



VARZA SCHOOL · THE FOUNDATIONAL 100

The Economics of Starting: Initial Investment, Working Capital, Runway, and Break-Even

Chapter 17 · Track 2 — Starting and Understanding a Business

THE QUESTION IT ANSWERS

How much money does a new business truly need before it can survive long enough to reach a viable operating level?

CONCEPTS DEFINED

Startup cost · Initial investment · Working capital · Runway · Break-even point · Contribution margin · Fixed cost · Scenario

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Varza promise: clear enough for a first-time learner, exact enough for a professional conversation, and practical enough to support a real decision.

Why this chapter matters

This track moves from personal decisions to an operating business. A business is examined as a repeatable system that creates value, coordinates people and resources, accepts risk, collects evidence, and converts activity into cash and durable capability.

Central question: How much money does a new business truly need before it can survive long enough to reach a viable operating level?

Startup affordability includes setup assets, pre-opening costs, opening working capital, operating losses, and contingency. Break-even estimates the required activity; runway asks whether available cash lasts long enough to get there.

Varza approaches the subject from life to ledger and from ledger to decision. We begin with what actually happened, identify the rights, obligations, resources, timing, and uncertainty, and only then choose the correct term, calculation, document, or account. This order protects the learner from a common error: learning a label without understanding the economic reality that the label is supposed to describe.

Learning outcomes

- Define and distinguish startup cost in plain and professional language.
- Define and distinguish initial investment in plain and professional language.
- Define and distinguish working capital in plain and professional language.
- Define and distinguish runway in plain and professional language.
- Apply the concepts to a numerical case and explain the result rather than only calculate it.
- Identify evidence, workflow, controls, and Varza entities required for reliable use.
- Recognize when jurisdiction-specific or licensed professional advice is required.

The Varza mental model

A financial concept becomes decision-ready when six questions have answers: **what, who, when, how much, based on what evidence**, and **under which assumption or rule**. A seventh question—**what should happen next**—turns knowledge into management.

This chapter uses internationally recognized terminology, but it remains jurisdiction-neutral unless explicitly stated. Accounting standards, tax rules, contract law, consumer protection, labor requirements, and investment regulation can produce different legal outcomes in different countries. The global foundation gives the learner a stable map; local collections must add the binding rules.

Core concepts

1. Startup cost

Working definition. Startup cost is a one-time or pre-operating resource sacrifice required to make a new activity capable of operating.

Separate startup costs from working capital, recurring expense, capital expenditure, and contingency. Their accounting treatment depends on the nature of the item and applicable rules. This is where operational activity and financial reporting meet.

Simple example. Registration, initial equipment, fit-out, launch marketing, and professional fees may arise before the first sale.

Decision test. Who can influence the result, and who only reports it? A reliable answer should state the unit, date or period, scope, evidence, and uncertainty. When one of these is missing, the concept may still be useful for discussion, but it is not yet decision-ready information.

2. Initial investment

Working definition. Initial investment is the total resources committed at the beginning of an undertaking, including assets, setup, deposits, opening inventory, and initial liquidity.

Include timing and recovery assumptions. A low equipment price does not make a project affordable if it leaves no working cash. In Varza language, the concept becomes useful when it changes a decision.

Simple example. A café needs CU 90,000 of equipment and fit-out plus CU 30,000 of opening cash and inventory.

Decision test. Does the item affect cash now, later, or not at all? A reliable answer should state the unit, date or period, scope, evidence, and uncertainty. When one of these is missing, the concept may still be useful for discussion, but it is not yet decision-ready information.

3. Working capital

Working definition. Working capital is the short-term resources and obligations used to sustain ordinary operations, often analyzed through current assets, current liabilities, and the cash conversion cycle.

A growing business can consume cash as receivables and inventory grow faster than supplier credit. Working capital is therefore an operating design issue, not only a ratio. The professional term matters because it prevents two different realities from being recorded as though they were the same.

Simple example. A profitable distributor requires additional cash when sales growth increases inventory and customer credit.

Decision test. What is being measured, and what has been left outside the boundary? A reliable answer should state the unit, date or period, scope, evidence, and uncertainty. When one of these is

missing, the concept may still be useful for discussion, but it is not yet decision-ready information.

4. Runway

Working definition. Runway is the estimated period an organization can continue before available liquidity is exhausted under stated cash assumptions.

Runway is a forecast, not a guarantee. Use multiple scenarios and distinguish unrestricted cash from funds reserved or unavailable. A non-specialist can understand this by separating the object, the timing, and the consequence.

Simple example. CU 120,000 of usable cash divided by a CU 20,000 monthly net cash burn suggests six months of simple runway.

