period, such as one year. It is a summary of the sources of income and the ways in which it was spent over the year. It should be done for at least the first three years of the business.

The profit and loss forecast is a useful budgeting tool that allows the interest group to review the records of the enterprise at the end of the period and compare its projections with the actual income and spending figures. As a result, its next projections will be even more accurate.

- ◉ **Projected income** is based mainly on the sales forecast. In order to work this out the interest group needs to estimate what volume is expected to be sold and at what price it will be sold. The analysis of the business environment will be the main guide to achieving a realistic estimate of sales for a given period.
- ◉ **Anticipated expenses** can be divided into the broad categories of fixed and variable costs described above. Interest expenses have to be included as operational expenses. However, since the profit and loss statement shows the projected income of the enterprise, the one-time opening expenditures for capital assets are not included as operating expenses. They are considered investments and will be shown on the balance sheet rather than on the profit and loss statement.
- ◉ **Depreciation** is a way of saving money for the eventual replacement of equipment bought at the start of the enterprise. Calculate the number of years in the expected lifetime of the equipment and divide that by the replacement cost, then save that amount every year. This can thus be considered an expense (this will appear again in the balance sheet in a later exercise).
- ◉ **Gross profit** is the sum of the fixed and variable costs and is deducted from the total sales. It may be used to pay principal on debt or to pay income taxes, or it may be kept in the business as retained earnings.
- ◉ **Net profit** is the remainder after tax is deducted from gross profit.



How to forecast profit and losses

To create this statement, the facilitator starts with the annual projected sales developed in the goals and used for determining initial capital needs. The information from the capital needs statement for operating expenses is used to calculate the total of the first year's operating expenses in the profit and loss statement. In the first year, some or all of the costs can be shown against sales as a percentage of the total projected sales. Then, in order to calculate projections for subsequent years, the increased volume of sales is estimated, and from that all of the next year's costs can be easily worked out. This provides a way of easily calculating increased management costs from increased sales. For example, in the example from Viet Nam, management is 0.3 percent of sales. Therefore, in the second year, management costs increase correspondingly to the increased sales.

EXAMPLE

The Quang Binh, Viet Nam, case study shows which costs are fixed costs and which are variable costs (see Table E.8). The two-year goals for the enterprise were used to predict the sales, and on this basis the group can work out the expenses and the annual profit (the example shows gross profit. Once taxes are deducted, it becomes net profit). In the section on financial ratios in this step, it can be seen how net profit is compared to initial assets in order to calculate the percentage return on investment (ROI) and assess the profitability of the enterprise.

The example of the Praja Cooperative in Nepal shows how profits were distributed on the basis of regulations in the Cooperative Act of His Majesty's Government of Nepal. The proportion that is retained profit (i.e. 25 percent) is not paid out to enterprise participants but instead is reinvested into the enterprise's working capital. It will therefore be part of the cash on hand that goes into the cash flow calculation of the second year and will show up in the equity section of the balance sheet as retained profits (see the following section).



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TABLE E.8 Forecast of profit and loss - Quang Binh, Viet Nam, case study

	UNIT PRICE	YEAR 1			YEAR 2	
		35 HIVES: HONEY, 525 KG BEESWAX, 175 KG			30% INCREASE 50 HIVES: HONEY, 750 KG BEESWAX, 250 KG	
		Units	Year 1	% of sales	Units	Year 2
Income from sales						
Domestic honey (bottles)	28 000 d	1 050	29 400 000 d		1 500	42 000 000 d
Beeswax (kg)	35 000	175	6 125 000		250	8 750 000
Total sales/revenues			35 525 000			50 750 000
Expenses						
<i>Fixed costs</i>						
Indirect labour/ management contribution (increases 30% in year 2)			120 000	0.3		152 250
Repair and maintenance (increases 30% in year 2)			50 000	0.1		50 750
Stationery, communications			60 000	0.2		101 500
Depreciation of equipment over 3 years (33% each year)	9 620 000		3 174 600			3 174 600
Interest (18%)	959 499		959 499			0
Total fixed costs			4 364 099			347 900
<i>Variable costs</i>						
<i>Raw materials:</i>						
Sugar = 5 kg/hive	7 000 d/kg	175 kg	1 225 000		250 kg	1 750 000
Medicine = 12000d/hive	12 000 d/hive	35 hives	420 000		50 hives	60 000
Bottles (650 cc bottle = 500 g honey)	1 500 d/bottle	1050 bottles	1 575 000		1 500 bottles	2 250 000
<i>Labour:</i> 15 days per hive per year	10 000 d/day	525 days	5 250 000		750 days	7 500 000
Total variable costs			8 470 000			11 560 000
Total fixed + variable costs			12 834 099			15 039 100
Profit			22 690 901 d			35 710 900 d

US\$1 = 13 000 dong(d)

Make a cash flow analysis

The cash flow analysis shows when money moves cyclically in and out of the enterprise on a monthly basis. It is essential for an enterprise, no matter what the size, to make a cash flow analysis in order to get a true picture of how the enterprise will operate financially. The analysis is also used to obtain an accurate estimate of the amount of operating cash reserves that will be required to get the enterprise started. Without this tool, the enterprise might appear to be making a profit, while in fact it could not operate because there could be a shortage of working capital for day-to-day expenses.

The cash flow analysis will show the effects of moneys owed to the enterprise (accounts receivable), moneys that the enterprise owes (accounts payable) and seasonal fluctuations of the enterprise. It will show the months of excess cash flow and the months when there is a deficit. It is a control and planning tool that can be used to borrow short-term money to run operations smoothly. The interest group needs to estimate as realistically as possible the amount of capital needed to launch and sustain the enterprise during the first three to six months. In the same way that the profit and loss forecast can be used as a budgeting tool, the cash flow projection will allow the group to look back over its records for a year and assess whether its estimates were accurate or not. Within a given month, the analysis can also help the group assess whether it is spending too much on any particular cost centre, to the detriment of other items that also need to be covered.

HOW TO PREPARE A CASH FLOW PROJECTION

The example from Viet Nam illustrates how to prepare a cash flow projection for one year (see Table E.9). The interest group starts by using the calculations made for the start-up capital needs and the profit and loss projection. It then has to decide when payments have to be made throughout the year. This is a very good exercise; it helps the group think about the details of the enterprise and appreciate the importance of working capital in the survival of the enterprise. The cash flow helps the group analyse and plan the cash needs of the business on a month-to-month basis by taking into account both sales and expenses. If the projection indicates that there will not be enough working capital in any one month, adjustments in expenses have to be made in order to remedy the situation.

The first step is for the interest group to estimate the cash on hand in the first month. This is the cash that the enterprise opens with. Therefore, the total amount of capital that was forecast in the start-up costs can be used here. Then, once sales begin, this income is also added to the cash on hand in order to give an indication of total cash (the cash flow projection only shows sales for which cash has actually been paid and does not show cash owed to the business). The expenses are also added up at the bottom of the table, and the total

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expenses are deducted from the total cash in order to estimate the cash remaining at the end of the month. This amount is then put at the top of the column in the following month as cash on hand. In order to ensure that the cash flow projections follow the profit and loss, a total of each row can be maintained in the first column.



EXAMPLE

The Quang Binh, Viet Nam, case study shows that some costs in the honey business, such as those for the purchase of bottles, could be postponed for two months. This helps the cash situation in the beginning, since sales do not begin until the third month. Similarly, the equipment purchase was spread out over two months in order to avoid a minus cash reserve. However, most of the other expenses are incurred on a monthly basis. The cash flow projection was used to estimate how much principal could be made in the first year without harming the cash position of the enterprise. The analysis showed that the entire loan could be paid in 12 equal instalments. Since principal is paid monthly, the amount of interest owed decreases throughout the year.

The cash position in the first month is 12 671 000 dong. This is the minimum required to run the business for four months. Therefore, the cash remaining at the end of the twelfth month needs to be at least this much in order to ensure there is enough cash for the following year. In fact, since sales are expected to increase in the second year, another cash flow should be projected for that year also. The projected cash balance at the end of 12 months shows how much of a margin is left for the following year's operational expenses.

In the example of the Praja Cooperative in Nepal, the enterprise intends to pay the principal of the loan back in the second year. This will leave it with a reduced cash on hand of only 122 831 Nepal rupees (NR). It will therefore need to plan other sources of financing by that time in order to maintain the same level of purchasing.

The cash flow projection also shows how profits are distributed to the enterprise participants. These have to be included in the cash flow, since they are expenses that will affect the amount of remaining cash.



