A FULL-COURSE MEAL WITH FINANCIAL CAPABILITY

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Introduction

Small businesses are often deemed the backbone of the economy, having over 20 million of these businesses in the United States. Many of these businesses, however, often fail after a few years. By doing a case study on restaurants and food trucks, the research team has deduced that financial capability is an essential ingredient in microenterprise and small business performance.

Background

In Florida, the economy is driven heavily by tourism, with 23% of the state's GDP derived from this industry. Orlando especially is a hub for tourism, with it making up 18.9% of the city's total GDP and generating $24.8 billion in tourism spending (Orlando Weekly). Small businesses, in general, are often risky, with half failing after 5 years. In particular, restaurants are often seen as one of the riskiest businesses to pursue, with 50% closing or changing ownership in the first year, and 80% by the fifth. This can be especially troubling in Florida, where there is a large restaurant industry. In 2018, there were 41,366 eating and drinking locations in Florida, with 12% of Florida employment concentrated in these businesses (National Restaurant Association).

Even though the term "small business" is often used to describe both an actual small business and a microenterprise, there is a specific difference. A microenterprise, also known as a microbusiness, has annual sales of less than $250,000 and around five employees (thebalance), and are often structured as a sole proprietorship or partnership. Small businesses, on the other hand, typically employ more than a microenterprise, but less than 500 employees. Total assets are valued at less than $1 million per year, and often identifies as an LLC [Limited Liability Corporation] (thebalance). In the food industry, a food truck would be considered a microenterprise, and a restaurant would be considered a small business.

This research connects the dots of why being financially capable is imperative when running a business, as well as presents solutions to the lack of financial literacy and financial inclusion, two of the three parts of being financially capable.

Purpose and Significance

Being financially capable is imperative . . . the role it plays in the performance of your business is day and night. It can determine whether or not your business will succeed. “Financial capability is the internal capacity to act in one’s best financial interest, given socioeconomic and environmental conditions. It encompasses the knowledge (literacy), attitudes, skills, and behavior of consumers with respect to understanding, selecting and using financial services, and the ability to access financial services that fit their needs.” Being financially capable is more than just handling finances, it is optimizing the performance of a business through your attitude, motivation, knowledge, and use of resources around you. The research team came up with three essential questions: ‘Can I do that?’ for resources, ‘Do I know what I’m doing?’ relates to knowledge, and ‘Do I want to do it?’ relates to motivation.

Research Design/Methodology

When gathering information, the research team used the internet to gather statistical and numerical data on starting, owning and managing a restaurant, held interviews with restaurant and food truck owners to gain personal insight on running their business and examples that showed a connection between financial capability and business performance; and interviewed banking experts to further understand the decision making process in funding a business in the food industry.

Measuring financial capability

Through research, the question of how to measure financial capability needed an answer to see the connection it has with the growth of a business. Whenever there is a way to measure anything, it makes it easier to understand, and in this case, easier for banks to determine if a person is financially capable.

According to a document by the World Bank "Financial Capability Surveys Around the World," the World Bank utilizes three concepts to measure financial capability:

1. Knowledge of fundamental financial concepts; do I know what I'm doing?
2. Awareness of products and services offered by different financial service providers and an understanding of the risks associated with using these products and services; can I do it?
3. Your attitudes and behaviors; do I want to do it?

The World Bank provided 2 definitions of financial capability that were given in this document:

- "Financial capability encompasses the knowledge, attitudes, skills, and behaviors of individuals with regard to managing their financial resources and understanding, selecting, and making use of financial services that fit their needs."

- "Financial capability means that individuals have the internal capacity to act in their best financial interest, given socioeconomic and environmental conditions, which can play an important role in constraining or facilitating individual financial capability."

The World Bank's document also cited a number of studies and individual parts they were looking at to come up with a way to measure being financially capable as a whole, and also how to measure those individual parts.

