

Business Plan Basics
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Goals

For rapidly growing companies, a business plan is a key management tool that can be used for a variety of reasons:

- Attract debt or equity financing
- Promote relationships with joint venture partners and large customers, suppliers, and distributors
- Provide strategic guidance, operating tactics and objectives
- Furnish a standard against which to judge future business decisions and results.
- Evaluate strengths and weaknesses and identify viable alternative strategies
- Establish the operational and financial structure of a management buy-out

Regardless of the exact impetus, a business plan is a fundamental requirement for all start-up and rapidly growing businesses.

Due to the array of business plan goals and the endless variety of circumstances, there is no such thing as a standard business plan. Furthermore, a business plan should not be static.

Over its lifetime, a business typically goes through several stages. Although the number and names of these stages vary by economist, it is safe to speak of at least three stages: start-up, growth, and maturity. Generally, each stage in the life of a business represents an increase in revenues and employees -- and perhaps in product lines, assets, etc. -- and requires a greater delegation of routine functions. The transition to a new stage represents a critical phase in the life of a business. This transition, along with changes inherent in a business's growth, changing market conditions, evolving company strategies, and actual financial results, signals the need to update the business plan.

The outline presented below has been formulated based on PricewaterhouseCoopers LLP's experience with start-up ventures and rapidly growing businesses. You will need to make certain modifications to your business plan depending on whether your company is in the technology, manufacturing, service, retail or export industry. However, the basics are the same. Regardless of your business, it is important to remember that this outline should be used as a guide, not as a rigid, all-encompassing format.

A few generalizations about business plans

The executive summary is critical: This two to three page summary of the business plan is what most investors turn to first; it often determines whether they will read the remainder of the plan or decline the opportunity. This section should always be written last.

Clarify the focus: The plan should be clear about the products to be developed and the markets to be addressed by the business. Try to avoid saying that the company will develop a widget and sell it to General Motors and the grocery store down the street without explaining how it will actually be done.

Transition into a rapidly growing environment: Businesses that are emerging from less dynamic environments need to provide an accurate critique of past performances (i.e., strengths/weaknesses) More importantly, they need to clearly describe what has changed about the business and the reasons for the changes.

Avoid superlatives: The "trust me" school of thought does not work in business plans. If your product is going to be the best in the market, thoroughly explain why.

Quantity does not equal quality: A well written plan should be succinct and to the point and is usually 30 to 50 pages.

First impressions are lasting impressions: There are many things that can sink a plan including incorrect spelling, grammar or punctuation; the use of unprofessional language; numbers that do not total; or poor organization. Take the time to have the plan reviewed by at least three other members of your team.

"Slick" plans can be a turnoff: Expensive looking plans are often perceived as form over substance, frivolous and a waste of scarce financial resources. To give your business plan a professional look,

consider including a plastic binding, a title page including your company name, address, date, contact name and copy number, numbered pages, and a detailed table of contents.

Support assumptions with independent sources: Assumptions made with regard to the target market and competition should be supported by independent, third-party data whenever possible. This lends credibility to the plan in the eyes of the reader.

Avoid the use of non-assertive language: Vague, qualifying words such as "might", "probably", "maybe" and "perhaps" can have a subtly negative effect on the reader. Be positive and definitive.

Confidentiality

Rapidly growing companies are usually heavily dependent upon a few key technologies which are not always patent protected and are particularly prone to competition while in a development stage.

Therefore, a business plan should be clear and concise but should not reveal information that could reduce the company's competitive edge. Two methods of promoting confidentiality are described below:

Non-disclosure Agreement: This is a statement indicating that the information in the plan is proprietary and is not to be shared, copied, disclosed, or otherwise compromised. The agreement can be verbal or take the form of signed documentation. Be prepared to negotiate on signed non-disclosures as potential investors sometimes balk at such agreements.

Control Numbering: The control number, usually included on the first page of the plan, is cross-referenced to a journal kept by the entrepreneur (e.g., copy 14 issued to Jake Johns on November 10, 1997). Control numbering helps to keep track of your plans and when they were issued. Should the recipient of a business plan not become an investor, control numbering facilitates the Company's requests for the return of the business plan. The number of plans that you distribute should also be kept to a minimum. Excessive exposure of your idea to the investing community can lessen its overall appeal.