TABLE E.9 Cash flow projection for year 1 - Quang Binh, Viet Nam, case study

	Total for the year	MONTH					
		1	2	3	4	5	6
Cash on hand		12 671 000 d	6 225 002 d	1 911 305 d	3 268 242 d	7 137 481 d	5 360 688 d
Sales	35 525 000 d	0	0	5 920 833	5 920 833	0	0
Total cash		12 671 000	6 225 002	7 832 138	9 189 075	7 137 481	5 360 688
Expenses							
Fees and royalties	0	0	0	0	0	0	0
Purchase of equipment	9 620 000	4 620 000	2 500 000	2 500 000	0	0	0
Equipment depreciation	3 174 600	264 550	264 550	264 550	264 550	264 550	264 550
Indirect labour/management	120 000	10 000	10 000	10 000	10 000	10 000	10 000
Repairs and maintenance	50 000	4 167	4 167	4 167	4 167	4 167	4 167
Stationery, communications	60 000	5 000	5 000	5 000	5 000	5 000	5 000
Sugar	1 225 000	102 083	102 083	102 083	102 083	102 083	102 083
Medicine (12 000 d per hive x 35 hives)	420 000	35 000	35 000	35 000	35 000	35 000	35 000
350 bottles x 1500d	1 575 000	0	0	262 500	262 500	0	0
Labour: (15 days/hive/year)	5 250 000	437 500	437 500	437 500	437 500	437 500	437 500
Interest payments (18%)	959 499	147 615	135 314	123 013	110 711	98 410	86 109
Principal payments	9 841 000	820 083	820 083	820 083	820 083	820 083	820 083
Total expenses	0	6 445 998	4 313 697	4 563 896	2 051 594	1 776 793	1 764 492
Total cash		12 671 000	6 225 002	7 832 138	9 189 075	7 137 481	5 360 688
Cash minus expenses		6 225 002	1 911 305	3 268 242	7 137 481	5 360 688	3 596 196
Principal balance		9 841 000	9 020 917	8 200 834	7 380 751	6 560 668	5 740 585
Payment towards principal		820 083	820 083	820 083	820 083	820 083	820 083
Remaining principal		9 020 917	8 200 834	7 380 751	6 560 668	5 740 585	4 920 502
Interest payments	959 499	147 615	135 314	123 013	110 711	98 410	86 109

US\$1 = 13 000 dong (d)

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MONTH						Total for the year	
7	8	9	10	11	12		
3 596 196 d	7 502 338 d	11 522 865 d	9 795 277 d	8 079 990 d	12 035 337 d		Cash on hand
5 920 033	5 920 833	0	0	5 920 833	5 920 833	35 525 000	Sales
9 517 029	13 423 171	11 522 865	9 795 277	14 000 823	17 956 170		Total cash
							Expenses
0	0	0	0	0	0	0	Fees and royalties
0	0	0	0	0	0	9 620 000	Purchase of equipment
264 550	264 550	264 550	264 550	264 550	264 550	3 174 600	Equipment depreciation
10 000	10 000	10 000	10 000	10 000	10 000	120 000	Indirect labour/management
4 167	4 167	4 167	4 167	4 167	4 167	50 000	Repairs and maintenance
5 000	5 000	5 000	5 000	5 000	5 000	60 000	Stationery, communications
102 083	0	102 083	10 2083	102 083	10 2083	1 225 000	Sugar
35 000	35 000	35 000	35 000	35 000	35 000	420 000	Medicine (12 000 d per hive x 35 hives)
262 500	262 500	0	0	262 500	262 500	1 575 000	350 bottles x 1500d
437 500	437 500	437 500	437 500	437 500	437 500	5 250 000	Labour: (15 days/hive/year)
73 808	61 506	49 205	36 904	24 603	12 301	959 499	Interest payments (18%)
820 083	820 083	820 083	820 083	820 083	820 083	9 841 000	Principal payments
2 014 691	1 900 306	1 727 588	1 715 287	1 965 486	1 953 184	0	Total expenses
9 517 029	13 423 171	11 522 865	9 795 277	14 000 823	17 956 170		Total cash
7 502 338	11 522 865	9 795 277	8 079 990	12 035 337	16 002 986		Cash minus expenses
4 920 502	4 100 419	3 280 336	2 460 253	1 640 170	820 087		Principal balance
820 083	820 083	820 083	820 083	820 083	820 083		Payment towards principal
4 100 419	3 280 336	2 460 253	1 640 170	820 087	4		Remaining principal
73 808	61 506	49 205	36 904	24 603	12 301	959 499	Interest payments

Prepare a balance sheet

The balance sheet is an accounting tool that tells the group on a given day how much its enterprise is worth and who owns it. It is also known as a statement of condition. It shows the financial strengths and weaknesses of the business and can help show a banker the working capital ratios in the business.

A balance sheet can be compared to a photograph, depicting an enterprise as it appears in a single instant. This is unlike the income statement (profit and loss statement), which can be compared to a motion picture, summarizing the business's income and expenses at the end of a specific period.

A balance sheet has two main sections, one listing the assets of the business and one listing the liabilities and capital or equity of the business. In accordance with the accounting equation, the two sides are always equal:

$$\text{Assets} = \text{Liabilities} + \text{Capital (Equity)}$$

This can readily be explained by the fact that all assets in a business are subject to the claims of creditors and owners. The aim of the interest group should be to increase the assets and equity. The balance sheet also tells whether management has been good or bad. All the items mentioned on a balance sheet actually represent accounts that are kept on each of those categories. For instance, under assets, a pick-up truck might have its own account showing the payments that have been made towards its purchase.



- ◉ **An asset** is anything of monetary value that is owned and operated under the name of the enterprise. Assets are generally classified as being current, fixed or intangible. Their liquidity refers to their ability to be converted into cash.
 - **Current assets** consist of cash and assets with high liquidity that are expected to be converted into cash within the coming year. This includes accounts receivable (money owed by customers) and inventory (merchandise, supplies, raw materials and parts).
 - **Fixed assets** consist of tangible property to be used over a period of years in operating the enterprise, such as land, buildings, machinery, equipment, motor vehicles, furniture and fixtures.
 - **Intangible assets** consist of items that are usually non-physical assets, such as trademarks, patents, copyrights and goodwill.

- ◉ **A liability** is a debt owed by the business. Liabilities show how much is owed on the assets listed in the enterprise. In other words, even though an asset may be used under the ownership of an enterprise, debts may be owed on that asset. Liabilities are classified as being either current or long-term.
 - **Current liabilities** consist of debts that are expected to be paid off within the coming year, such as accounts payable (money owed to suppliers and creditors), notes payable (money owed to the bank) and accrued liabilities (wages, interest, taxes, deposits and other amounts due but not paid as of the balance sheet date).
 - **Long-term liabilities** consist of debts that are not due to be paid within the coming year, such as mortgages, term loans, bonds and similar future obligations.
 - **Capital** is the difference between the assets of a business and its liabilities.

$$\text{Assets} - \text{Liabilities} = \text{Capital (Equity)}$$

Capital represents the amount of owner investment in the business, as well as any profits (or losses) that have accumulated. In other words, capital (or equity) is the part of the business that the owner actually owns clear of debt and it includes retained profits, or earnings from sales. These retained earnings represent the portion of net income earned in a fiscal period that has been retained or reinvested in the enterprise, rather than paid out as dividends (owners' withdrawals).

HOW TO PREPARE A BALANCE SHEET

The first step in preparing a balance sheet is to subtract the figure for initial investments and operating costs from the start-up costs for the enterprise. As in profit and loss statements, the projections for the balance sheet in the second year can also be worked out using the percent-of-sales method. The analysis of the balance sheet can be done using the financial ratios described below. The amount of cash on hand at the end of the year can be obtained from the cash flow projection for the last month. Depreciation of equipment can be deducted from the value of the assets (see Table E.10).

TABLE E.10 Balance sheet for year 1 - Quang Binh, Viet Nam, case study

	BEGINNING OF YEAR 1	END OF YEAR 1
ASSETS		
<i>Current assets:</i>		
Cash on hand	1 980 000 d	16 002 986 d
Accounts receivable	0	0
Raw materials inventory	1 071 000	0
<i>Total current assets</i>	3 051 000	16 002 986
<i>Fixed assets:</i>		
Equipment	9 620 000	9 620 000
(Less accumulated depreciation)	0	(3 174 600)
<i>Total fixed assets</i>	9 620 000	6 445 400
Total assets	12 671 000	22 448 386
LIABILITY		
Bank loan	9 841 000	4
Accounts payable	0	0
Total liability	9 841 000	4
EQUITY		
Equity	2 830 000	2 830 000
Profits re-invested	0	19 618 384
Total equity	2 830 000	22 448 382
TOTAL LIABILITY + EQUITY	12 671 000 d	22 448 386 d

US\$1 = 13 000 dong (d)

Calculate financial ratios

Financial ratios are tools that help the target group and potential investors assess the strengths and weaknesses of the enterprise.

RATIO OF EQUITY/ASSETS

A banker is interested in seeing what stake the owner has in the enterprise (i.e. does he owe more than he owns?). In the Vietnamese enterprise, at the beginning of the year the producers owned only 22.3 percent of the assets and owed the rest to the bank as liability (see Table E.11). The Praja Cooperative in Nepal owned only 6.7 percent of its assets as equity.

Outside investors are also interested in knowing whether the enterprise is well managed or not. The interest group can use this assessment, once its enterprise is active, in order to show a potential investor the strength and management capacity of the enterprise.

The assessment is done by looking at the change in ownership over time. For instance, as shown in Table E.11, at the end of the first year in the Quang Binh, Viet Nam, case study, equity increased from 22.3 percent to almost 100 percent of the assets. This shows that interest groups paid back their liability and reinvested profits in the growth of the enterprise. In the example of the Praja Cooperative in Nepal, equity as a percentage of the assets increased from 6.7 percent at the beginning of the first season to 15 percent at the end of the season and then increased to 100 percent when the full loan was paid back at the end of the second season.