- Measure consumers' knowledge on how to save, invest, borrow, and even protect themselves from financial fraud.
- The World Bank also checked to see if the respondents knew their consumer rights, and how to pursue recourse against fraud and other financial practices that aren't fair to everyone.
- The respondents' personal views, beliefs, or psychological traits, and the connection that it has with their decision making, and how it can become a form for their internal financial capability.
- A number of studies asked about the reasoning that someone had for saving, borrowing, long-term planning, budgeting, etc. These studies focused on the motivation behind these financial behaviors, through the use of scales developed in psychological research.
- "A number of studies focus on motivations for financial behavior using scales developed in psychological research, or simply by inquiring about the reasons for adopting certain kinds of behavior. These surveys ask about reasons for saving, borrowing, long-term planning, and budgeting, among other indicators."

The Facts and Figures (Food Truck vs. Restaurant)

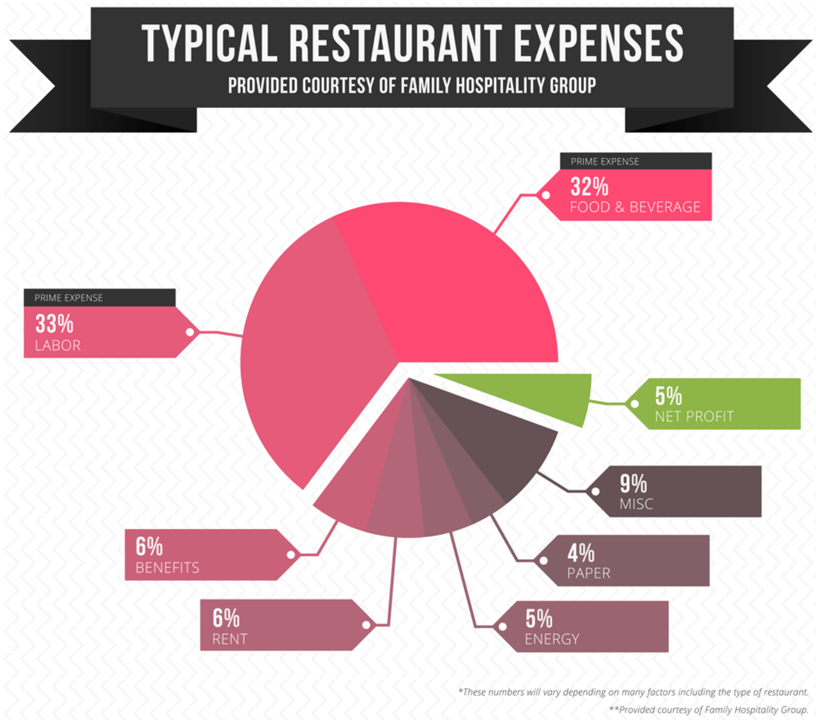
Food Trucks

When it comes to food trucks, these are some basic recurring costs. When you are making the financial decisions, you have to be able to not only calculate the total amount of costs, but also to pay them, and also make changes. Being financially capable enables you to make the decision that is right for your business, throughout the ups and downs of costs, changes in the market, etc.

Recurring Startup Costs	
Payroll (3-4 staff members)	$1,500 - $3,500
Commercial kitchen/commissary rent	$500 - $3,000
Monthly credit card processing fees	~ 3% of sales
Fuel	$250 - $400
Insurance	$5,000
Permits & licensing	$50 - $10,000 depending on location
Total Estimated Costs	$40,000 - $200,000

Funding

- You should have a good personal and business credit, which will increase your chances of receiving a business loan.



Advantages of a food truck

- Less upfront cost and lower expenses
- Mobility - Being able to bring your business to different locations.

Restaurant Challenges

- More types and amount of expenses.
- Fixed location, once you choose it, moving is much harder (webstaurantstore).
- Requires several federal, state and local permits and licenses

Restaurants

Advantages of a restaurant

- Less of a workload
- Easier to Market - Physical Location
- More Predictable (Bplan)

Food Truck Challenges

- Time - Long hours are a normality with a food truck business. There is shopping, prep, marketing, event bookings, cleaning, maintenance, accounting, etc. (businessnewsdaily).
- Competition and Market (ForaFinancial)
- Seasonal (foodonatruck)
- Ordinances and zoning - every area is different in terms of where you can park your food truck and how long you can park there.
- Food truck owners are legally obligated to prepare food in a certified kitchen (priceonomics)

