

HOW TO PREPARE A BUSINESS PLAN
~ Guidelines for Entrepreneurs ~

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HOW TO PREPARE A BUSINESS PLAN

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I. INTRODUCTION

The business plan is the principal sales tool in raising capital. Before risking any capital, bankers or investors want to assure themselves that you have thought through your plans carefully, that you know what you are doing, and that you can respond effectively to problems and opportunities. They will insist on seeing your business plan before considering any financial commitment, and often will not even meet with you without a prior review of the business plan. Therefore, your business plan must be well prepared and persuasive in conveying the potential of the enterprise it describes. It should address all major issues, and yet not be so detailed that it “turns off” the reader. You should try not to have a business plan more than 50 pages long.

The guidelines that follow describe:

1. The necessary sections of a business plan
2. What should be included in each section and subsection
3. Why the information is necessary

Intelligent use of these guidelines should result in a complete professional business plan that makes an orderly presentation of the facts necessary to obtain a decision from any funding source.

Because these guidelines were written to cover a variety of possible ventures, rigid adherence to them is not possible nor even desirable for all ventures. For example, a plan for a service business would not require a discussion of manufacturing or product design. Space has been provided for you to address topics and make notes. Be prepared to use additional space as needed. Use this information in preparing the text of your plan.

II. SUMMARY OF BUSINESS PLAN

Summary Statement

Prepare a 1 or 2 page summary of your business plan. It should be a brief, appealing and accurate presentation of the highlights of your venture and its opportunities. The summary is best written after the plan has been completed. It must contain information on at least the following:

A. Present Status of Company:

Indicate:

- When the company was formed and its current status
- Company purpose
- What is special or unique about it
- Who are the founders
- Background of the entrepreneurs that makes them particularly qualified (for example, unique know-how) to pursue the business opportunity.

B. Market Opportunity:

Identify and explain (briefly) the market opportunity:

- * Information on the size and growth rate of the market for the company's product or service.
- * Percentage of that market that will be captured
- * Brief statement about industry-wide trends
- * Plans for the expansion of the initial product line

If existing:

1. Why the business has been successful or not
2. Key factors of business growth
3. Profitability patterns
4. Transitions

B. Mission statement: (why you are in business, what you do, who you serve)

Address these topics:

- | | |
|--|-----------------------------------|
| ▪ Target markets | • Technological position (if any) |
| ▪ Current or anticipated customer list | • Operational resources |
| ▪ Integration strategy (forward or backward) | • Company strengths & weaknesses |
| ▪ Pricing strategy | • Key success factors |
| ▪ Proprietary position (if any) | • Competitive position |

C. Goals and Objectives (List most important business, personal, and financial goals and objectives)

Short-Term

Long-Term

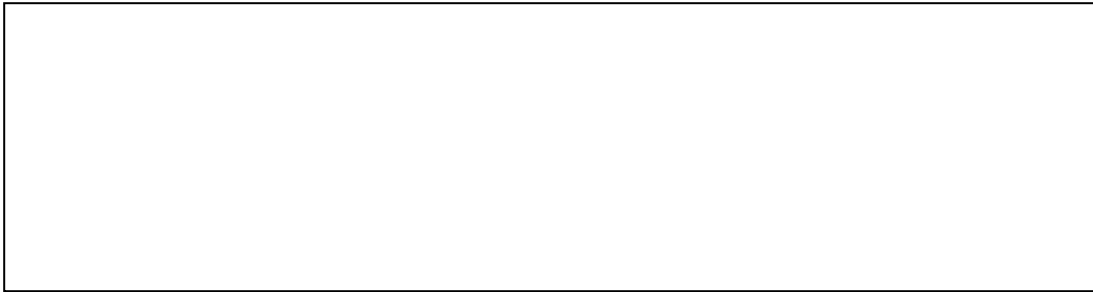
2. **MANAGEMENT TEAM**

The Management team is the key to turning a good idea into a successful business. Bankers and investors look for a committed management team with a proper balance of technical and business skills, and experience in doing what is proposed.

Accordingly, this section of the business plan will be of primary interest to potential bankers or investors and will significantly influence their decisions.

A. Organization:

Graphically show the key management roles in the company, the individuals who will fill each position, and their relationships to each other and the employees.



- ◆ Discuss any previous experience of the management group in working together. Indicate how their skills complement one another and result in an effective entrepreneurial management team.

- ◆ If any key individuals will not be on board at the start of the venture, indicate when they will join the company.

- ◆ Describe the use of outside consultants, etc. to fill key roles as appropriate

B. Functions of Personnel:

- Describe the exact duties and responsibilities of each of the key members of the management team. Include a brief (three or four sentence) statement of the career highlights of each individual that focuses on accomplishments demonstrating ability to perform the assigned role.