**EXAMPLE****TABLE E.11 Comparison of equity/assets in Viet Nam and Nepal**

THE HONEY PRODUCERS OF QUANG BINH, VIET NAM	
Equity/assets beginning of first year =	$2\,830\,000\text{ d} / 12\,671\,000 = 0.223 \times 100 = 22.3\%$
Equity/assets end of first year =	$22\,448\,386 / 22\,448\,386 = 1 \times 100 = 100\%$
PRAJA COOPERATIVE, NEPAL	
Equity/assets beginning of first season =	$11\,017\text{ NR} / 163\,466 = 0.067 \times 100 = 6.7\%$
Equity/assets end of first season =	$26\,671 / 177\,671 = 0.150 \times 100 = 15\%$
Equity/assets end of second season =	$220\,752 / 220\,752 = 1 \times 100 = 100\%$

US\$1 = 13 000 dong (d); US\$1 = 71 Nepal rupees (NR)

Return on investment (ROI):

$$\text{Return on investment} = \text{Net profit} / \text{total assets}$$

The example from the Quang Binh, Viet Nam, case study for honey shows a ROI of 179 percent in only one year. This is very good compared to other investments that are possible in small enterprises. On the other hand, the case study of the Praja Cooperative in Nepal shows a ROI of 23 percent, which is lower, but still a reasonable amount compared to other investment options available.

EXAMPLE

TABLE E.12 Comparison of ROI for year 1 in Viet Nam and Nepal

THE HONEY PRODUCERS OF QUANG BINH, VIET NAM	
$22\,690\,901\text{ d} / 12\,671\,000 = 179\%$ (i.e. net profit is 179% of the original investment)	
PRAJA COOPERATIVE, NEPAL	
$37\,413\text{ NR} / 161\,017 = 0.23 = 23\%$ (i.e. net profit is 23% of the original investment)	

EXAMPLE

Financial plan for a bamboo basket weaver

In this enterprise, a basket weaver assembles 45 baskets, which she takes to the market in one load by bus. Her start-up costs show that she needed investment capital of 1090 Nepal rupees (NR) (US\$15.35) (see Table E.13). Since she had no capital of her own, she borrowed all of it from her community savings and credit organization (SCO) for an annual interest rate of 24 per cent. Her enterprise plan covered two months, the time needed for production and marketing. She projected her profit and loss and cash flow over six months, in which she could manufacture and sell three full loads (see Table E.14). For her calculation of net profit, she included her labour as an expense (see Table E.15). Using her cash flow projection, she was able to work out the amount of loan that she would require in order to manufacture each successive load. The balance sheet shows that with each successive load, she borrowed less and less capital, since she was saving her profits and reinvesting them into her business (see Table E.16).

TABLE E.13 Start-up costs for bamboo basket weaver

(One market load = 45 baskets)	
Bamboo	630 NR
Tax	420
Transportation and food	40
Total costs	1 090
Owner's capital	0
Local SCO	1 090 NR

US\$1 = 71 NR

TABLE E.14 Profit and loss for bamboo basket weaver

	UNIT PRICE	1ST LOAD	2ND LOAD	3RD LOAD
TOTAL INCOME FROM SALES	45 NR	1 800 NR	1 800 NR	1 800 NR
One market load, 45 baskets Sale price: 40 NR				
EXPENSES				
Variable costs (VC)				
Labour (50 days)	60	300	300	300
Bamboo	14	630	630	630
Tax	30	420	420	420
Fixed costs (FC)				
Transportation and food		40	40	40
Interest on loan (2 months x annual rate of 24%)		44	32	16
Total VC + FC		1 434	1 422	1 406
PROFIT/LOAD		366 NR	378 NR	394 NR

US\$1 = 71 NR

TABLE E.15 Labour cost calculation for bamboo basket weaver

Production capacity	1 basket/day, 45 baskets = 45 days
Total time to collect and prepare materials	5 days
Total production time	50 days
Equivalent wage for 1 day of labour	60 NR
Total labour	60 NR x 5 days = 300 NR

US\$1 = 71 NR

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TABLE E.16 Cash flow for bamboo basket weaver

	MONTH					
	1	2	3	4	5	6
Loan	1 090 NR	0 NR	800 NR	0 NR	400 NR	0 NR
Cash	0	310	366	386	744	364
Sales	0	1 800	0	1 800	0	1 800
Total cash	1 090	2 110	1 166	2 186	1 144	2 164
EXPENSES						
Labour	150	150	150	150	150	150
Bamboo	630	0	630	0	630	0
Tax	0	420	0	420	0	420
Transportation and food	0	40	0	40	0	40
Principal	0	1 090	0	800	0	400
Interest	0	44	0	32	0	16
Total expenses	780	1 744	780	1 442	780	1 026
Total cash	1 090	2 110	1 166	2 186	1 144	2 164
CASH MINUS EXPENSES	310 NR	366 NR	386 NR	744 NR	364 NR	1 138 NR

US\$1 = 71 NR

TABLE E.17 Balance sheet for bamboo basket weaver

	BEGINNING OF 1ST MONTH	END OF 2ND MONTH	END OF 4TH MONTH	END OF 6TH MONTH
ASSETS				
Cash on hand	1 090 NR	366 NR	744 NR	1 138 NR
Total assets	1 090	366	744	1 138
LIABILITY				
SCO loan	1 090	0	0	0
Total liability	1 090	0	0	0
EQUITY				
Owner's capital	0	0	366	744
Retained earnings	0	366	378	394
Total equity	0	366	744	1 138
TOTAL LIABILITY + EQUITY	1 090 NR	366 NR	744 NR	1 138 NR

US\$1 = 71 NR



STEP 6 | Obtain financing

The objective is to build the capacity of the members of the target group to identify the options available for raising capital to finance the enterprise, and to implement the steps that lead to obtaining the capital.

The financial plan in Step 5 helped the target group assess how much outside financing is needed for the enterprise. It was also able to establish what kind of ownership and management structure the enterprise would have. This decision was made partly on the basis of strategies for meeting financing needs. This section will discuss those financing sources in more detail.

How to identify options for enterprise financing

The target group needs to determine the internal financing that it can provide, such as land, buildings and equipment. Internal financing comprises funds that belong to the owners and become part of the assets of the enterprise. Additional funds will need to come from external financing from sources outside the enterprise, and can be either debt or investment capital from interested investors.

- ◉ External debt capital may take the form of negotiated loans from creditors, such as banks or suppliers of raw materials or equipment. Buyers may also provide advances negotiated according to projected future production and sales.
- ◉ External investment capital is raised through the sale of some portion of the ownership interest of the enterprise to an outside investor.

Financing needs of enterprises

The target group may need four basic types of external financing: seed money, start-up capital, working capital and long-term financing and/or growth capital.

- ◉ **Seed money** is needed to develop and refine the business concept and includes the costs associated with implementing the pilot phase in Step 7. Outside investors (including prospective buyers) are rarely willing to take the risk that exists in supporting an enterprise at such an early stage. This kind of debt financing therefore needs to come from internal sources or grants.
- ◉ **Start-up capital** usually consists of short-term working capital, needed to get the business going, and long-term capital, needed to obtain physical and human resources.

Although it may be easier to get start-up capital than to obtain seed money, it is still difficult to capture the interest of potential investors at this stage. Banks are normally reluctant to make start-up loans because the degree of risk involved is too high. However, certain rural development and credit banks may be in a position to help at this stage. Venture capitalists may also furnish start-up capital, but it will be based on a solid business plan that can show evidence of market acceptance of the concept, promise of large-scale returns on the money invested, and capable production and administrative skills on the part of the group.

- ◉ **Working capital** is short-term financing needed to build up current assets (inventory, accounts receivable and cash) and it is usually available from commercial banks and trade creditors. This kind of financing is usually the easiest for a viable firm to obtain.
- ◉ **Long-term financing** and/or growth capital used to finance the enterprise's fixed asset base (buildings, equipment) is usually a combination of long-term debt and owners' equity capital. For instance, after some time, a successful enterprise may encourage members to invest their own income in expanding production.

Options for raising investment capital

Target groups can raise investment capital through the following options.

- They can take a partner into the enterprise for either cash or collateral value (i.e. general and limited partnerships).
- They can form a cooperative. This is an association of many partners who buy shares in order to raise capital.
- They can attract investors by selling stock in a corporation. This is a way of obtaining cash without incurring debt. Profits are shared, but management is not shared.
- They can enter into a joint venture with investors who are usually looking for opportunities to gain a financial interest in innovative or high-tech enterprises that start on a small scale but have large-scale potential. Although this is another way of raising capital without debt, this type of partner often demands a controlling interest in management.



EXAMPLE

In the Quang Binh, Viet Nam, case study it was seen that the five members of the interest group provided some of the share capital, and they will distribute the profits according to the amount of honey that they produce and sell. They obtained the remainder of the capital from a bank loan.

In the case study of the Praja Cooperative, interest groups were offered membership through the purchase of shares in exchange for cooperative benefits, such as decision-making and dividends. In addition, they received a grant and a soft loan in order to cover the rest of their financing needs.



STEP 7 | Initiate the pilot phase and training

The objective of Step 7 is to test the strategies developed in previous steps and to prepare the target group for managing the enterprise. During this phase the facilitator will see the importance of pilot studies and market testing as a strategy for reducing risk in a new venture. The facilitator will design training that aims to ensure that the target group has the capacity to implement the strategies that it developed.