Financial Capability in relation to a Business

In the interviewing process, the research team came across the owner of El Super Mofongo Resbaloso Food Truck, who made a decision to go from owning a restaurant to a food truck. The owner moved to the continental U.S. from Puerto Rico, where he had 2 different restaurants. He came to the continental U.S. to start another restaurant, but realized the expenses were too much for him to handle. He made two decisions that seemed simple, but demonstrates how capable he is making financial decisions that “act in one’s best financial interest, given socio-economic environmental conditions. It encompasses the knowledge [literacy], attitudes, skills and behaviors of consumers with regard to managing their resources, and understanding, selecting, and making use of financial services that fit their needs.” Those two decisions were to transition from a restaurant to a food truck, and since he knows that he has no experience with finances, he hired an accountant.

The team interviewed a number of people who had restaurant experience to better understand the connection that financial capability has with businesses by getting real examples. Monica McCown is an executive chef and managing partner at Artisan's Table, a casual dining restaurant in the heart of Downtown Orlando.

Monica didn't have any prior history with finances, rather she learned from working in a corporate restaurant. In the interview with her, she agreed there is a connection between a businesses' performance and being financially capable. When speaking to Monica she stated, "Being financially capable is important, as the margins in the restaurant are incredibly slim, that's why so many restaurants go out of business." Working in an industry where net profits only amount to a small percent, micromanaging the monetary aspects of the restaurant is critical. This is an example of Financial Literacy, a category of Financial Capability, in making a profit, thus leading to growth.

Monica then stated, "Part of 'can we do it' is do we have enough money? A lot of people start businesses with much less capital than they truly need to make that business successful. A restaurant has a lot of moving parts, you have to be super-dialed in on all the tiny factors that create the ability to have any bit of profit at all." When asked how Monica controls budgeting for inventory and payroll, she stated, "Making sure people are efficient to keep labor costs down. Pricing is an art and a factor, make sure to know the right markup." Monica tracks raw cost to minimize waste, the restaurant uses QuickBooks to track expenses, and they use a year-over-year projection to foresee expenses and revenues. As the restaurant is situated in the heart of Downtown Orlando, McCown tracks the events coming up, and has event calendars for the venues around them. McCown generally runs the business practices herself, only working with a CPA to do taxes. Those are examples connected to financial accessibility, a category of financial capability . . . do I have access to these services?

Dennis Kneesi, bartending for 10 years and managing restaurants for 12 years, is a seasoned professional in the restaurant industry, and he gave insight on how financial capability plays a role in starting a restaurant. “Financial capability is hugely important, when you open a restaurant, you won’t get paid for at least 5 years. You are looking at probably $750,000 to get a decent restaurant.” What Kneesi said reinforced the notion that a restaurant has an incredibly low profit margin, with a high upfront need of capital. Knowledge of budgeting and inventory is an important aspect of financial capability when working in a managing role of a restaurant. Kneesi does inventory weekly so that the restaurant runs out of food more often than they waste it. To help achieve this, the restaurant keeps a waste log each week for food and drinks that are thrown away, as well as using waste in cooking, such as making a stock. If they lacked the business acumen [a sense that allows you to quickly understand and deal with different business situations], which is another form of financial capability, the profit margins would be nonexistent.

Financial Capabilities’ different forms

In an interview with Patrice Phillips, who runs “Something Fishy,” a seafood fast-casual restaurant situated on the edge of Apopka with her husband, there was an encounter with a different form of financial capability. The two of them didn’t have any prior restaurant experience, rather they both came from corporate America. Their background allowed them to develop business acumen [a sense that allows you to quickly understand and deal with different business situations] while gaining business experience. "The business plan is 100% the most important part when you start. You need to see a template of an established plan . . . Forecasting sales is the most important part of controlling costs." They do payroll together, review taxes together, and the financial statement that summarizes the revenue, cost and expenses [P&L] together. "You need to use professional services, a tax accountant and CPA [Certified Public Accountant]. If you're not strong at doing your own books, you have to have professional services and tools that are available to you." Business acumen can also be described as business experience, which fits into the decisions that you make, another form of financial knowledge.