- Complete resumes for each key management member are included as exhibits of the business plan. These resumes should stress the training, experience, salary history and accomplishments of each manager, in performing functions similar to the role in the venture. List accomplishments such as:

- ✓ Profit improvement
- ✓ Labor management
- ✓ Manufacturing or technical achievements
- ✓ Ability to meet budgets and schedules
- ✓ Community organization
- ✓ References
- ✓ Recognition or rewards received, e.g. pay increases, promotion, etc.

A sample resume is attached.

C. Management Compensation and Ownership:

The likelihood of obtaining financing is small when the founding management team is not prepared to accept modest initial salaries. If the founders demand substantial salaries, the potential banker or investor will conclude that their psychological commitment to the venture is less than it should be.

- State the salary that is to be paid to each key person
- Describe the stock ownership planned for the key personnel, the amount of their equity investment (if any), and any performance-dependent stock-options or bonuses that are contemplated

D. Board of Directors:

- Discuss the company’s philosophy as to the size and composition of the board.
- Identify and propose board members and include a one or two sentence statement of the member’s background that shows what he or she can bring to the company.
Include resumes for each board member as an exhibit to the business plan.

E. Management Assistance and Training Needs:

- ◆ Outline the strengths and weaknesses of your management team and board of directors.
- ◆ Describe the kind, extent, and timing of any management training that will be required to overcome weaknesses in any of the following:

Accounting and taxes:

Planning:

Organizing:

Financial management:

People management:

Time management:

Sales:

Promotion:

Decision-making:

Cost control:

Personnel policies:

Pricing:

F. Supporting Professional Services:

C. Identify outside consultants and advisors:

Your CPA tax advisor: _____

Your accountant: _____

Your business lawyer: _____

Your patent attorney: _____

Your banker: _____

Your insurance broker: _____

Other key outsiders: _____

3. **INDUSTRY ANALYSIS**

Describe the background of your industry.

- How the industry has developed (Include previous trends and their cause)
- Industry's growth patterns
- The industry's future (new products, developments, markets, customers trends, etc.)
- Impact of socio economic trends, government policy, and population shifts.
- How international trade impacts the industry
- How well small businesses prosper in the industry
- How small businesses are affected by large companies
- How small businesses are affected by franchises
- How your business fits into the industry

List source of this information (for example, US Industrial Outlook or Industry Surveys)

- Define the present state of development of the product or service. For products, provide a summary of the functional specifications. Include product literature and or service photographs when available.
-
-

C. Proprietary Position:

- Describe any patents, trade secrets or other proprietary features. Attach copies of any patent applied for or granted.
 - Discuss a head start that you might have that would enable you to achieve a favored or entrenched position.
-
-
-
-

D. Potential:

- Describe any features of your product or service that may give it an advantage over the competition.
 - Discuss any opportunities for the expansion of the product line or the development of related products or services.
 - Emphasize your opportunities and explain how you will take advantage of them.
 - Discuss any product disadvantages or the possibilities of rapid obsolescence because of technological or styling changes, or marketing fads.
-
-
-
-

5. DESIGN AND DEVELOPMENT PLANS

If the product, process or service of the proposed venture requires any design and development before it is ready to be placed on the market, the nature and extent of this work should be fully discussed. The banker or investor will want to know the extent and nature of any design and development, and the costs and time required to achieve a marketable product. Such design and development might be: the engineering work necessary to convert a laboratory prototype to a finished product; the design of special tooling; the work of an industrial designer to make a product more attractive and saleable; or the identification and organization of manpower, equipment and special

techniques to implement a service business.

A. Development Status and Tasks:

- ◆ Describe the current status of the product or service and explain what remains to be done to make it marketable.
- ◆ Describe, briefly, the competence or expertise that your company has or can acquire to complete this development.
- ◆ Indicate the type and extent of technical assistance that will be required, state who will supervise this activity within your organization and experience in related development work.

B. Difficulties and risks:

- ◆ Identify any major anticipated design and development problems and approaches to their solution.
- ◆ Discuss their possible effect upon the schedule, cost of design and development, and time of market introduction.

C. Product Improvement and new products:

- ◆ Discuss any on-going design and development work that is planned to keep your product or service competitive, and to develop new related product that can be sold to the same group of customers.

D. Cost:

- ◆ Present and discuss a design and development budget. The costs should include labor, materials, consulting fees, etc. Miscalculations are often made about design and development costs and this can seriously impact cash flow projections. Accordingly, consider and perhaps show a 10-20% cost contingency. These cost data will become an integral part of the financial plan.

6. MARKET ANALYSIS

Market Research and Evaluation:

To be an attractive investment, a company should be selling to a market that is large and growing, and where a small market-share can provide significant sales volume. The company's competition should be profitable but not so strong as to overwhelm you.

The purpose of this section is to present facts to convince the reader that the product or service has a substantial market and can achieve profitable sales in the face of the competition.

Marketing research can help you learn many things about your business. One of the most important is an idea of how many customers you potentially have, and how many of these potential customers are likely to become actual buyers. Marketing research is the basis for the overall business strategy, especially the marketing and financial plans.