Having secured financing, the group members are ready to begin implementation of their enterprise. However, they need to initiate their marketing efforts one step at a time and increase their knowledge base before they take any unjustified risks.

The objective of the pilot phase is to test the market before a large-scale initiative is planned. It will serve in itself as training for the target group. It will help the group solve the problems of the management, production and delivery mechanisms that it has designed for the enterprise, and it will help the group identify its training needs. It will ensure that the training is designed according to the market demand and on the basis of its real needs. In addition, it can help the facilitator identify the interest groups that are really serious about and committed to the enterprise.

Test the strategies and prepare the target group

The facilitator will help the target group:

- review the results of the pilot phase and assess whether the enterprise development strategies need any adjustments or changes; and
- assess the training needs of the members of the target group in order to implement the enterprise strategies.



Pilot phase

Since the enterprise is in its early stages, the goals and objectives that were developed earlier can be regarded as pilot initiatives. In the beginning, the facilitator helps the target group plan frequent workshops in order to make the most of this opportunity to work closely with it and facilitate learning.

Pilot initiatives can be considered as a way of following an action-research approach in which small-scale activities can:

- prepare the target group to participate in the enterprise and to adjust its enterprise development plans according to new information on the business environment;
- build its capability to manage the enterprise;
- help it finalize technical aspects of production; and
- guide it in testing the first samples of production in the target market or market niches.



EXAMPLE

In the Quang Binh, Viet Nam, case study, in order to check the assumptions made regarding the market interest in its product, the target group needed to take samples of the first batch of production to the prospective buyers and have them check the product. It then received suggestions from the buyers that helped ensure that the final batch at the end of the season closely matched the requirements of the customers. If the product does not meet the expectations of the buyer, additional training might be needed for the interest group in order to improve the product's quality.

Similarly, in the case of the Praja Cooperative in Nepal, the first season of production was an opportunity to test many of the strategies that were developed for the enterprise plan. Methods for extraction of the resource, interest among the target groups, collection systems, regulatory procedures, buyer interest, gender involvement, and the status of disadvantaged members of the community were all evaluated during the pilot phase. On the basis of the information obtained, improvements in the strategies could be planned for the next season. For instance, in the area of resource management, it became clear that although the farmers said initially that they were aware of sustainable harvesting methods, and even though rules were in place to prevent collectors from selling material that was harvested in an unsustainable manner, still in some cases these rules were not followed. Therefore, before the next season, workshops and training on this issue will need to be organized and participatory forest resource assessments will need to be planned to supplement the information obtained from the earlier interviews conducted during Phase 1.

A pilot phase can be very useful when developing handicraft products such as grass brooms, bamboo baskets and woven fabrics from natural fibres. Manufacturing can be initiated on a small scale in order to check production quality and the ability of the craftspersons to get the orders ready within the specified delivery time.

Train the target group

The enterprise strategies will almost surely include some form of training. Each of the areas of enterprise development requires a different kind of capacity building. Although the target group has to integrate all these skills in order for the enterprise to be successful and sustainable, skill-building normally has to be coordinated through agencies specializing in certain sectors.

How to facilitate training for the target group

The facilitator can help the members of the target group identify their training needs. It is necessary to link up their strategy with the capacity-building that they will need to implement that strategy, and the facilitator should suggest appropriate indirect actors (agencies) and funding channels that might support the activities. Several methods can be used to transfer skills. In the case of traditional handicraft or cultivation methods, existing experience within the community is often available, and the best trainers may be other farmers who can share their experience. In addition, study tours to observe other communities can also be a good learning experience. Demonstration plots for nurseries and domesticated medicinal and aromatic plants are also very useful. Apprenticeships for learning specific skills can be given to a group representative who will then share the new skills with the others.

TRAINING OPTIONS

There are options for training in each of the four main issues to be addressed in developing an enterprise.

- ▲ **Marketing** These options include enterprise literacy, budgeting, record-keeping, management of cooperatives and of producer savings funds, inventory and stock control, customer liaison, product development, quality control, production management, and identification of market opportunities.
- ▲ **Resource management** Among these options are harvesting, cultivation, community mechanisms for resource control, management of common property resources, and intellectual property rights on local resources and products.
- ▲ **Social development** Options include group formation, strengthening and facilitation, conflict resolution for resource management, and legal advocacy for tree and forest products.
- ▲ **Science and technology** These options include processing and storage technology.

Assistance in obtaining training will depend on what sector offers it. Facilitators may find that training offered by government is appropriate, particularly because of the extension services. In many cases, the only input needed to make the training effective is market demand orientation and capacity-building for the extension workers, in addition to support in follow-up to the communities.



STEP 8 | Monitor progress and deal with change

The objectives of Step 8 are to ensure that members of the target group have the ability to foresee unexpected events and are prepared to cope with them, and to ensure that the enterprise can be judged for its performance on an annual basis according to the progress it has made in achieving its stated objectives. The facilitator needs to learn how to carry out an annual assessment of the business environment in order to help the enterprise stay competitive in a changing marketplace. This will ensure that the objectives formulated in the enterprise development plan are still realistic. Annual planning provides a way of measuring progress and identifying problems as they arise and then developing new strategies to correct them.

The major goals of monitoring are:

- to test the success of the activities;
- to learn from experience; and
- to prevent mistakes and give an early warning of ecologically or culturally negative impacts and economically non-viable options.

The facilitator needs to help the target group set up a system that ensures that it will monitor the performance of the enterprise plan and adjust it for unforeseen market conditions. The monitoring system should consist of tools for gathering information for a baseline survey and of an analysis of that information, at least on an annual basis, so that appropriate decisions can be taken regarding what must be done to ensure achievement of stated sales and profit goals. In addition, if the enterprise aims to be sustainable, the target group needs to evaluate regularly the impact of its activities on the ecology and on the social issues raised during strategy development.

Develop a monitoring and evaluation system

Choosing the proper indicators is the first step in a good monitoring and evaluation system. Meaningful indicators can be developed only with the participation of the target group. Monitoring can be done at the output, effect and impact level. Each level requires different kinds of indicators, which should be linked to the objectives and strategies of the enterprise. Collection of baseline information about the community can then be planned according to the indicators that are used.

For example, in order to monitor the income obtained by cooperative members and non-cooperative members in the community, it is necessary to collect data from each collector who brings the product to the weighing station at the road-head. Data that should be obtained includes the name and address and gender of the person, in addition to the amount of product that they bring and the cash they receive.

Effect indicators try to measure the effect that the activities had on the target group or its enterprise. For example, did the participatory planning meetings give the group a greater understanding of the markets? Did more women become involved in the second year as a result of successful marketing in the first year? Did the group start cultivating the product in order to ensure supply for the next season? Similarly, impact indicators may try to measure the impact of the enterprise on the community as a whole. How was the wealth ranking affected by the enterprise? Did the more disadvantaged members benefit? In what way?

How to help the target group do annual evaluations

Facilitators will need to organize workshops with representatives of interest groups for a product. In these workshops, the study of the enterprise environment that took place in Step 1 will be repeated, although not in the same depth. Once the information has been gathered, facilitators need to discuss the results of the study with the interest group. Working groups should again be formed for each of the four areas of enterprise development, and working group members will go through the objectives and strategies developed in the previous year in order to determine whether those targets were achieved. The activities of the previous year should be evaluated by each group and the strengths and weaknesses within that area of enterprise development should be identified. On the basis of this assessment, the group will develop its goals, objectives, strategies and action plans for the following year.

During the annual planning workshops, target groups should share their experiences in working with the enterprise in the previous year. A participatory environment should be enabled that gives everyone opportunities to make suggestions for improvements. Once the interest groups have developed a plan for the following year, they need to follow through with implementing it. In order to ensure this, a process should be facilitated through which all the enterprise participants are directly involved in the annual formulation of the plan and have a feeling of ownership about it. Annual planning should result in the delegation of specific tasks to individuals who are to be responsible for carrying out those activities.



EXAMPLE

In Nepal, a non-governmental organization (NGO) had been supporting the ethnic group of the Praja in a plan to use the product from their chiuri trees in order to make a juice concentrate that they bottled and sold in Kathmandu. However, after two years, sales dropped and the NGO was left with a large surplus stock. This was because of problems such as difficulties in hygiene, packaging, promotion and distribution of a new product to a new market. When the NGO conducted an MA&D exercise with the Praja groups, they decided that instead of trying to overcome the difficulties, they would instead target an existing market for oil from chiuri seeds, which is used for lighting lamps. Since this is not a food product, hygiene was not an issue, and when they visited potential customers in advance they found that distribution would be much easier than for the juice product.

As regards the issue of **resource monitoring**, the Praja Cooperative had been formed a year later in the same project area, and another product, a medicinal herb used in making tea, was collected. The cooperative members agreed among themselves on the quantity that could be sustainably collected. Having obtained the necessary permits from the district forest officer (DFO), they began to harvest it from their national forest. However, many other local people heard about this opportunity and also started to collect large amounts of the product. These people were not originally included in the project cluster villages, nor had they been interested in joining the cooperative. Concerns of resource depletion would be addressed once the harvest area was handed over as a community forest (the process had been started and it was expected that it would be finalized before the next season). Forest user groups (FUG) would then have to control a predetermined area and ensure that other villagers do not harvest from it.

