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Financial Strategy for Supporting Business Entities in Conditions of Innovative Development of the Economy

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Abstract

The current state and unstable development of its areas pose challenges for entrepreneurs, the successful solution of which will contribute to their financial well-being in the process of production activities. Since the market to a certain extent represents uneven development, which is characterized by transitional processes, a particularly important role in developing a strategy for the behavior of business entities is given to forecasting the dynamics of market components (demand, prices, etc.), which act as controlling external influences about management functions entrepreneurial entity.

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The current state and unstable development of its areas pose challenges for entrepreneurs, the successful solution of which will contribute to their financial well-being in the process of production activities. Since the market to a certain extent represents uneven development, which is characterized by transitional processes, a particularly important role in developing a strategy for the behavior of business entities is given to forecasting the dynamics of market components (demand, prices, etc.), which act as controlling external influences about management functions entrepreneurial entity. The decision-making process about a possible behavior of a business entity in the market should be based on a good information base that allows for reducing the instability of financial and economic activity, i.e. transition from one painful state to another. However, despite the apparent chaos and spontaneity of production reigning in the market, an entrepreneur has the opportunity to regulate his production taking into account market dynamics. One of the factors involved in regulating the production process is information that can be obtained without much difficulty by analyzing the market. The number of potential buyers will tell us the size of the market, the index of price growth and income, and what changes the level of sales will undergo.

An entrepreneur entering the market with a new product, in our opinion, should be guided by considerations according to the proposed scheme.

1. Based on the number of potential buyers, determine the size of the market;
2. determine the number of competitors producing a similar or interchangeable product;
3. find out the prices and consumer properties of competing products;
4. develop a matrix of buyer behavior in the market and, on its basis, obtain forecast estimates of market distribution between competing products
5. based on the total sales of all manufacturers per unit of time, determine the average time of market saturation;
6. based on an analysis of one's own production capabilities, determine the time required to saturate the distributed market share;
7. determine the sales volume of the product in value terms;
8. Determine the total volume of production costs and costs associated with the development and implementation of innovations;
9. determine the level of profitability of the production of an innovation and compare it with a standard (some minimum acceptable level of profitability);
10. if the actual level of profitability is below the reference value, it is necessary to implement measures aimed at redistributing market share in its favor. Note that the equilibrium distribution of the market occurs when the time of market saturation corresponds to the time of saturation of the share of the distributed market by a competitor, taking into account its production capabilities. In this case, it is necessary to redistribute market share and actual sales volume between competitors. In connection with the inevitable occurrence of a shortage, draw up a matrix of "capital expenditure on expanding production capabilities - additional sales volume in the time interval representing the difference between the time of market saturation and the time of saturation of the distributed market share";
11. determine the feasibility of additional investments in expanding production capabilities by comparing the profitability of product production with its reference value.

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It should be noted that the structure of the activities of a business entity will radically change, since the guarantee of sales of its goods will disappear due to the severance of strictly established ties with consumers and their possible reorientation to goods from other manufacturers. At the same time, business entities must plan their production activities taking into account a new factor for them called market risk. This means that their sales volume will depend directly on the compliance of their characteristics with market requirements. An enterprise should assess the sales volume of its products at the early stages of the life cycle to avoid losses if the product is not accepted by the market *(see Fig . 1).*