*The information you need to identify and count potential customers falls into four basic areas: **a.**) information within your own files, **b.**) information available to everyone (known as secondary sources), **c.**) research you do yourself, and **d.**) research you pay to have done.*

A. Customers:

Your customers are the most important part of your business. Without customers you wouldn't be in business. It's critical to carefully analyze who your customers are, how much and how often they buy from you, and why they do business with you rather than someone else.

The first place to start is to define customers by their physical characteristics such as age, gender, occupation, income, etc. These are important because they represent the natural categories of customers or segments. There are many but some of the more common customer characteristics include:

Gender – Men and women often exhibit very different habits when it comes to purchasing.

Age – is second only to gender as most important characteristic to measure.

Income – is a good indicator because it often shows whether the customer can buy.

Occupation – relates closely with age, income, and education.

Family status – couples needs differ significantly from singles.

Children – households with children can exhibit very different buying habits.

Education – is an indicator of advertising comprehension, reasoning power, etc.

Ethnic origin – people from different cultures have different values and needs.

Focusing on a target market begins with market segmentation. Market segmentation is the process of dividing a total market into market groups consisting of people who have similar product or service needs. Once this is accomplished, a marketing mix can be designed to meet the needs of the individuals in the group. The marketing mix is defined as the price, product, promotion, and distribution strategy used to reach the segmented market.

▪ **Identify customer characteristics for each segment**

- | | | | |
|------------------------------------|---|--|--|
| <input type="checkbox"/> Gender | <input type="checkbox"/> Age | <input type="checkbox"/> Income | <input type="checkbox"/> Occupation |
| <input type="checkbox"/> Location | <input type="checkbox"/> Marital status | <input type="checkbox"/> Children | <input type="checkbox"/> Education |
| <input type="checkbox"/> Race | <input type="checkbox"/> Religion | <input type="checkbox"/> Ethnic origin | <input type="checkbox"/> Home ownership |
| <input type="checkbox"/> Job title | <input type="checkbox"/> Industry type | <input type="checkbox"/> Experience | <input type="checkbox"/> Previous purchase |
| <input type="checkbox"/> Authority | <input type="checkbox"/> Annual sales | <input type="checkbox"/> Orientation | <input type="checkbox"/> Interests |
| <input type="checkbox"/> Other | | | |

Segment # 1	Segment # 2	Segment # 3

Adapted from Your Business Plan, Oregon Small Business Development Center, 1995

▪ **Buying Behavior**

- Describe who and where the *major purchasers* for the product or service in each market segment are. What are the bases of their purchase decisions: **Price, quality, service, personal contact, political pressures.**

- List any potential customers who have expressed an interest in the product or service and indicate why. List any potential customers who have shown no interest in the proposed product or service and explain why this is so. Explain what you will do to overcome negative customer reaction.

Further definition of the target market and market share is covered in the “Marketing Plan”.

B. Competition:

A key to the success of your business is establishing a unique market niche. In this section you will compare your business to your three major competitors. Be honest with yourself, the purpose is to help identify areas where you have a competitive advantage as well as areas for potential improvement.

- ❖ Make a realistic assessment of the strengths and weaknesses of competitive products and services and name the companies that supply them. Consider sales volume, geographic location, similarity of products, or similarity of business practices. **State data sources used to determine products and strength of competition.**

	<u>Competition Name & Address</u>	<u>Major strengths</u>	<u>Major weaknesses</u>
1-	_____	_____	_____
2-	_____	_____	_____
3-	_____	_____	_____
4-	_____	_____	_____

- ❖ Evaluate each competitor on the following factors:

1. *Products* – Which products do they carry? How do they compare with your products?
2. *Price* – Are pricing practices consistent? Explain.
3. *Quality* – How long does it last, how good is the workmanship?
4. *Product selection* – How complete is the product line?
5. *Customer service* – How politely and thoroughly is service performed?
6. *Product service* – Is the product serviced correctly and quickly?
7. *Reliability* – Does the product require frequent service or repair?
8. *Expertise* – The more knowledgeable the staff, the better.
9. *Image/Reputation* – How important is the company or product name?
10. *Location* – Consider accessibility, parking, convenience, and visibility.
11. *Layout* – Is the space efficiently utilized?
12. *Appearance* – Does the appearance match the customer's expectations?
13. *Sales methods* – Is the staff polite and effective at making sales?
14. *Credit policy* – Can customers use a variety of payment methods?
15. *Availability* – Does the customer have to wait for a product to arrive?
16. *Management* – Does the store owner take an active part in the business?
17. *Longevity/Stability* – How old is the business? In general, older businesses are considered more stable.
18. *Advertising* – Those who advertise are more visible than those who don't. What means are used? What message is sent? To Whom?

Present a short discussion of the current advantages and disadvantages of competing products and services and say why they are not meeting customer needs. Indicate the knowledge of competitor's actions that could lead you to new or improved products and an advantageous position.