During the last harvest, there was an example of **social impact** that was identified through monitoring. Some of the cooperative members hired very poor Praja to collect the product in the forest and paid them nominal daily wages. As a result, some households received a much larger income than others. Further investigation will be needed to understand the economic situation of the disadvantaged households. However, the situation probably arose because these households are so poor that they needed immediate cash for the daily collection, or perhaps because they were in debt to the other households and needed to pay them back in labour. They could not afford to buy cooperative shares and they had no time to go to planning meetings, consequently they were not informed about the opportunity. The marginalization of these disadvantaged households needed to be addressed with some new strategies during the subsequent year.

In regard to **institutional monitoring**, the regulations of the DFO were not clearly understood during the first year. Although permits were obtained by the cooperative in order to collect the product from the forest, the permits should have included a clause stipulating that the product would be stored at the rented site in the market town before it was transported to the final buyer. Because this clause was not included in the permits, the rangers did not allow the product to leave the small village at the road-head near the collection area, where there was no adequate, safe storage. Fortunately, a buyer who could accept the product immediately was found right away, so that the material was not put in danger of deterioration or theft. This was a good learning experience for the cooperative members, and through it they have understood that they need to obtain the appropriate paperwork for the next season.

Monitor progress

Economic analysis

The economic objectives of the target group were assessed during Phase 1. This can serve as a baseline with which to compare progress in achieving those objectives after a period of time. As mentioned in the example above, it can give a good indication of whether any very disadvantaged groups are being marginalized by the process. It is particularly useful to document whether increased income results in a greater commitment by the target group to conserve its natural resources.

MARKET/ECONOMY ANALYSIS: FINANCIAL PROJECTIONS

The function of financial projections (or budgets) is to single out components that need to be measured and ensure that meaningful performance can be measured against predetermined standards.

The financial projections made in the first year should be discussed by the target group in order to prepare more accurate statements for the next period. Facilitators should help members of the group identify errors in judgment, since these become learning experiences that can be applied to the next cycle of planning. Involvement of all the participants in the budget gives them experience in understanding the mechanics of the enterprise and ensures that the objectives that are developed are realistic.

The objective of the monitoring system is to compare marketing performance with the annual projections. Data that should be reported at regular intervals should include sales, gross profits and expenses. This kind of reporting has the advantage that it pinpoints problem areas, highlights serious deviations from the marketing plan and budget projections, and provides data for future planning. Using this information, the target group can evaluate progress according to such criteria as reported expenses, marketing mix, planning assumptions, sales forecast and pricing.



EXAMPLE

A community-based handicraft production cooperative owned and managed by women was having problems maintaining its market links with the capital. The local women could not see the relevance of marketing efforts to improving their sales and the turnover of inventory. The facilitator proposed hiring a highly paid marketing manager who would be based in the city. This proposal was difficult for the women to accept, however, because they were empowered in the management of the enterprise, they were suspicious, and they were also reluctant to make the investment. In the end, the production manager, who had worked with the women for some time and had already established a relationship with them, was given the additional role of doing the marketing in the city.

For this discussion to be meaningful to them, the producers had to become aware of such factors as inventory and sales targets, marketing strategies, and salaries for outside expertise. There was no perfect solution to this problem. However, by discussing it and the possible options for solving it, the target group became aware of the financial implications of its decisions. The discussion should be repeated after it has had time to see whether the strategy it chose was effective or not.

RESOURCE MANAGEMENT/ENVIRONMENT ANALYSIS

An essential aspect of monitoring should include ensuring that the enterprise does not have a negative impact on the ecological environment through harvesting of the resource. In Step 1 of Phase 3, three ways were mentioned of doing rapid assessments of a forest in order to determine whether the extraction of a species is sustainable. However, it may be difficult for local target groups to hire forestry experts on a regular basis. In that case, the facilitator needs to ensure that the groups themselves understand the basic methods to be used for rapid assessment of the forest and that they fully recognize the importance of regular monitoring.

Annual reviews of the enterprise should include an appraisal of the impact of harvesting, and if necessary, discussion and implementation of corrective measures. For example, rotation cycles can be increased if the plant regeneration is slower than anticipated. In many cases, it may also be possible for the communities to initiate trials in agroforestry conditions of domestication of a species. Should harvesting result in a negative impact, the interest group can then decide to rely more heavily on the planted stands of a species. Other strategies may be needed, such as devising a product mix in order to reduce dependence on a single product, thereby promoting only limited harvesting of that species.

SOCIAL/INSTITUTIONAL ANALYSIS

The social impact of the enterprise can be assessed against a predetermined set of indicators that were used initially for gathering information. For example, the role of women in decision-making for product selection, pricing or income distribution can be assessed, and the impact on marginalized groups in a forest user group can be determined. The capacity building of a community cooperative or association of forest collectors can be assessed. Potential negative impacts should be carefully identified and monitored. For example, a successful enterprise may cause parents to take their female children out of school so that they can help them with processing of a product. The only way to monitor this change is by establishing a baseline for households that indicates the school attendance of the children, and by later comparing the situation with this baseline.

POLICIES, RULES AND REGULATIONS

The interest groups must monitor national and international policy carefully, either by themselves or with the support of a national network. Otherwise, they might easily be caught unprepared, which could result in a serious problem for the enterprise. They should maintain a close relationship with the local forest officer in order to be able to negotiate in the case of an unclear ruling. If national policy is about to be modified in a way that is not in their favour, they need to lobby as members of the national network. If international rules that may affect their enterprise are proposed, they should respond rapidly. For example, the interest groups in Karnali, in midwest Nepal, had built a distillation unit and were making jatamansi oil (*Nardostacys*), when they heard that a proposal had been submitted for placing jatamansi on the list of the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES). This would have dealt a serious blow to their enterprise. They quickly wrote to the committee to state their case before the ruling could be ratified.

SCIENCE AND TECHNOLOGY ANALYSIS

Interest groups need to keep informed about new technology that can make their product more competitive either by decreasing the production price or by improving the product. Processing technology, such as improved drying, agrotechnology to accelerate growth rates, and oil extraction machines running on biological fuels, are just some of the areas in which technology is rapidly changing. Infrastructure improvements, such as additional telephone lines and extensions of roads, can open up new markets for the groups and their products.

MARKET INFORMATION SYSTEMS

It is important that enterprises develop market information systems, which are a tool that enables them to stay in touch with the changing reality outside of their own locations. Data should not only be collected on a regular basis, but it must also be disseminated effectively and then analysed so that decisions can be made on the basis of perceived changes in market conditions.

This section shows that information is needed not only in regard to changes in prices and customer needs, but also in the areas of national and international policy and technology. Therefore, the interest groups need to devise a way of staying in touch with the outside world. Facilitators can assist this process by organizing study tours so that representatives of the village-based enterprises can become familiar with the outside sources of information. These could include research institutions, national networks in the forestry sector, and private sector traders with export linkages.

**EXAMPLE**

The Praja of Chitwan district in Nepal were linked up with the Butwal Technology Institute, which was developing an oil extraction machine. The institute was interested in testing chiuri seed as a potential raw material and contacted the Praja Cooperative in order to get an initial supply of several hundred kilograms for testing purposes. If the trials are successful, the institute will provide training for the Praja to learn how to use the machines, and it could also act as a facilitator to help them obtain financing.

The annual planning exercise conducted by the target group needs to include an assessment of all the areas mentioned above. Facilitators should support the group during this critical period. After going through a few cycles of planning and implementation, the members of the group will realize the usefulness and relevance of the exercise, and they will then be motivated to do it on their own, with minimal support from outside. Facilitators can also encourage participation and capacity building in a local NGO as part of their support to the group, so that in the future there will be a core group of experienced people in the area who can support the group as consultants if requested.

**EXAMPLE**

Strategies for dealing with change need to be developed by a company distilling medicinal herbs into oil in the mountains of the Karnali region of Nepal. During the first two or three years of operation, the unit did well by offering a good price for raw material, and thanks to an ample supply it produced 20 to 30 litres of oil for Indian and export markets. However, in the third year, local traders started offering higher prices for raw material, with the result that the distillation company could not obtain enough of it to operate at full capacity.

The company did not have the capital to be able to pay advances to collectors, which made it less attractive for them to sell the product to the company. In addition, it took time to sell the oil. The choice was either to sell it at Indian prices and barely break even or store it until the time when the much higher export price could be obtained.

The company's overhead costs were very low, so it could afford to remain idle for several months. The owners decided to reduce production of the herbs to a smaller scale and at the same time to start developing other oil products. It would wait until it could have an assured export market before deciding to invest more capital in the purchase of raw material, when it would perhaps offer advances or competitive prices in order to win out over the other traders.



ANNEX | ENTERPRISE DEVELOPMENT PLAN 1998

OF THE PRAJA COOPERATIVE LTD¹ Chitwan, Nepal

Enterprise description

This enterprise will be implemented by the Praja Cooperative Ltd. Five administrative village development committees (VDC) of Chitwan district will be involved. They represent the villages of Lothar, Korak, Siddhi, Shaktikhor and Kaule, and include a total of 889 targeted households that have already received social mobilization training from the Praja Community Development Programme.