Decision test. When did the underlying right, obligation, benefit, or sacrifice arise? A reliable answer should state the unit, date or period, scope, evidence, and uncertainty. When one of these is missing, the concept may still be useful for discussion, but it is not yet decision-ready information.

5. Break-even point

Working definition. Break-even point is the activity level at which relevant revenue equals relevant fixed and variable costs, producing zero profit under the model.

It is an assumption-based planning threshold. Capacity, product mix, taxes, financing, and cash timing may require separate analysis. The concept should be measured at the smallest level that still supports a real action.

Simple example. With CU 50 contribution per unit and CU 100,000 fixed cost, simple break-even is 2,000 units.

Decision test. Which document or observation would allow another person to verify it? A reliable answer should state the unit, date or period, scope, evidence, and uncertainty. When one of these is missing, the concept may still be useful for discussion, but it is not yet decision-ready information.

6. Contribution margin

Working definition. Contribution margin is revenue less variable costs under a stated decision definition, representing the amount available to cover fixed costs and profit.

Contribution supports short-term volume, mix, pricing, and capacity decisions but does not mean a product is profitable after all relevant costs and constraints. The number alone is not enough; its definition determines whether comparisons are valid.

Simple example. CU 100 selling price less CU 60 variable cost gives CU 40 contribution per unit.

Decision test. How would a different assumption change the result? A reliable answer should state the unit, date or period, scope, evidence, and uncertainty. When one of these is missing, the concept may still be useful for discussion, but it is not yet decision-ready information.

7. Fixed cost

Working definition. Fixed cost is a cost whose total does not change within a relevant range in response to short-term changes in a specified activity driver.

Fixed does not mean permanent or uncontrollable. It is fixed only for the selected period, range, and driver. This is where operational activity and financial reporting meet.

Simple example. Monthly warehouse rent remains the same between 5,000 and 8,000 units handled.

Decision test. Who can influence the result, and who only reports it? A reliable answer should state the unit, date or period, scope, evidence, and uncertainty. When one of these is missing, the concept may still be useful for discussion, but it is not yet decision-ready information.

8. Scenario

Working definition. Scenario is a coherent set of assumptions describing a possible future state and its financial and operational consequences.

A scenario is not just one number changed. Demand, price, currency, capacity, collection, and management response may interact. In Varza language, the concept becomes useful when it changes a decision.

Simple example. A downside scenario combines 15% lower sales, slower collection, and higher imported material cost.

Decision test. Does the item affect cash now, later, or not at all? A reliable answer should state the unit, date or period, scope, evidence, and uncertainty. When one of these is missing, the concept may still be useful for discussion, but it is not yet decision-ready information.

How the concepts connect

The concepts in this chapter are a system, not a vocabulary list. Startup cost, Initial investment, Working capital, Runway, Break-even point, Contribution margin, Fixed cost, and Scenario describe different parts of the same decision. Confusing them usually creates one of three failures: the wrong amount is measured, the right amount is assigned to the wrong period or person, or a correct report is used for a decision it was never designed to support.

A useful analysis therefore preserves both **classification** and **relationship**. Classification tells us what an item is. Relationship tells us what caused it, what it affects, and what could change it. Varza should store both. A report that shows only totals may be suitable for orientation; a controlled decision requires traceability to the underlying relationships.

Formulas and quantitative relationships

Unit break-even

Break-even units = Fixed costs ÷ Contribution per unit

The formula estimates the volume needed to cover fixed cost under stable unit economics.

Boundary: Product mix, capacity steps, tax, financing, and cash timing require separate analysis.

Simple runway

Runway months = Usable opening cash ÷ Average monthly net cash burn

The ratio provides a first liquidity horizon.

Boundary: Use a dated cash forecast where burn varies or major one-time outflows exist.

Worked case — The business needs more than the equipment price

An entrepreneur plans a workshop with the following startup model.

Item	Amount or observation
Equipment and fit-out	CU 140,000
Deposits and pre-opening cost	CU 30,000
Opening inventory	CU 40,000
Monthly fixed cash cost	CU 24,000
Unit selling price / variable cost	CU 500 / CU 300
Available funding	CU 300,000

Calculation and reasoning

1. Initial setup and opening working assets consume CU 210,000, leaving CU 90,000 usable cash.
2. Contribution per unit is CU 200.
3. Simple break-even is $24,000 \div 200 = 120$ units per month.
4. If early net cash burn averages CU 18,000, simple runway is five months; a slower sales ramp or late receivables could shorten it.
5. The founder should model monthly dates and a downside ramp before committing all funding.

What the result means

The project is not safe merely because CU 300,000 exceeds the CU 140,000 equipment quote. Viability depends on reaching contribution break-even before liquidity is exhausted.