Advantages

Disadvantages

_____	_____
_____	_____
_____	_____
_____	_____

Ability to Meet Needs

Perceived Opportunity

_____	_____
_____	_____
_____	_____
_____	_____

Adapted from Your Business Plan, Oregon Small Business Development Center, 1995

- Given your review of the strengths and weaknesses of the competing companies, determine and discuss the share of the market of each competitor-company, their sales, distribution and production capabilities. Review also the profitability of the competition and their profit trend. Who is the pricing leader and quality leader? Discuss why companies have entered or dropped out of the market in recent years.

Price leader: _____

Quality leader: _____

Reasons for market turnover: _____

- Discuss three of your four key competitors and why the customer buys from them. From what you know about their operations, explain why you think that you can capture a share of their business. Discuss what makes you think it will be easy or difficult to compete with them.

Competitor

Competitive Factor

<hr/> <hr/> <hr/> <hr/>	<hr/> <hr/> <hr/> <hr/>
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C. Achieving a Share of the Market

- Describe what it is about your product or service that will make it saleable in the face of current and potential competition.

- Identify any major first-year customers who are willing to make purchase commitments. Indicate the extent of those commitments and why they were made. Discuss which customers could be major purchasers in subsequent years and why.

D. Ongoing market evaluation:

Explain how you will continue to evaluate your market so as to:

- ◆ Assess customer needs and guide product improvement programs and new-products programs;
- ◆ Plan for expansions of your production facility;
- ◆ Guide product/service pricing

7. **MARKETING PLAN**

The marketing plan should detail the: Overall marketing strategy, sales and service policies, pricing, distribution and advertising strategies that will be used to achieve the estimated market share and sales projections. The marketing plan should describe what is to be done, how it will be done, and who will do it.

A. Overall Marketing Strategy:

The general marketing philosophy and strategy of the company develops from the market research and evaluation. It includes a discussion of what kind of customer groups will be targeted for initial intensive selling effort and what customer groups for later selling efforts; what features of the product or service (e.g. quality, price, delivery, warranty) will be emphasized to general sales; and any innovative or unusual marketing concepts that will enhance customer acceptance (e.g. leasing where only sales were previously attempted).

Based on customer profile in section 6, Market Analysis, continue with the following.

- Identify the marketing strategy most consistent with:

Targeted marketing strategy - Which reflects a base of customers that is unique, very well defined, concentrated in a particular area, or limited in some way.

General marketing strategy - reflects a customer base which includes a wide variety of people, a large market area, or a large number of buyers.

Combination marketing strategy - which reflects a blend of both targeted customers and general customers.

- ◆ Indicate whether the product or service will be introduced nationally or on a regional level. If on a regional level, explain why and indicate any plans for extending sales to

other sections of the country.

- ◆ Discuss any seasonal trends and what can be done to promote sales out-of-season.

Adapted from Your Business Plan, Oregon Small Business Development Center, 1995

B. Estimated market share and sales:

Given your assessment of the advantages of your product or service; the market size and trends; customers; the competition and their product; attempt to estimate the share of the market that you will acquire in each of the next 2-3 years. The growth of the company's sales and its estimated market share should be related to the growth of its industry and customers and the strength and weaknesses of competitors.

- ❖ Determine the number of potential customers. Use the segment characteristics you have identified and sources of data and methods used to establish size.

- 100 % Identify the total market (for example, all who fit the segment characteristics)
- X 50 % Identify the available market (all the markets you could potentially work with)
- X 50 % Identify the addressable market (eliminate least likely categories)
- X 50 % Identify the target market (most likely in terms of competition, demand, etc.)
- X 20 % Identify the capture market (The % of the target market you can count on the first couple of years)

- *Source "Gain Creditability with Financiers by Identifying Capture Market" by Scott Clark, Arizona Business Journal, 5/11/95*

Identify and explain

- ❖ Any differences between past and projected annual growth rates. Indicate the sources of all data and methods used to make projections
- ❖ Project markets and growth trends for at least three future years.
- ❖ Determine your average customer sales per year (sources may include Trade Association or industry publications.)

A. How many purchases will your average customer make in a year? _____

B. How much will they spend on each purchase? \$ _____

C. Multiply A * B to determine the annual spending of an average customer \$ _____

- ❖ Determine annual sales volume

Number of customers in Capture Market _____

Average customer sale X \$ _____

Annual Sales volume \$ _____

(Be sure facts support this estimate)

C. Pricing

Consumers consistently evaluate products by some combination of price and quality. Of course there are other conscious and unconscious factors which can govern behavior, but price and quality are the two factors commonly found in nearly all purchase decisions.

Each product has a product identity, or profile, based on the balance of these two variables. Competition begins by evaluating the perceived differences in each product's basic price/quality profile. Product profiles tend to run in cycles based on product age. Examples of the four basic profile combinations are:

Low Price/High quality -An ideal product profile which balances price and quality in the customer's favor. Many new businesses establish themselves with this profile because it competes so easily with the other three possible profiles.