The function of the cooperative is to collect semi-processed raw material from households that are gathering products in the wild from community and national forests and are cultivating on common property or private lands. The cooperative will store the products at the main market centre near the collection area until a good price can be obtained, and will arrange delivery to final processors or manufacturers.

Gaps and needs fulfilled by the product

Products offered by the road-head traders are not of consistent quality. Their products are found improperly dried, packed and stored; infected with moulds and pests; and contaminated with foreign matter. Sometimes they also purchase fresh product that has not been dried and keep it in that condition for several days. Such products are of very low quality and do not store well. In addition, product size (especially of gurjo) does not fulfil the requirements of processing machines.

The cooperative will address all these issues and will offer the products with best quality, best service, lowest price and best value.

Competition

The major competitors of the cooperative are the road-head traders of Taadi, Shaktikhor, Lothar and Manohari. Most of these road-head traders have similar characteristics. Table E.18 shows the SWOT (strengths, weaknesses, opportunities, threats) analysis and comparison of the cooperative with road-head traders.

¹ Prepared with the assistance of staff from the Praja Community Development Programme (PCDP/SNV-Nepal) and the School for Ecology, Agriculture and Community Works (SEACOW).

TABLE E.18 SWOT (strengths, weaknesses, opportunities, threats) analysis and comparison with road-head traders - Praja Cooperative, Nepal

	PRAJA COOPERATIVE	ROAD-HEAD TRADERS
PRODUCT		
Quality	Offers quality products passed in quality control	Offer low-quality products and want to sell all their stock
Total supply	Meets the demand	May not be able to meet the demand, as the traders also purchase from the cooperative working area and they will have to compete with the cooperative in purchasing
Storability	Good	Poor
PRICE		
Pricing policy	Competitive pricing	Competitive pricing
Conditions of payment	Payment on delivery	Payment on delivery
PROMOTION		
Advertising	Cost-effective media will be used if found to be appropriate	No
Discounts	No	No
Credit terms	Yes, if trusted, but for no more than one month	Yes, if trusted, but for no more than one month
DISTRIBUTION		
Distance factor	No problem	No problem
Market channel	Has information on a few channels	Has information on several channels
IMAGE	Yet to be established	Already established
SERVICE	Competent, reliable, responsive, gate supply on time	Competent, reliable, responsive, gate supply on time
CLASS OF BUYER	Herbal or ayurvedic medicine companies in Nepal	Herbal or ayurvedic medicine companies in Nepal

PHASE 3: Plan enterprises for sustainable development

ANNEX: Enterprise development plan 1998 of the Praja Cooperative LTD

STRENGTHS	Committed to offering quality-controlled products	Possess established image of non-timber forest product (NTFP) trader
WEAKNESSES	Has insufficient experience in marketing	Not conscious of the quality of the product and depend mostly on the cooperative members for the products
OPPORTUNITIES	Buyers prefer to purchase quality products with quality service	Buyers choose them to be assured of the supply
THREATS	Buyers may not believe in the cooperative, as it has not established an image in NTFP marketing	Chances of being unable to meet the order, and threat that the cooperative may over take their NTFP trade

Mission statement

The Praja Cooperative Ltd is a producer-owned business organization dedicated to providing the cooperative members with sustainable income from NTFPs within the context of social, managerial and environmental sustainability. It aims to promote saving by its members, self-sufficiency and mutual cooperation. It will encourage members to work together to fulfil their needs and uplift their socio-economic status while at the same time promoting local culture.

Goals

Note: all values are expressed in Nepal rupees - US\$1 = 71 Nepal rupees (NR).

In its first four-month season it intends to achieve:

- a sales target of 201 281 NR;
- a supply/quantity target of 7560 kg;
- a net profit target of 37 413 R;
- benefits for the members by increasing their income from NTFPs by 25 percent;
- a ROI of 23 percent (as a function of net profit/initial assets); and
- a break-even point of 1162 kg (31 374 R).

MARKETING AND OPERATIONAL PLAN*

Products offered

In the first season, the following products will be offered:

- destoned, dried amala (*Embllica officinalis*);
- cut and dried gurjo (*Tinospora cordifolia*);
- destoned, dried harro (*Terminalia chebula*); and
- destoned, dried barro (*Terminalia bellerica*).

These products will be cleaned and properly dried (without any residual contamination from smoke) and will be hygienic and free of impurities, pest infestation and mould growth.

Processing

- Products will be processed using local technology. The processed products will be of high quality in order to satisfy the quality requirement of demand. They will be processed on the basis of information disseminated by the marketing information system.
- Processing will include sorting, cleaning, grading, peeling, destoning, steaming, drying and storing in hygienic conditions. The finished products will be properly packed in clean, dry and hygienic sacks provided with polyethylene liner. Storability of the processed products under normal conditions will be at least one year.

Storage

- Special care will be taken in storage of the products. Sacks will be stored in a cool, dry and clean place and protected from rain and smoke. If the products are to be stored on the ground floor, a flat structure made of wood or bamboo will be raised above the floor level to protect them from damp rising from the ground.

Quality control

- A representative selected/elected from the group will be responsible for controlling the quality of the products of their group.
- Quality, packing and storage conditions of the products will be checked in the household by the representative before they are delivered. The representative will have the right to reject low-quality, improperly packed and improperly stored products. Rejected products will not be delivered to the product collection centre.

* Corresponds to market/economy strategy (see p. 20).

- Quality control will be conducted randomly also in the collection centre. If anyone is found delivering rejected products and cheating the cooperative's representative, all the products delivered by that person will be seized and the person may be excluded from the cooperative. Similarly, if anyone adulterates the products that have passed quality control and delivers them to the collection centre, that person will be charged in the same way.
- The representative will use the quality control parameters shown in Table E.19. Quality control will be conducted using visual methods.

TABLE E.19 Quality control parameters and standards - Praja Cooperative, Nepal

PARAMETERS	STANDARDS
PRODUCTS <ul style="list-style-type: none"> ■ Appearance ■ Dryness ■ Impurities (straw, soil, animal excreta, etc.) ■ Mould growth ■ Pest infestation ■ Smokiness 	<ul style="list-style-type: none"> ■ Appealing (each product will have its own colour) ■ Dry as a bone ■ None ■ None ■ None ■ None
PACKING	<ul style="list-style-type: none"> ■ Use of sacks with polyethylene liner ■ Airtight packing
STORAGE CONDITIONS	<ul style="list-style-type: none"> ■ Cool, dry and clean storage place ■ Flat structure made of wood or bamboo, raised above floor level to protect from damp rising from the ground ■ Adequate measures to protect the products from rain, smoke and rodents and other animals

Product delivery to collection centre

- Only the products that have passed quality control will be delivered to the collection centre. The producers themselves will deliver their products to the collection centre. At the time of delivery, they will be paid the price fixed by the cooperative for their products.

Product collection centre

- There will be three product collection centres. The collection centre in Khurkhure will serve the groups of Korak VDC. The collection centre in Shaktikhor bazaar will serve the groups of Siddhi and Shaktikhor VDC. Similarly, the collection centre in Mowakhola will serve the groups of Kaule VDC.
- In each of these collection centres, a store will be rented. The representative of the corresponding VDC will play a major role in making all the necessary arrangements in the collection centre.

Marketing strategy

- This enterprise will adopt offer-differentiating and positioning strategy. The differentiation variables will be:
 - product (appearance, quality, size, storability);
 - services (gate supply, competence, reliability, responsiveness);
 - personnel (competence, honesty, courtesy, credibility, reliability, responsiveness, communication); and
 - others (cooperative mission, profit/savings distribution).
- The cooperative will effectively signal to the target market how it differs from its competition. The major positions to promote will be:
 - best quality;
 - best service;
 - lowest price;
 - best value; and
 - profit/savings returning to the community.
- The cooperative will follow a competitive pricing strategy. It will study the size of demand for the products and the prices offered by the processors and, finally, it will make decisions on how long to store and on when and at what price to sell the products. However, it wants to be known for quality, not for bargain prices.

Market options

This enterprise initially will consider the two product and market development options:

- to make existing products for existing markets; and
- to make existing products and add new markets.

After working on these options for two to three years and after building enough confidence in marketing, two additional options also will be considered:

- to introduce new products to sell to existing markets; and
- to introduce new products to sell to new markets.

Marketing information system

The central component of the MIS will be the marketing arm of the cooperative. It will organize the collection, analysis and communication of marketing information.

Telephone contact will be established in order to collect the marketing information. marketing information will include the quality, quantity, price and service requirements of demand. This information will then be analysed and the results communicated to the executive committee (EC) of the cooperative. Members of the EC will communicate this information to all of the members, the primary producers.

Targeted market outlets

The cooperative will not depend upon one buyer. Targeted market outlets are the manufacturers of herbal tea and ayurvedic preparations (medicines) of Chitwan, Kathmandu, Hetauda, Butwal, Gorkha and Parsa, in Nepal. No Indian market outlets are targeted this year, as the price of NTFPs offered in India is very low. Appropriate buyer(s) will be identified on the basis of the results of analysis of the marketing information.