Financial Inclusion and its impact

When defining financial capability, the next pillar is the use of financial services. In the interview with Patrice, she alluded to Financial Inclusion by stating "You need to make use of professional services, a tax accountant and a CPA. If you're not strong at doing your own books you have to have professional services and tools that are available to you." These professionals will be able to assist you in getting legal and accounting information associated with running a restaurant business (Stimmel-law). Financial inclusion is when you have access to useful and affordable financial services and products that meet the needs of your business.

The term, Financial Exclusion, is the opposite of Financial Inclusion. Underbanked and unbanked are the segments that categorize Financial Exclusion. Unbanked refers to when a household 'doesn't have a bank account at an insured institution,' underbanked is when a household 'has an account but have used an alternative financial service within the past 12 months.' Many of the top unbanked areas are small, rural towns, based on CFED's report, "The Most Unbanked Places in America." For people who are unbanked, the charges and fees, such as for cashing a check, takes away from their money. "You'll pay up to $4 for all printed checks up to $1,000 and up to $8 for all printed checks between $1,000.01 and $5,000," says J.R. Duren, a personal finance analyst and senior editor at the consumer reviews site, www.HighYa.com. These charges take away from people who are in the LMI {Low- to Moderate-Income} bracket. Based on the Huffington Post, "Each of those 68 million Americans could have an extra $108 every month for food or gasoline or clothing. A family of four would see an extra $432 every month."

The OECD [Organisation for Economic Co-operation and Development] council, whose goal is to stimulate economic progress and world trade, released a document called "Enhancing the Contributions of SMEs in a Global and Digitalised Economy." In the document, it states that "SMEs' contributions also depend on their access to strategic resources, such as skills, knowledge networks, and finance, and on public investments in areas such as education and training, innovation and infrastructure." Therefore, if a business isn't in an area of Financial Inclusion, they can't succeed.

During an interview with Philip Zeman from CenterState Bank, he said that "we (CenterState Bank) won't be that funding source at the time, but will put them in contact with some of the resources in the community like BBIF [Black Business Investment Fund]." Not all businesses know that there are different resources that are available to them to use. The OECD also stated "The lack of appropriate forms of finance, especially of the equity-type, stands in contrast with large businesses"

The OECD believes that the reason why businesses cannot get funding from other sources is because they don't know the existence of these sources. In the document "Enhancing the Contributions of SMEs in a Global and Digitalised Economy," it states, "the availability of bank lending and of alternative sources of finance is held back by a combination of demand-side barriers, most notably limitations in financial knowledge, strategic vision, resources, and sometimes even the willingness or awareness to successfully attract sources." This goes into Financial Literacy, a category of Financial Capability, does the business owner know of those resources, products, and if they do how do they utilize them? These factors connect back your degree of Financial Capability.

In the interview with the food truck owner of El Super Mofongo Resbaloso Food Truck, he stated how he had access to a CPA, who handled the financial side of his business for him because he had no history in finance. This takes the burden off; that's one of the many services that businesses and individuals need to take advantage of to improve the performance of their business. It goes deeper than just funding services, but also finding a financial and accounting service, which goes into Financial Accessibility, a category in Financial Capability.

This lack of financial inclusion is very complex, but it plays a major role in Financial Accessibility a category in Financial Capability. For those in rural areas that are considered to be in the LMI {Low- to Moderate-Income} bracket who may be trying to start a microenterprise or small business, the 'Can I do it?', or the Financial Accessibility aspect, plays a major role in the success of their business.

Funding

Due to the high risk associated with the restaurant industry, financial institutions are often weary of lending the upfront cost to these businesses. “This cash-intensive business requires enough liquidity to cover employee paychecks, supplies, and other operating costs (Fundera).” If a business owner does not have enough capital to cover the upfront cost and the capital to keep their business going, then their business is already at a high risk of closing. When speaking with Philip Zeman, a commercial relationship manager at CenterState Bank, the research team was able to understand what goes into funding small business and microenterprise, which CenterState has a focus on.