High Price/High Quality - As demand for product increases, producers realize they can increase the price assuming quality also remains high. Mercedes Benz, Rolex, and Nike are all representative of this group.

High Price/Low Quality - Companies with older well-established products are lured by the profit inherent in cheapening the product and coasting on a quality reputation. Customers, once betrayed, seldom give these products a second chance.

Low Price/Low Quality - The “discount” philosophy of many mass merchandisers was once thought to be the wave of the future. Because product quality from discounter to discounter is the same, price assumes greater significance.

- ◇ Discuss the prices to be charged for your product and/or service and compare your pricing policy with those of your major competitors.

- ◇ Discuss the gross profit margin between manufacturing costs and sales prices. Indicate whether this margin is large enough to cover the cost of: distribution and sales; warranty, service; amortization of development and equipment expense; price competition; and still allow a profit

- Explain how the price you set will enable you to:
 - ~ Get the product or service accepted.
 - ~ Maintain and desirably increase your market share in the face of competition.
 - ~ Produce profits.

- ◆ Justify price increases over competitive items on the basis of newness, quality, warranty and service, etc.

- ◆ If a lower price than your competition's is to be charged, explain how you will do this and maintain profitability, for example, greater effectiveness in manufacturing and distributing the product, lower labor costs, lower overhead, or lower material costs.

- ◆ Discuss the relationship of price, market share and profits. For example, a higher price may reduce volume but result in a higher gross profit.

- ◆ Describe any discount allowance for prompt payment or volume purchases.

Adapted from Your Business Plan, Oregon Small Business Development Center, 1995

D. Sales Tactics:

In this section , describe the methods that will be used to make sales and distribute the product or service. Will the company use: its own sales force; sales representatives; distributors? Are there ready-made manufacturer's sales organizations already selling related products that can be used? Describe both the initial plans and long range plans for a sales force. Discuss the margins to be given to retailers, wholesalers, and salesmen and compare them to those given by your competition.

- Indicate how your sales force will be structured and at what rate it will be built up. If it is to replace a dealer or representative organization, indicate when and how.
- Show the sales expected per salesman per year, and what commission, incentive and/or salary they are slated to receive.

- Describe how they have been selected, when they will start to represent you, and the areas they will cover.
- Show a table that indicates the build-up of dealers and representatives by month and the expected sales to be made by each dealer.
- Describe any special policies regarding discounts, exclusive distribution rights, etc.

If OEM (original equipment manufacturer) or government contracts are to be sought, discuss *how*, *why* and *when* these will be obtained.

- As an exhibit, provide a selling schedule and a sales budget that includes all marketing, promotion and service costs.

E. Service and warranty policies:

If your company will offer a product that will require service and warranties, you need to indicate the importance of these to the customer's purchasing decision and discuss your methods of handling service problems.

- ◇ Describe the kind and term of any warranties to be offered, whether service will be handled by company servicemen, agencies, dealers and distributors, or factory return.
- ◇ Indicate the proposed charge for service calls and whether service will be a profitable or breakeven operation.
- ◇ Compare your service and warranty policies and practices with those of your principal competitors.
- ◇ Indicate what kinds of service manuals will be prepared.

F. Promotion and Advertising:

Promotion is the element in the marketing mix that “encourages the purchase of a product or service”. It includes advertising, personal selling, sales promotion, and public relations.

Advertising is defined as “paid non-personal communication from an identified sponsor using mass media to persuade or influence an audience.” It provides information that helps match buyers and sellers in the marketplace.

The first step in developing a promotion strategy is to identify your objectives. Example objectives are:

- Create awareness
- Enhance comprehension (establish knowledge of the product’s and its uniqueness)
- Gain conviction (create a positive liking and a preference for the product)
- Influence action (elicit a response that results in a purchase)

The objective and the customer profile will influence the best type of methods and media to use to achieve the results you want.

OEM and industrial products common advertising and promotional activities include:

- 1) Tradeshow participation
- 2) Trade magazine advertisements
- 3) Direct-mailings
- 4) Preparation of product sheets and promotional literature
- 5) Use of advertising agencies, service and products.

- Indicate what kind of advertising and promotional campaign is contemplated to introduce the product/service and what kind of sales-aids will be provided to dealers. Include a schedule and cost of promotion and advertising.

- If advertising is a significant part of company expenses, show how and when these costs will be incurred.

8. **MANUFACTURING AND OPERATION PLAN**

The manufacturing and operations plan should describe the kind of facilities, plant location, space requirements, capital equipment and labor force (part and full time) that are required to produce the company's product or service. For a manufacturing business, stress should also be given to the production process that will be used, inventory control, purchasing and production control, and make or buy decisions, (for example, which parts of the product will be purchased and which operations will be performed by your work force).

A service business may require particular attention and focus on an appropriate location, ability to minimize overhead, lease the required equipment, and obtain competitive productivity from a skilled or trained labor force.

The discussion guidelines given below are general enough to cover both product and service businesses. Only those that are relevant to your venture - be it product or service should be addressed in the business plan.