RESOURCE MANAGEMENT/ENVIRONMENT PLAN

Harvesting of NTFPs

- Harvesting will be done only from mature stands.
- Destructive harvesting practices that lead to a decrease in the resource base or extinction of the products and consequent disappearance of the activities related to them will not be followed.
- Amala, harro and barro will be harvested by climbing the trees, shaking the branches or bending the branches by using a *tango* (a long stick with a hook at one end). No trees or parts of trees will be cut down, trimmed off or hacked away.
- Gurjo will be harvested without destroying the resource base. When the gurjo stem is harvested, several of the bottom and upper parts that are entwined around other plants and possess regenerative potential will be left intact.
- If overharvesting of the NTFPs (e.g. gurjo) is likely to take place in the effort to generate a high level of income, the forest will be divided into several parts on the basis of the calendar cycles of the products or the biological regeneration cycle, and the products will be harvested by rotation in the various parts of the forest.
- If anyone neglects to observe this plan, he faces a charge of evading forestry laws and regulations. In such a situation at the village level, the person will be fined up to 500 NR per plant, all the harvested products will be seized, and/or the person will be excluded from the society and/or the cooperative. The money obtained this way will go into the cooperative's reserve fund.
- These plants will not be used as fodder.



Obtaining fuelwood

Only dead trees and felling debris will be used for fuelwood. No green trees will be cut down to obtain fuelwood.

Harvesting time

The harvesting time schedule will be as shown in Table E.20.

**TABLE E.20 Harvesting schedule -
Praja Cooperative, Nepal**

NTFP	STARTING DATE
Amala	First week of October
Gurjo	First week of November
Harro	First week of October
Barro	First week of November

Plantation of NTFPs

- Table E.21 shows the numbers of saplings for NTFPs that will be planted in the marginal land by each of the households.

**TABLE E.21 Number of saplings for NTFPs -
Praja Cooperative, Nepal**

NTFP	NUMBER OF SAPLINGS
Amala	200-300
Gurjo	200-300
Sinkauli	200-300

Taking over the community forest

- Village-level discussions will be continued and the official process will gradually be completed to take over the forest as community forest.

SOCIAL PLAN

Relations with non-members/non-shareholders

- Membership in the cooperative will be open only to Prajas. Forest users of the same forest who do not have membership or shares in the cooperative but are eligible for membership or for buying shares can participate in the cooperative initiatives. However, the cooperative will not provide patronage refunds to these non-shareholders. Cooperative representatives selected or elected from the same forest user group (FUG)-level group will play a major role in keeping a record of the accounts of shareholders from their community.

Relations with outsiders

- Forest users of the same forest who cannot be accepted as members or shareholders of the cooperative will not be included in the cooperative initiatives. However, they can sell their products to the cooperative at the rate that it offers to them. This rate may be different from that offered to the shareholders. A cooperative representative selected or elected from the same or the nearest FUG-level group will play a major role in making the necessary arrangements.

Relations with road-head merchants

- Attempts will be made to maintain and improve the existing relationships with the road-head merchants.

Provision for the poor

- The poorest people or households in a group that are interested but are unable to buy share(s) in the cooperative can acquire share(s) by contributing NTFPs during the product collection period. Identification of the poorest households and arrangements for selling shares to them will be the responsibility of the representative who is selected or elected from the same FUG-level group.
- No one in a group will use the poor selfishly or unfairly to harvest, process and/or deliver products for individual advantage or profit. If someone is found guilty of such unjust actions against the poor, he/she will be excluded from the society, and/or the products will be seized and returned to the poor. The cooperative representative selected or elected from the same FUG-level group will play a major role in implementing this plan.
- No one in a group will buy products from the poorest households at a lower price than that offered by the cooperative and bring them to the product collection centre to obtain a higher price. If someone is found doing such an injustice to the poor, he/she will be excluded

from the society, and/or the products will be seized and returned to the poor. The cooperative representative selected or elected from the same FUG-level group will play a major role in executing this plan.

- All members in a group will clearly communicate information about the cooperative and market information to the poor.

Provision for women

- Half of the income generated from the products by a household will be handed over to women.
- Equal opportunities will be provided for women so they can be directly involved in all aspects of cooperative affairs. No one will discourage their participation under any circumstances.
- The EC of the cooperative will play a major role in the execution of these plans.

INSTITUTIONAL PLAN

Obtaining legal rights of access to the resources

- The cooperative will establish linkages with like-minded and supporting organizations/institutions and become involved in advocacy.
- The cooperative will actively seek to establish good relations with the DFO on the basis of transparency and accountability in all transactions.
- The cooperative will register with the Department of Cooperatives and will seek to take advantage of their capacity-building services.

SCIENCE AND TECHNOLOGY PLAN

Research and development

- The objective is to develop a line of high-quality products and packaging by obtaining information on customer needs from the market study tour, and to investigate the location of expertise on technology improvements.

Risks (scenarios)

The following factors contribute to risk:

- overharvesting of NTFPs;
- alternative fruiting characters of some NTFPs;
- evasion of cooperative principles by the members;
- poor leadership quality of the cooperative representatives;
- poor marketing knowledge and skills;
- dependence on a sole buyer;
- decrease in product demand;
- decrease in selling price;
- change in government policies;
- inflation; and
- uneven distribution of cooperative benefits.

To minimize and/or handle these risks, training will be given to the groups, the EC and the accounts committee members, and/or discussions will be held regularly in the group to further enhance its capacity to handle the different aspects under risk.

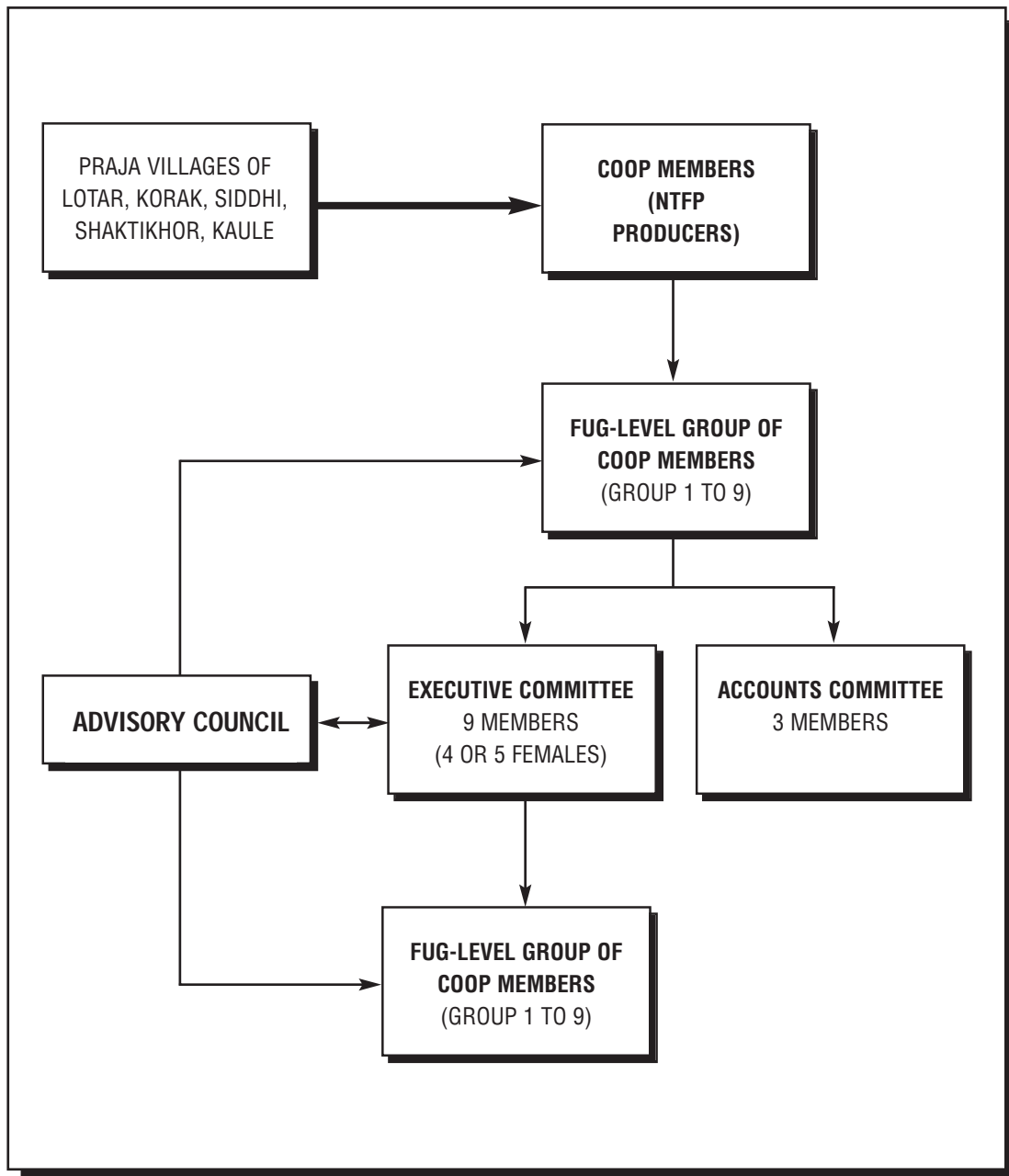
A loss recovery refund in the cooperative covers the monetary loss (if any) of the enterprise.