Fig. 1. Graphical functions of sales volume, costs, and profit

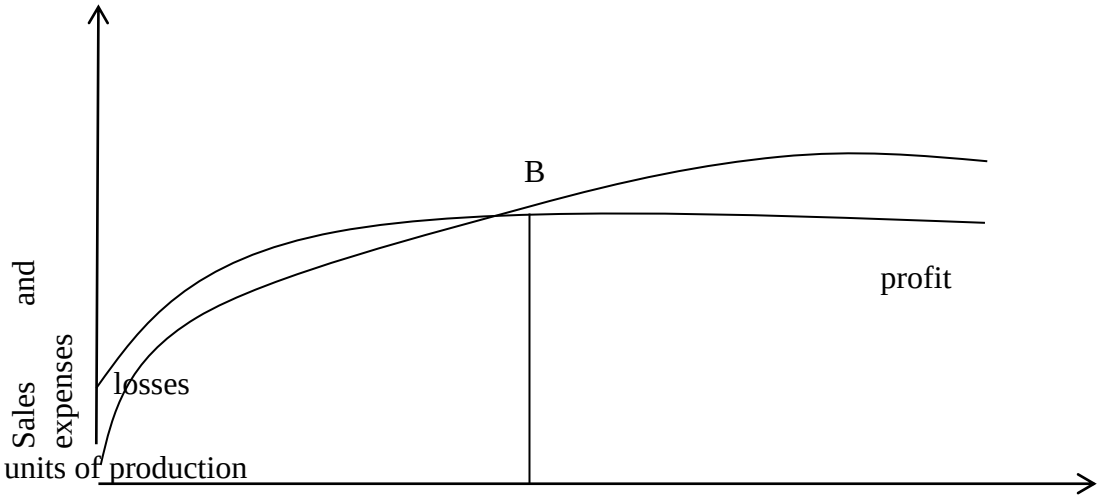
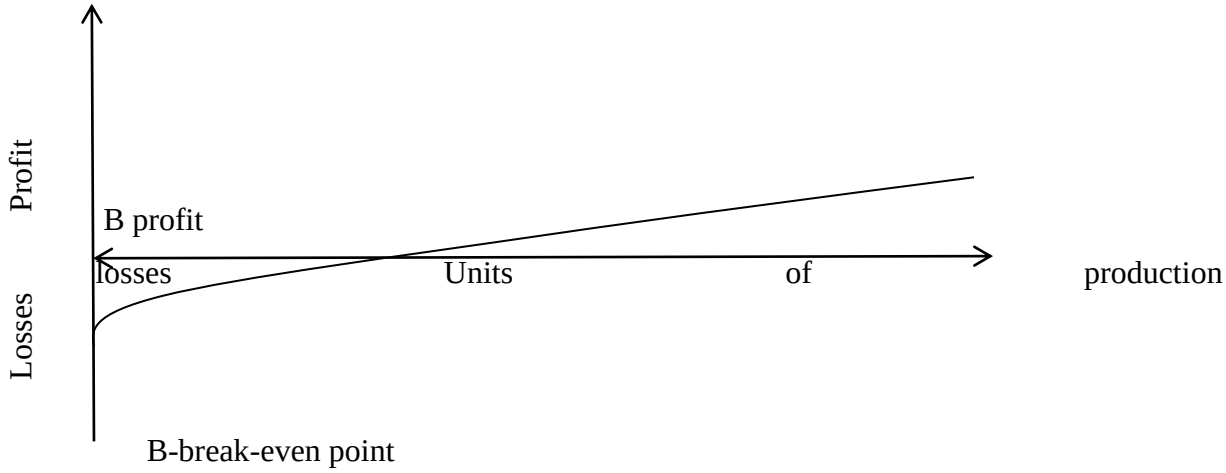


Fig 2. Graphical functions of profit and loss



Therefore, even at the production stage, it is necessary to develop forecasts for the distribution of goods on the market and, on their basis, to develop production programs, taking into account the instability of the development of the economy of a particular region and the level of inflation, i.e. inflationary profits (losses).

Along with this, it should be noted that the financial condition of a business entity is characterized by the elasticity of demand prices “B”, where growth is caused by a continuous

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decrease in the real price "C" of the product in such a way that the amount of demand "BC" grows in proportion to the decrease in prices.

According to economic theory, the entrepreneur chooses his pricing policy to thus maximize his expected booked profits in the future, i.e. trying to solve a problem like:

$$\int \pi_1(\tau)\, b^{-r\tau} d \rightarrow \max \quad (1)$$

$$\pi_1(t)=[\, C(t)-CC(t)]\, BC(t) \quad (2)$$

where CC (t) is the cost of production of goods at time t ;

r - discount factor;

π - forecast (planning period).

In a competitive market, the market share available to each producer depends on the prices charged by others. However, for an innovative new product, it makes sense to assume that the producer is a monopolist, or perhaps a group of individuals who have bought the license of the original and innovator, and that the producers can set a single market price T (t). In other words, the market price decreases over time in such a way as to cause a constant increase in the market at a given rate (T), i.e. $Sun_0(t) = Sun_{01}\, b^{t\,1}$ (3)

Where Sun_0 is market demand at t = 0

In a market with a constant price elasticity of demand b (defined by a positive number), this market growth rate requires the market price to decline at a rate

$$C = C\, b^{rb} \quad (4)$$

$$=\frac{DBc}{D\text{Ц}} - \frac{\text{Ц}}{\text{Bc}}$$

The cost of producing a product decreases over time also as the manufacturer gains experience. Then it is convenient to propose a well-known formula for reducing cost, i.e.

$$SS = SS_{about}\, SP^{to} \quad (5)$$

Where is the k-coefficient characterizing the development of innovation in production;

SP - total production for a certain period of time

$$SP = \int BC(\tau) D\tau\, b \quad (6)$$

Where

$$\frac{\text{ДСП}}{dt} = DC \quad (7)$$

Using equation (3), (5) and (7) and applying the expression for gross profit

$$\pi = Bc_0\, (\text{Ц}_0\, b - \text{т}\, ib - Cc_0\, b^{kti})\, bti \quad (8)$$

a series of subsequent algebraic calculations can show that the gross profit of an enterprise supplying a new product will grow if (and only if) when

$$K_0 > 1$$

If this market condition is not met, the new product will not successfully replace the old one, i.e. the replacement process will not be self-sustaining. In practice, the minimum price elasticity

required for long-term profitability growth is quite high. This means that there must be many potential buyers willing to pay. Because at least a few users of innovations must pay higher prices than the average user.

Assuming that technological substitution is potentially self-sustaining, the question arises whether there is an upper limit to the pace of the market. It turns out that there is at least a maximum rate of price decline caused by the fact that if the price of a new product drops too quickly, some potential users will delay their purchasing decision while waiting for prices to drop. So, as can be seen from equation *(4)*, prices are directly related to market growth; there is an automatically built-in regulatory mechanism that limits the noticeable rate of price decline and increase in market growth.

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