A. Geographical Location

- Describe the planned geographical location of the business and discuss any advantages or disadvantages of the site location in terms of wage rates, labor unionization, labor availability, closeness to customers or suppliers, access to transportation, state and local taxes and laws, utilities and zoning. For a service business, proximity to customers is a "must." Describe your approach to overcoming any problems associated with the location.

Address of facility: _____

<u>Advantages</u>	<u>Disadvantages</u>
_____	_____
_____	_____
_____	_____

Access to transportation: _____

Zoning: _____

Taxes and laws: _____

Utilities: _____

Nearby businesses: _____

* Provide photos and map *

B. Facilities and Improvements:

- * Describe the facilities required to start and conduct the company's business. Indicate the requirements for: Plant and office space; storage and land areas; machinery, special tooling and other capital equipment; and utilities.

*

*

*

*

Facilities requirements

- Provide layout drawing
- Discuss whether equipment and space will be leased and improved, or bought and indicate the costs and timing of such actions. Indicate how much of the initial financing will be devoted to plant and equipment. These cost data will become part of the financial plan.

- ◆ Describe occupancy costs of location

Lease:	Insurance:	Water/Sewer:
Taxes:	Electric:	Telephone:
Gas	Maintenance	Garbage:
Other:		

◆ Future needs of facility

- 1) List how and when initial plant space and equipment will be expanded and the capacities required by future sales projections.
- 2) List any plans to improve or add to existing plant space or move the facility.
- 3) List future equipment needs and indicate the timing and cost of such acquisitions. (A three-year planning-period should be used for these projections)

1) _____

2) _____

3) _____

C. Strategy and Plans

Outline the manufacturing process involved in your product's production, and any decisions with respect to subcontracting of component parts rather than complete in-house manufacture.

The "make or buy" strategy adopted should be determined by consideration of inventory financing, available labor skills and other non-technical questions as well as purely production, cost and capability issues (your company might operate as a labor-intensive assembly plant and purchase basic parts and subassemblies). Justify your proposed "make or buy" policy. Provide the results of any surveys of potential sub contractors and suppliers, and list who these are likely to be.

Present a production or operations plan that shows cost-volume information at various sales levels of operation with full breakdowns of applicable material, labor, purchased components, and factory burden.

- * What inventory is required at various sales levels? (These data will be incorporated into cash flow projections.)
- * What are plans for a build-up in the labor force and the added labor hours needed to increase output.
- * How will seasonal production loads will be handled without severe dislocation? For example, by building inventory or using part-time help in peak periods?
- * How will daily shift-to shift variations in the labor force be handled?

* Describe your approach to:

1) Quality control

2) Production control

3) Inventory control

What quality control and inspection procedures will the company use to minimize service problems and associated customer dissatisfaction?

- * Explain how the purchasing function will be organized and operated to ensure that adequate materials are on hand for production, that the best price has been obtained and what raw materials and in-process inventory, and hence, working capital needs have been optimized.

D. Labor Force:

1. Exclusive of management functions, explain how the local labor force has the necessary skills in sufficient quantity and quality (lack of absenteeism, adequate productivity) to manufacture the product or supply the services of the proposed company.

If the skills of the labor force are inadequate to the needs of the company, describe the kinds of training that you will use to upgrade labor skills.

2. Identify

- ~ Job titles and skills
- ~ Pay scale
- ~ Sources of employees

- ~ Processes to recruit, screen, and hire
- ~ New employee training
- ~ Cost of training
- ~ Upgrade training

3. Describe how and where employees will be recruited, screened, and hired

4. Outline plans for training employees: new, upgrades, costs involved

9. **OVERALL SCHEDULE**

A schedule that shows the timing and interrelationship of the major events necessary to launch the venture and realize its objectives is an essential part of a business plan. In addition to being a planning aid and showing deadlines critical to a venture's success, a well-prepared schedule can be an extremely effective sales tool in raising money from potential investors. Properly prepared and realistic, it demonstrates the ability of the management team to plan for venture growth in a way that recognizes obstacles and minimizes investor risk.

Prepare a month-by-month schedule that shows the timing of such activities as: product development; market planning; sales programs; production and operations. Sufficient detail should be included to show the timing and responsibility of the primary tasks required to accomplish an activity.

Show, on the schedule, the deadlines or milestones critical to the venture's success. This should include events such as:

- ◆ Incorporation of the venture
- ◆ Completion of design and development

- ◆ Completion of prototypes (a key date; its achievement is a tangible measure of the company's ability to perform)
- ◆ Product display at trade shows
- ◆ Ordering of materials in production quantities
- ◆ Start of production or operation (another key date because it is related to the production of income)
- ◆ First orders received
- ◆ First sales and deliveries (a date of maximum interest because it relates directly to the company's credibility and need for capital)
- ◆ Payment of first accounts receivable (cash in)

The schedule should also show the following and their relation to the development of the business.