TABLE E.22 Financial plan - Praja Cooperative, Nepal

Break-even point (for the product mix)			
Break-even point in kg	$\frac{5\ 807\ \text{NR}}{27\ \text{R} - 22\ \text{R}}$	=	1162 kg
Break-even point in revenue	$1162\ \text{kg} \times 27\ \text{R}$	=	31 374 R

Table E.22 shows that the break-even point is 1162 kg, or 31 374 R, out of a projected total of 7560 kg (or 201 281 R) for the season. This is a comfortable margin for reaching the target profits.

FIGURE E.1 Organization structure of the Praja Cooperative



Payback period on investment

Total start-up costs are expected to be 161 017 NR (US\$2268). Financing will be provided in part by member share capital (220 members who purchase shares of 50 R each), partly by a grant from the project (75 000 R) and partly by a soft loan, also from the project (75 000 R). The loan will be paid back by the end of the second season of collection. The loan and grant will be administered with assistance of an NGO, the School for Ecology, Agriculture and Community Works (SEACOW).

ROI in the first season

Table E.23 shows ROI for the Praja Cooperative in the first season.

TABLE E.23 ROI in the first season - Praja Cooperative, Nepal

$\frac{\text{Net profit}}{\text{initial assets}}$	$\frac{37\,413\text{ NR}}{161\,017\text{ NR}}$	$= 0.23 \times 100 = 23\%$
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Distribution of profits

The net profits at the end of the first season, after repayment of half of the loan principal, will be divided as follows: 25 percent will be paid out to members as dividends and the remainder will be re-invested in the enterprise as savings.

Balance sheet

Ownership of the enterprise by the members increases from 6.7 percent to 11.9 percent in the first season.

Cash flow

At the end of the first season, there is cash on hand in the amount of 173 219 NR. This will be enough to finance the increased production and sales in the second season. By the end of that season, the principal will have been paid back on the loan, leaving cash in the amount of 122 831 R. This will be enough for a reduced collection season in the third season without using borrowed capital, or, if additional financing is available, production can again be increased.

TABLE E.24 Start-up costs - Praja Cooperative, Nepal

Purchasing of NTFPs	NTFP	QUANTITY (KG)	RATE (NR/KG)	TOTAL AMOUNT (NR)
	Gurjo	1 935	12	23 220
	Amala	1 025	18	18 450
	Harro	1 500	15	22 500
	Barro	3 100	15	46 500
	Total	7 560		110 670
Packaging costs	PACKAGING MATERIALS	QUANTITY	RATE	TOTAL AMOUNT
	Jute sacks (capacity 50 kg)	152	20	3 040
	Rope	3	30	90
	Total			3 130
Fees and royalties	NTFP	QUANTITY (KG)	RATE (NR/KG)	TOTAL AMOUNT
	Gurjo	1 935	2	3 870
	Amala	1 025	2	2 050
	Harro	1 500	2	3 000
	Barro	3 100	2	6 200
	Total	7 560		15 120
Staff costs	STAFF	NUMBER	WAGES/MONTH (NR)	TOTAL AMOUNT
	Manager + accountant	1	–	–
	Storekeeper	4	2 000	8 000
	Allowances to representatives	9	50 NR/day	3 150
	Total			11 150 NR

	PARTICULAR	NUMBER	RENT/MONTH (NR)	TOTAL AMOUNT (NR)
Store costs	Store in Shaktikhor	4	250	1 000
	Store in Birendranagar	4	250	1 000
	Store in Mowakhola	4	250	1 000
	Total	12		3 000
Machines/equipment	UNITS		RATE (NR)	TOTAL AMOUNT
	Weighing machine	1	5 000	5 000
	Stitching needle	6	5	30
	Total			5 030
Transportation				7 182
Administration				TOTAL AMOUNT
	Stationery			5 235
	Total			5 235
Furniture and fixtures				500
Total start-up costs				161 017
Amount financed from member shares (220 members x 50 R/ share)				11 017
Grant from the project				75 000
Soft loan from the project				75 000 NR

TABLE E.25 Profit and loss projection - Praja Cooperative, Nepal

	ITEMS	QUANTITY	QUANTITY AFTER WEIGHT LOSS	RATE (NR/ KG)	TOTAL AMOUNT (NR)	TOTAL 1 ST SEASON (NR)	TOTAL 2 ND SEASON (SALES INCREASE 25%) (NR)
Total income from sales (revenue in NR)	Gurjo	1 935	1 838	25	45 956		
	Amala	1 025	974	40	38 950		
	Harro	1 500	1 425	30	42 750		
	Barro	3 100	2 945	25	73 625		
	Total	7 560					
	Total income					201 281	201 281
Fixed costs (FC)	ITEMS	TOTAL VALUE	RATE		TOTAL AMOUNT		
	Depreciation expense						
	Machines and equipment	5 030	10%	503			
	Furniture and fixtures	500	15%	75			
	Total depreciation expense			578	578		
	Miscella- neous - 5%	277		29			
Total fixed costs				607	607		

	ITEMS				TOTAL AMOUNT		
	Variable costs (VC)	Purchasing of NTFPs				110 670	
Packaging costs					3 130		
Fees and royalties					15 120		
Staff (direct labour) costs					11 150		
Store costs					3 000		
Transportation costs					7 182		
Administration costs					5 235		
<i>Subtotal</i>					<i>155 487</i>		
Miscellaneous (5%)					7 774		
Total variable costs					163 261	163 261	204 077
Total FC + VC					163 868	204 684	
Net profit					37 413 NR	46 918 NR	

TABLE E.26 Distribution of the net profits - Praja Cooperative, Nepal

Net profit		37 413 NR
Retained profit	net profit x 25%	9 353
Distributions to members	net profit x 75%	28 060
Breakdown of distribution to members		
Dividends to members	28 060 x 73%	20 483
Members' funds	28 060 x 27%	7 576
Total		28 060 NR

PHASE 3: Plan enterprises for sustainable development
ANNEX: Enterprise development plan 1998 of the Praja Cooperative LTD

TABLE E.27 Cash flow projection for a four-month season - Praja Cooperative, Nepal

	MONTH				TOTAL
	1	2	3	4	
Cash on hand	161 017 NR	89 960 NR	24 433 NR	113 496 NR	
Sales	0	0	101 281	100 000	201 281 NR
Total cash	161 017	89 960	125 714	213 496	
EXPENSES					
Fees and royalties	3 780	3 780	3 780	3 780	15 120
Equipment	5 030	0	0	0	5 030
Transportation			3 591	3 591	7 182
Administration	1 309	1 309	1 309	1 309	5 235
Furniture	500	0	0	0	500
Harvesting costs	55 335	55 335		0	110 670
Packaging	1 565	1 565	0	0	3 130
Staff costs	2 788	2 788	2 788	2 788	11 150
Storage rent	750	750	750	750	3 000
Dividends				20 483	
Deposit into members' savings funds				7 576	
Total expenses	71 057	65 527	12 218	40 277	
Total cash	161 017	89 960	125 714	213 496	
CASH MINUS EXPENSES	89 960 NR	24 433 NR	113 496 NR	173 219 NR	

TABLE E.28 Cash flow projection for the second season with increased sales of 25% -
Praja Cooperative, Nepal

	MONTH				TOTAL
	1	2	3	4	
Cash on hand	173 219 NR	91 309 NR	9 399 NR	145 728 NR	
Sales	0	0	151 602	100 000	251 602 NR
Total cash	173 219	91 309	161 001	245 728	
EXPENSES					
Fees and royalties	4 725	4 725	4 725	4 725	18 900
Transportation			4 489	4 489	8 978
Administration	1 636	1 636	1 636	1 636	6 544
Harvesting costs	69 169	69 169	0	0	138 338
Packaging	1 957	1 957	0	0	3 913
Staff costs	3 485	3 485	3 485	3 485	13 938
Storage rent	938	938	938	938	3 750
Dividends				25 688	
Deposits into members' savings funds				6 936	
Principal				75 000	
Total expenses	81 910	81 910	15 273	122 897	
Total cash	173 219	91 309	161 001	245 728	
CASH MINUS EXPENSES	91 309 NR	9 399 NR	145 728 NR	122 831 NR	

TABLE E.29 Balance sheet: first season - Praja Cooperative, Nepal

	BEGINING 1ST SEASON	END 1ST SEASON	END 2ND SEASON	% OF SALES
ASSETS				
Cash on hand	161 017 NR	173 219 NR	86 216 NR	378 NR
Equipment, furniture	5,500			
Less depreciation (equipment 10%, furniture 15%)	-578			
Value of equipment	4 452	4 452	4 374	
Total assets	161 017	177 671		220 752
LIABILITY				
Bank loan	75 000	75 000	0	
Total liability	75 000	75 000	0	
EQUITY				
Initial equity (220 members x 50 R/share)	11 017	11 017	11 017	
Retained profits (savings fund)	0	9 353	21 082	
Invested capital	75 000	82 301	188 653	
Total equity	86 017	102 671	220 752	
TOTAL LIABILITY + EQUITY	161 017 NR	177 671 NR	220 752 NR	

NOTES

In Phase 3, the facilitator will work with the future entrepreneurs to develop a plan for the growth of the enterprise, develop strategies for each of the four areas of enterprise development, and draw up action plans to prepare the way for implementation. This will involve defining the mission, goals and objectives of the enterprise, assessing its profitability, and determining capital start-up needs. The enterprise development plan will be used to obtain financing. Guidelines are presented for the development of market strategies and preparation of an enterprise development plan.