The case is deliberately compact. In practice, Varza would preserve the supporting documents, currency, dates, counterparty, project or cost center, approvals, and links to the resulting records. The lesson is not merely to reach a number; it is to make the path to that number reviewable.

Practical workflow

1. **Define the decision, responsible person, economic unit, period, and acceptable uncertainty.** Define the owner, required evidence, status, date, and exception route. Do not allow the next step to erase the record of the previous one.
2. **Separate one-time setup, capital assets, deposits, opening inventory, and recurring monthly cost.** Define the owner, required evidence, status, date, and exception route. Do not allow the next step to erase the record of the previous one.
3. **Estimate realistic sales ramp, contribution, collection, and supplier payment timing.** Define the owner, required evidence, status, date, and exception route. Do not allow the next step to erase the record of the previous one.
4. **Calculate break-even by unit and revenue under more than one mix.** Define the owner, required evidence, status, date, and exception route. Do not allow the next step to erase the record of the previous one.
5. **Build base, downside, and severe cash scenarios through the point of stability.** Define the owner, required evidence, status, date, and exception route. Do not allow the next step to erase the record of the previous one.
6. **Reconcile the result to source evidence and investigate exceptions rather than forcing agreement.** Define the owner, required evidence, status, date, and exception route. Do not allow the next step to erase the record of the previous one.
7. **Approve the decision or record at the authority level required by value, risk, and legal consequence.** Define the owner, required evidence, status, date, and exception route. Do not allow the next step to erase the record of the previous one.
8. **Monitor the outcome, compare it with the original assumption, and retain the learning for the next cycle.** Define the owner, required evidence, status, date, and exception route. Do not allow the next step to erase the record of the previous one.

How this concept should appear in Varza

The minimum Varza data model for this chapter includes `startup_budget`, `capital_asset`, `opening_inventory`, `preopening_cost`, `working_capital_plan`, `monthly_cash_forecast`, `break_even_model`, `funding_source`. These names are not merely interface labels. Each entity should have a stable identifier, status history, responsible owner, applicable currency or unit, effective dates, evidence links, and access controls.

A useful Varza screen should answer four questions without forcing the user to reconstruct the story manually:

1. **What happened or is expected to happen?** Show the operational event, obligation, or decision in plain language.
2. **What changed financially?** Show cash, asset, liability, equity, income, expense, commitment, or risk effects.
3. **Why should the user trust it?** Show source documents, calculations, approvals, and revision history.
4. **What requires attention now?** Show exceptions, due dates, thresholds, and the next responsible action.

The Varza design principles most relevant here are:

- Turn information into a decision, a control, or a question; otherwise it is only decoration.
- Begin with the real event, not the accounting label.
- Keep value, cash, profit, and ownership distinct until their relationship is proven.

Varza AI may explain, classify, compare, simulate, and prepare a proposed action. It should not silently change a legal record, post a material transaction, close a period, release a payment, or make an investment decision on the user's behalf. Material actions require visible evidence, permissions, validation rules, and an accountable human approval path.

Controls and professional boundaries

1. **Contingency governed by risk rather than a flat unexplained percentage.** The control should be proportionate to value and risk, documented clearly, and tested often enough to detect failure before the consequence becomes irreversible.
2. **No long-term commitment before funding and downside capacity are confirmed.** The control should be proportionate to value and risk, documented clearly, and tested often enough to detect failure before the consequence becomes irreversible.
3. **Monthly actual-to-startup-model review from pre-opening onward.** The control should be proportionate to value and risk, documented clearly, and tested often enough to detect failure before the consequence becomes irreversible.
4. **Stable definitions, versioned assumptions, and consistent units across plans, records, and reports.** The control should be proportionate to value and risk, documented clearly, and tested often enough to detect failure before the consequence becomes irreversible.
5. **Traceability from every material total to evidence, calculation, owner, and change history.** The control should be proportionate to value and risk, documented clearly, and tested often enough to detect failure before the consequence becomes irreversible.
6. **Access and approval rights aligned with responsibility and the possible consequence of error or misuse.** The control should be proportionate to value and risk, documented clearly, and tested often enough to detect failure before the consequence becomes irreversible.

A control is effective only when it operates in practice. A policy that everyone can bypass is a statement of hope, not a control. Likewise, a control that blocks ordinary work without distinguishing low-risk and high-risk cases encourages hidden workarounds.

Common mistakes and better responses

Mistake 1: Funding only the equipment and forgetting opening liquidity

Better response. Reconstruct the underlying event, state the definition being used, obtain the missing evidence, and recalculate before making a decision. Correct the process as well as the current number so the same error does not become routine.

Mistake 2: Assuming full planned sales from the first month

Better response. Reconstruct the underlying event, state the definition being used, obtain the missing evidence, and recalculate before making a decision. Correct the process as well as the current number so the same error does not become routine.