- ◆ Number of management personnel
- ◆ Number of production and operations personnel
- ◆ Additions to plant or equipment

Describe the activities most likely to cause a schedule slippage, and what steps you would take to correct such a slippage. Discuss the impact of schedule slippage on the venture's operation, especially its potential viability and capital needs. *(Keep in mind that the time to do things tends to be under-estimated, even more than financing requirements. So be realistic about your schedule).*

10. **COMMUNITY BENEFITS**

The proposed venture should be an instrument of community and human development as well as economic development, and it should be responsive to the expressed desires of the community.

Describe and discuss the potential economic benefits to members of the community that could result from the formation of the proposed venture.

Among the benefits that may merit discussion are:

A. Economic

- Number of jobs generated in each of the first three years of the venture
- Number and kind of new employment opportunities for previously unemployed or underemployed individuals
- Number of skilled and higher paying jobs
- Ownership and control of venture assets by community residents
- Purchase of goods and services from local suppliers

B. Human Development

- New technical skills development and associated career opportunities for community residents.
- Management development and training
- Employment of unique skills within the community that are now unused or underused

C. Community Development

- Development of community's physical assets
- Provision of needed, but not supplied, services or products to community
- Improvements in the living environment
- Community support, participation and pride in the venture
- Development of community-owned economic structure and decreased absentee business ownership

Describe any compromises or time lags in venture profitability that may result from trying to achieve some or all of the kinds of benefits cited above. Any such compromise or lags in profitability should be justified in the context of all the benefits achieved and the role of the venture in a total, planned program of economic, human and community development.

11. **THE FINANCIAL PLAN**

The financial plan is basic to the evaluation of an investment opportunity and should represent the entrepreneur's best estimates of future operations. Its purpose is to indicate the venture's potential and the timetable for financial viability. It can also serve as an operation plan for the financial management of the venture.

In developing the financial plans, five basic exhibits must be prepared:

- a. *Sources and Uses Statement*
- b. *Profit and loss forecasts for three years*
- c. *Cash flow projections for three years*
- d. *Pro forma balance sheets for three years*
- e. *Breakeven chart*

A breakeven chart should be presented that shows the level of first-year production that is required to cover all operating costs.

A. Sources and Uses Statement

Be sure assumptions about loan terms and equity requirements are correct. Written estimates on assets contributed or to be purchased must support the Sources and Uses Statement. For purposes of estimating, use a straight line depreciation method on equipment and vehicles. An estimate of three to six months available cash for working capital is realistic. The amount of "Sources" must equal the amount of "Uses." If letters of credit or commitments from bankers or vendors have been received, they should be attached.

Sources and Uses Statement example is provided in Exhibit II.

B. Profit And Loss Forecast

1) Discussion of Assumptions

Because of the importance of profit and loss projections as an indication of the potential financial feasibility of any new venture to potential investors, it is extremely important that assumptions made in its preparation be fully explained and documented. If these statements are to be useful they must represent management's realistic assessment and best estimates of probable operation results. Sales or operational cost projections that are either too conservative or too optimistic have little value as aids to policy formulation and decision-making. Thinking about assumptions before startup is useful for identifying issues that require consideration before they turn into major problems.

Reference the market research in section **Estimated Market Share and Sales, page 22** for revenue estimates.

Once the sales forecasts are in hand, production (or operations for a service business) should be budgeted. There must be a determination of the level of production or operation that is required to meet the sales forecasts and fulfill inventory requirements. The material, labor, service and equipment requirements must be developed and translated into cost data. A separation of the fixed and variable elements of these costs is desirable, and the effect of sales volume on inventory, equipment acquisitions and manufacturing costs should be taken into account. The operation plan is the source for these cost data. Earnings projections should be prepared monthly for the first two years of operation and quarterly for the third year.

Cost of Goods Sold is deducted from gross revenue to obtain a gross profit margin. This category should include all costs directly related to creating the revenue. For example, a manufacturer will include direct labor (including benefits), materials, and manufacturing overhead. Service companies will include the costs of direct labor (including benefits) and materials or supplies used to perform the service. Retailers will include their beginning inventory, purchases, and ending inventory to calculate the costs of goods used during the period.

Operating Expenses are indirect expenses that are incurred even if revenue is not gained. Sales expense includes the costs of selling and distribution, storage, discounts, advertising and promotion. General and Administrative expense includes management salaries, clerical costs, and legal and accounting expenses, rent, utilities, management fringe benefits, telephone, etc.

The pro forma profit and loss statement will be more meaningful if all costs are shown as a proportion of sales. It will allow figures to be compared with industry standards and enable comparisons of subsequent years. Dun and Bradstreet Industry Norms and Key Business Ratios and Robert Morris Annual Statement Studies are good sources of industry benchmarks.

Projected cash flow should include assumptions made on timing of collection of receivables, trade discounts given, terms of payments to vendors, planned salary and wage increases, anticipated increases in other operating expenses, seasonal characteristics of the business as it affects inventory requirements, and capital equipment purchases. It is especially important to anticipate quarterly and annual tax payments since these require holding funds in reserve until needed. As with the sales and income projections it is also important that these assumptions represent management's best estimates.