Executive Summary

Many consider this the most important part of the business plan because it is what investors usually will read first. It is the "teaser" through which you need to convince an investor to spend more time on the plan itself. This section should always be written last so that each individual section being summarized has been thought through and analyzed fully.

The executive summary should be between one and three pages in length. It should be a concise and clear highlight of what the company is all about and what's in it for the investor. The executive summary should include a few sentences on each of the following, while at the same time remaining concise:

The company

- When formed?
- To pursue what purpose?
- Exploit a particular technology
- Design a new product
- Manufacturing
- Marketing

What are the Company's goals?

- Short-term
- Long-term

What are the Company's critical success factors?

- The product(s)
- What are you selling?
- What makes it unique?
- Is it a proprietary product? Other entry barriers?
- At what stage is its development?

Features that distinguish it from competition:

- Pricing

- Quality
- Speed

The market

- Current size
- Domestic/international
- Recent growth (cite sources)
- Projected growth (cite sources)
- Estimated company market share

Financial

- For what purposes?
- Will carry company how far?
- Exit strategy for investors?

Management

- How complete is the team?
- Brief past experience
- Highlight strengths

The company

In this section, a more thorough description of the company is given, including the short- and long-term goals of the company, its strengths/weaknesses, and critical success factors.

What business are you in?

- Address in broad terms before getting specific
- Be imaginative (go beyond obvious answer)

What are your company's goals?

- Be as explicit as possible
- Include sales, income, Return on Investment (ROI)
- Try to quantify more obscure goals (e.g., customer satisfaction rates)

What are the company's critical success factors?

- These are not the same as business objectives, but will lead to their achievement.

What are the company's past achievements and strengths?

- Do you plan to do more of what has worked in the past or start new, complementary lines of business?

What are the company's past problems and weaknesses?

- Those that threaten company survival must be eliminated/controlled.
- Those that do not may be eliminated if cost-effective.

Other general information to be included as appropriate:

- Date and form of business organization
- Past and anticipated changes in business form
- Principal investors and management
- Organizational structure

Products (services)

Provide a detailed description or illustration of existing products and plans for future products. Are products market-ready or, if not, when will they be? Also included should be any unique features (e.g. brand names) or other possible sources of competitive advantage. This section of the business plan should present information derived from the answers to the following questions:

Existing products

- Does your product have any patents or other proprietary features? (trademarks, copyrights)
- How is your product different from the competition's?-- compare capabilities, strengths/

weaknesses, and characteristics of your product to those of your competitors.'

- How up-to-date are your products? -- address potential obsolescence or losses of market share.
- What is the output and sales mix for each of the company's products/services?
- What are the sales price, cost, and profit margin for each product line?
- Who makes up your current customer base? (both direct and ultimate end-users)
- What is included in the product's bill of materials? (major components only, not too detailed)
- Are there any current/potential component supply problems?

Future Products

- Any planned innovations to the existing product lines? Any new products/services?
- If the answer is affirmative, provide development time projections.
- What are the expected sales price, cost and profit margin on future products and how is the overall sales mix and profitability expected to change?

Industry analysis

The purpose of this section is to explain why your product/service will give your company a sustainable competitive advantage.

By answering the following questions, you can effectively assess your competitive environment: (Be sure to include information on current industry status and trends as well as the industry status and trends of your customers, indirect competitors, and key suppliers.)

- What is the size, maturity, and competitive nature of the industry?
- What are the barriers to entry and growth?
- How do economic developments affect the industry?
- What is the industry's financial position and performance?
- What is the role of innovation and technological change?
- How is the industry affected by government regulation?

Market analysis

Emphasize the opportunities for your company to achieve its goals by answering the following questions:

- What is your target market and to whom are you trying to sell? (may be different)
- What is the size of your target market?
 - Historical
 - Current
 - Projected (5 years)
- How can you segment your target market? (by region, age, income, profession, etc.)
- Natural splits--geographic, industries, volume vs. unit buyers, etc.
- Growth prospects within each segment
- What are the trends in your target market?
 - Where is the market going and why?
 - What are the economic trends?
 - Maturity of the market--growth stage or stable?
- Who are your competitors? What do you know about them? Address the following aspects:
 - Relative size
 - Competitive strengths/weaknesses
 - Markets addressed/market share
 - Reputation
 - Prospects
- Who are your customers and what are their product/service preferences and reasons for purchasing?
 - Who is buying? OEMS, end users?
 - Why are they buying?