Mistake 3: Using gross margin percentage as though it were cash collection

Better response. Reconstruct the underlying event, state the definition being used, obtain the missing evidence, and recalculate before making a decision. Correct the process as well as the current number so the same error does not become routine.

Mistake 4: Calculating runway from average burn while ignoring a large near-term payment

Better response. Reconstruct the underlying event, state the definition being used, obtain the missing evidence, and recalculate before making a decision. Correct the process as well as the current number so the same error does not become routine.

Mistake 5: Using a technically correct number outside the period, entity, currency, or decision boundary for which it was calculated

Better response. Reconstruct the underlying event, state the definition being used, obtain the missing evidence, and recalculate before making a decision. Correct the process as well as the current number so the same error does not become routine.

Mistake 6: Accepting an automated result without reviewing the evidence, assumptions, exceptions, and required professional judgment

Better response. Reconstruct the underlying event, state the definition being used, obtain the missing evidence, and recalculate before making a decision. Correct the process as well as the current number so the same error does not become routine.

Decision checklist

- ☐ Can I explain startup cost in plain language and in professional terms?
- ☐ Can I explain initial investment in plain language and in professional terms?
- ☐ Can I explain working capital in plain language and in professional terms?
- ☐ Can I explain runway in plain language and in professional terms?
- ☐ Have I stated the entity, currency or unit, date or period, and decision boundary?
- ☐ Can another person reproduce the number from retained evidence?
- ☐ Have I separated actuals, estimates, commitments, and scenarios?
- ☐ Have I tested timing, liquidity, risk, and at least one adverse outcome?
- ☐ Is the required approval proportional to the possible loss or legal consequence?
- ☐ Does the final output lead to a specific action, owner, and review date?

Practice lab

1. **Explain it.** Describe Startup cost to a person who has never studied finance. Then add the professional definition and identify one boundary your simple explanation omitted.
2. **Classify it.** Create five examples from your household or a small business and classify each using Initial investment. State any assumptions.
3. **Calculate it.** Rebuild the worked case with amounts 20% higher. Identify which conclusions change and which remain structurally true.
4. **Challenge it.** Describe a situation in which Working capital could be measured correctly but still lead to a poor decision because timing, risk, or incentives were ignored.
5. **Design it.** Sketch a Varza screen or report for this chapter. Include fields, evidence links, status, owner, exceptions, and one AI-assisted action.

Answer guidance

A strong answer uses consistent definitions, reveals assumptions, distinguishes fact from estimate, and connects the result to an action. More than one conclusion may be reasonable when the learner clearly states the decision objective and uncertainty. The worked-case recalculation should preserve the method even when the numbers change.

Varza AI knowledge capsule

This capsule is intentionally explicit so that a retrieval system can distinguish canonical teaching points from examples and commentary.

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    "Working capital: the short-term resources and obligations used to sustain ordinary operations, often analyzed through current assets, current liabilities, and the cash conversion cycle.",
    "Runway: the estimated period an organization can continue before available liquidity is exhausted under stated cash assumptions.",
    "Break-even point: the activity level at which relevant revenue equals relevant fixed and variable costs, producing zero profit under the model.",
    "Contribution margin: revenue less variable costs under a stated decision definition, representing the amount available to cover fixed costs and profit.",
    "Fixed cost: a cost whose total does not change within a relevant range in response to short-term changes in a specified activity driver.",
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Suggested questions for Varza AI

- Explain this chapter using an example from a household, a shop, and a service business.
- Ask me five diagnostic questions before applying this concept to my situation.
- Show the difference between cash effect, accounting effect, and decision effect.
- Recalculate the worked case using my currency and assumptions, but preserve the original definitions.
- Identify which parts require local accounting, tax, legal, labor, or investment rules.

Sources and standards horizon

This chapter is original Varza educational content. It paraphrases and synthesizes concepts; it does not reproduce a standard or third-party article. The following sources were used to establish terminology, scope, and current professional context:

- **S003 — OECD-INFE, *Core Competencies Framework on Financial Literacy for MSMEs*.** 2018; accessed 2026-08-31. Financial capability for entrepreneurs and small-business managers. Source: https://www.oecd.org/en/publications/oecd-infe-core-competencies-framework-on-financial-literacy-for-msmes_220101c9-en.html
- **S007 — U.S. Small Business Administration, *Plan your business*.** accessed 2026-08-31. Business plans, market research and startup-cost planning. Source: <https://www.sba.gov/counseling/plan-your-business/>
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Standards horizon. Reviewed through 2026-08-31. IFRS 18 and the third edition of the IFRS for SMEs Accounting Standard are included as transition knowledge where relevant; both have mandatory effective dates beginning in 2027, with early application permitted under their respective requirements.

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