The Cash Budget worksheet (Exhibit IV) describes the revenue and expense categories of profit and loss as well as cash flow projections. It must be comprehensive and thorough.

In addition to serving as a basis for planning, the projected income statements should be used for operation control functions. Through comparisons with actual operation sales and profit information, the operating status of the venture can be determined relative to the objectives that have been set in the plan. This type of analysis can be used by management to indicate critical factors which need attention and can indicate the need for a reassessment of the underlying assumptions used to develop the projections. See Profit and Loss Worksheet Exhibit III

2) Risks And Sensitivity

Once the most likely statements have been prepared, discuss the major risks that could prevent those goals from being attained, and the sensitivity of profits to these risks.

Outline some of the risks that might be encountered in the firm itself, the industry, and the environment. This could include things as specific as the impact of a 20% reduction in sales projections on the learning curve requirements of management and non-management employees, and how this will affect the level of productivity over time.

C. Pro Forma Cash Flow Analysis

1) Discussion of Assumptions

For a new venture the cash flow forecast can be more important than the forecasts of profits because it details the amount and timing of expected cash inflows and outflows. Usually the level of profits particularly during the startup years of a venture, will not match the outflows on a short-term basis. The cash flow forecast will indicate these conditions and enable management to plan cash needs.

Given a level of projected sales and capital expenditures over a specific period, the cash forecast will highlight the need for additional financing and indicate peak requirements for working capital. Management must decide how this additional financing is to be obtained, on what terms, and how it is to be repaid. This information becomes part of the final cash flow forecast.

If the venture is in a seasonal or cyclical industry, or is in an industry in which suppliers require a new firm to pay cash, or if inventory build-up occurs before the product can be sold for revenues, this cash forecast is crucial to the continuing solvency of the business. A detailed cash flow forecast which is understood and used by management can enable them to direct their attention to operation problems without distractions caused by periodic crises which should have been anticipated. Cash flow projections should be made for each month of the first year of operation and quarterly for the second and third years.

See Cash Budget Worksheet Exhibit IV.

See Cash Flow Worksheet Exhibit V.

2) Cash Flow Sensitivity

Once the cash flow has been completed, discuss the implications for funds needs that possible changes in some of the crucial assumptions would have. This is designed to enable the entrepreneurial team to test the sensitivity of the cash budget to a variety of assumptions about business factors and to view a wider range of possible outcomes. Investors are vitally interested in this because it helps them estimate the possibility that you will need more cash sooner than planned.

D. Pro Forma Balance Sheets

The balance sheets are used to detail the assets required to support the projected level of operations indicated in the income projections and, through liabilities and equity, how these assets are to be financed. Every accounting transaction can be recorded in terms of its effect on the balance sheet. Investors look to the projected balance sheets to determine debt to equity ratios, working capital current ratios, inventory turnover, etc.

In forecasting balance sheets, it will be necessary to project inventory levels, capital expenditures and incurrence of debt in addition to the other forecasting data described above. Pro forma balance sheets should be prepared at startup, quarterly for the first year, and at the end of each of the first three years of operation.

See Balance Sheet Worksheet Exhibit VI

1) Discussion Of Assumptions

The Pro Forma Balance Sheet must be consistent with the Sources and Uses Statement as well as descriptions of management participation and ownership.

E. Break-even Chart

A break-even chart is a way of determining the level of sales of production at which sales will cover costs. This includes those costs that vary with production level (manufacturing labor, materials, sales costs) and those that do not change with production level (rent, interest charges, executive salaries, etc..) The sales level that just covers all costs is the minimum sales objective for the venture. It is very useful for the investor and the management to know what the break-even point is and whether it will be easy or difficult to attain. You should prepare a break-even chart and discuss how the break-even point might be lowered in case you start to fall short of your sales projections. You should also discuss the effect of lower production quantities on the cost of production.

See Exhibit VII for Break-Even Analysis

12. **PROPOSED FINANCING**

This section is to be devoted to a discussion of the current and proposed capital structure of the venture and to a summary of management's conclusions about the timing and probable sources of funds to meet peak cash requirements.

Structure so that the following issues are covered:

- ❖ Identification of the initial equity investors: name _____
Amount invested _____, Shares received _____,
At what cost _____
- ❖ Initial long-term debt: Interest rate _____, repayment terms _____,
and sources _____.
- ❖ Description of the type of funding requested _____
- ❖ Description of how the capital funds will be allocated to the various business operations. Approximately how will the funds be used: working capital _____, Equipment purchases _____, debt repayment (if any) _____, cover projected operating losses, etc. _____
- ❖ Based on the cash flow forecast, management's conclusions about the timing of peak cash needs and how they plan to meet these requirements. For example, return to original sources for additional funding, secure a line of credit with the bank, take on additional long term debt, attract new equity investors, factor receivables.