- What are they looking for?
- What are the factors that drive their buying decisions?
- How does distribution take place in your target markets?
- Value Added Resellers (VARs)
- Direct sales
- Distributors
- Manufacturers' representatives
- What are your company's sales and profits by market segment? (current and projected)
- What is your company's current and projected market share? (This is an important indicator of your company's success.)

How well you know your market will also be demonstrated in this section. The sources for intelligence in any market are numerous. The following are just a few suggestions:

- Existing competitors
- Product brochures
- Annual reports filed with the SEC (public companies only)
- Interviews with marketing people. This requires a degree of brashness. Don't be timid about asking a potential competitor to lunch to pick his or her brain.
- Trade publications: If you don't know what's available, ask someone who does. Call editors for further suggestions on sources.
- Users of existing products
- Purchasing directors
- Manufacturing directors
- Potential customers: It is absolutely essential that you have as many discussions as possible with users before, during, and after the formation of the company. Their feedback should be incorporated into both your products and plans.

Marketing strategy

After the thorough description of the market, this section should be an in depth coverage of how you plan to get products to your buyers and what strategies you'll use to help accomplish that task. Answers to the following questions will encapsulate your business's approach to marketing:

- What is your target market (by segment)?
- Geographic
- Industry
- Type of buyer

Specifically identify the customer groups you will address. What is it about the segment that makes it right for your rapidly growing company? Are the customer groups ignored or ill-served by your competitors? If you enter this market and make a profit, why won't a larger competitor enter it (revenue volume too low, buyers in the market are unit purchasers, etc.)?

What geographic advantages/disadvantages does your company face?

- How will you establish credibility (company and product)? Why should customers buy a new product from an unproven company?
- Will your pricing strategy be high, moderate, or low relative to the market and why?
- Will credit be extended and under what conditions?
- Will warranty policies be standard or non-standard with your product? Will their cost be included in the cost of the product or be additional?
- To generate sales, what product or service attributes will your company emphasize?
- What will be the image you strive for? Your level of quality, reliability, service, response time should fit neatly with other strategies (i.e., quality and low price may not appear to make sense--if they do in your case, explain why).

- How much will be spent on advertising and public relations? In which channels will these dollars be spent? (These strategies should match with others; i.e., are ads in Modern Mechanics compatible with the objective to develop an image of quality?)
- What distribution channels will you utilize?

Describe the physical means by which the product will be delivered to buyers:

- Factory distribution
- Company-owned regional distribution
- Independent remote distribution
- Order lead times
- How will product servicing be facilitated so that fixing product problems entails the least cost to you and minimum disruption to your customer?
- Factory-only service
- Company field service engineers
- Contracted service
- Services contracts
- Profit centers
- Loss leaders
- How are you going to sell the product? If you use sales reps, what kind of incentives will you use to get them to know and push your products? Is it a highly technical product requiring skilled sales people? Should senior management in your company participate directly in the sales effort to establish company and product credibility? How many salespeople will you require to reach projected sales levels?
- How will you compensate sales people-- commissions (payable on order or on receipt of payment), bonus, salary, or some combination?
- Direct sales
- Reps
- Distributors
- Retailers
- Hybrid

Management

The strength of management simply cannot be overstated in an investment decision. Remember the venture capital axiom that a mediocre product with great management is always preferred to the opposite. Highlight the past experiences of the management team that will combine to reduce the risk typically associated with a start-up venture or rapidly growing company. The following information should be included in this section of any business plan:

- Summary resumes of key management and owners — List education, skills, experience (including past duties). Focus on important past accomplishments but don't be too lengthy. Detailed resumes may be included in an appendix to the business plan.
- Functional responsibilities — Who is charged with what in the operations of the company? How is this anticipated to change in the future?
- Management holes — If important functional areas are not filled, what steps will be taken to fill them and when?
- Management philosophy — What is the company's decision-making and management philosophy?
- Board of Directors — If already in existence, include affiliations and experience of each member. If not, discuss current status of plans for formation.