In looking for any predisposed perceptions of restaurants, Zeman was asked how financial institutions look at restaurants. “There are a handful of industries that we scrutinize more than others and restaurants, frankly, are one of those industries. You drive through the community, and a lot of times restaurants are here one day, and the next day another brand comes in,” said Zeman. Getting a food truck loan isn’t any easier. “Banks are skeptical lending money because some believe that the food truck trend is just a fad and may suddenly vanish” (foodonatruck). Obtaining funding from a traditional lending source may not always be possible, especially for this type of business, so sometimes those who want to own a restaurant have to obtain capital from unconventional sources. In the case of McCown, one of her business partners sold a house for adequate funding.

One doesn’t always have to risk a large source of their own personal capital, however. For Patrice Phillips, she got funded through the BBIF, one of the several programs that assist in funding small businesses. Another one of the many options available is a CDFI (Community

Development Financial Institution), which like the BBIF, is “focused on generating economic growth and opportunity in some of [the] nation’s most distressed communities” (CDFIFUND). There is a source of funding that many aspiring restaurant owners borrow from, and that is through the help of the SBA [Small Business Administration]. The SBA attempts to help resolve the problem of lending institutions being wary of restaurants, and restaurants being unable to get a loan. This agency “doesn’t lend money directly to small business owners. Instead, it sets guidelines for loans made by its partnering lenders, community development organizations, and micro-lending institutions” (SBA).

Although even with this vast array of options available, restaurants aren’t automatically accepted. Like any business or person looking for a loan, a lending agency will look at their credit history. “The red flags would be if they don’t have that experience, the 5 C’s of credit that we always evaluate. These are all things that we address through that initial conversation to really understand the business owner’s capability,” said Zeman. The 5 C’s of credit are what makes up a person’s credit score, it shows how that person deals with credit, i.e., how financially capable they are at managing what they owe.

The 5 C’s are defined in NerdWallet as:

- Character - A lender’s opinion of a borrower’s general trustworthiness.
- Capacity - Your ability to repay the loan.
- Capital - The amount of money invested by the business owner or management team.
- Conditions - How the business will use the loan and how that could be affected by economic or industry factors.
- Collateral - Assets that can be pledged as security.

When starting a business, there's no credit history of the actual business for lenders to evaluate, so the owners themselves are evaluated.

Conclusions

Being financial capable is imperative to the success of your business. Through all the research, the team determined with full confidence that there is a connection between being financially capable and the performance of their business. The reason why business leaders, especially in the food industry, need to be financially capable is because of the connection it has with a businesses' performance. Business owners can finally understand the three components and different ways to incorporate them into their business. They need to answer the questions of 'Can I do it?,' 'do I know what I'm doing?,' and 'do I want to do it?'

Through this research, business owners can easily understand the importance of integrating financial capability through the interviews, and the examples that those interviews gave. This was also evident through the eyes of those in the food industry, and through the eyes of the banks. Since the research was on microenterprises and small businesses, and the case study was looking into restaurants and food trucks, business owners benefit in knowing the differences, but also the examples that are given for each. When looking at the entirety of this research, we see so many different viewpoints, terms, definitions, and examples that made it a bundle of wisdom that will enable a business to succeed.

Recommendations/Proposed Solutions

The team proposed that there be a scale, or a reasonable way to measure an individual's financial capability. When it comes to measuring a skill, it's more than just you have it, or you don't, it's about the different levels that you are at and continual progression. This scale can help the individual know what they need to improve upon to become more financially capable, but also for the banks to measure the financial capability of an individual more accurately.

In terms of creating businesses where the owners will have financial knowledge, a possible way for this to occur is to create a new mandatory certification for businesses. When you have any type of business, there are certain permits and certifications that are required, such as a food service certification in a restaurant. This new "financial capability" certification will make it so any aspiring business owner will have to take a training course that shows and/or teaches the aspects of financial capability. This will help prevent a business from f alling down any holes created by this lack of financial capability, giving the business success and helping to reassure any potential lenders that the money lent won't be lost as easily.

Limitations/Constraints

One of the many limits that was encountered was gaining interviews with food truck operators. They are either too busy to grant an interview, or not interested in assisting. The time constraints were something that held back the amount of research that could be found and put together. Another limitation was finding information on the differences between microenterprises and small businesses, as when talking about a business with less than 6 employees, the terms are used interchangeably.

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