Implementation plan

Having responded to questions basic to any business plan or relevant to your unique circumstances, you are ready to develop a plan for executing your business strategy. This can be achieved by listing the following actions and activities, by business function, that are necessary to achieve the goals of the business (be sure to include a timetable indicating when each planned activity is to be undertaken and completed):

- Research and development (R&D): Resources committed or planned Expected results
- Facility requirements: Leased Purchased

- Labor requirements: Local labor pool Skilled/unskilled
- Subcontracted production: Sole or multi-sourced Quality control Supply problems
- Capital needs: Equipment list Financial requirements
- Quality control: Raw materials Manufacturing Finished goods
- Critical processes: Capacity Critical paths Cost characteristics (fixed, variable, semi-variable)
- Seasonality Inventory control: Inventory turnover Production size Lead time Storage requirements
Waste/shrinkage factors Obsolescence

Financing

Before your business plan will be considered by investors, you must answer the following questions:

- What is the total amount of funds needed by your business? Is it needed immediately or over the next two to five years?
- What part of this financing is being sought from the investors or lending institution who will receive this business plan? (including the amount, terms, and any related security agreement)
- For equity financing—What percentage of the company are you willing to give up and what is the proposed return on investment and anticipated method of taking out the investor (e.g., buy-back, public offering, sale)?
- For debt financing—What is your company's proposed interest rate and repayment schedule?

Financial information

Financial projections should include high level figures, although underlying detail should be available for further discussion. Present five-year projections: monthly for the first two years, and quarterly for the remaining three years. Also include any historical financial information that is available, including all applicable footnotes and any audit or review opinions. In addition, the financial information:

- Should be a reflection of your business plan quantified (therefore, it must be consistent with the body of the plan)
- Will help demonstrate whether your strategy is financially feasible and whether it allows you to reach your goals and objectives
- Is a key indicator of the amount of outside financing necessary to support the execution of your strategy
- Should include future projections which answer the following questions:
 - How will the company perform financially? - Profit and loss projections
 - What will the company's cash position be? - Cash flow projections
 - What will the company's financial position be? - Projected balance sheets
- Should include a list of significant assumptions used in any individual section or throughout the financial projections that are:
 - Material to the projected amounts
 - Especially sensitive to variations
 - Deviations from historical trends
 - Especially uncertain
- Should include key financial ratios and should compare to competitors/industry averages. Key ratios include current, debt-to-net worth, return on equity, gross margin, and break-even point (in both sales units and dollars)

Industry-specific data

The foregoing material represents the minimum you should include in a business plan. To provide further reassurance to yourself and outside investors, you should develop additional industry specific information to supplement your basic plan.

Technology

Several characteristics tend to distinguish technology companies:

- High intellectual content of such companies is difficult to value and protect.
- Obsolescence is likely.
- Effective management and retention of key personnel is critical.
- Commercialization of innovations may require major changes to business structure.

- R&D costs usually exceed expected cash flows and revenues for several years.
- High growth is expected relative to other markets and industries.

Answers to the following questions should be included in the business plan of a technology company. In addition, answers to applicable questions for manufacturing companies should also be incorporated into the business plan.

- What products has your company introduced in the last one to three years? (Review age of product mix for signs of obsolescence.)
- What is the status of products/services still undergoing research and development?
- What is required to complete the development process? (Mention specific equipment or personnel, costs and other financial requirements, timing, and anticipated obstacles.)
- How does R&D fit into your company's strategy? (Consider the following about R&D programs: purpose, direct costs, facility requirements, financing needs, and expected benefits - often 10-15% of revenue is spent on R&D by technology companies.)
- What is the best way to protect the intellectual content of your innovations? (e.g., internal security, patents, copyrights, or reliance on R&D to bring new products to market quickly.)
- How will your company fight technological obsolescence? (e.g. search for new or pending patents to deter impending competition, maintain rapid development and technical leadership to increase market share and decrease production costs).
- Does your company have the management information systems to cope with the demands of a technology enterprise? (The company must keep current on rapid changes in competition, markets, prices, production costs, and its cash position.)
- How well will your company meet its personnel needs? (Through its hiring, training, and other personnel practices, the company must demonstrate confidence in its ability to recruit and retain qualified people.)
- Will your company have the cash to survive rapid growth? (Small technology companies face a compressed life cycle, rapid growth, and the need for continual innovation (R&D), creating a crucial need for financial and cash-flow projections that are updated on a regular basis.)

Manufacturing

Manufacturers usually meet customer needs by converting various inputs (raw material, labor, equipment, etc.) into inventory. Therefore, the following questions should be answered in the business plan of a manufacturing concern:

- Will manufacturing be outsourced to a turnkey vendor? Who will perform the final testing and assembly of the product?
- When and how many units of output will your company ship? (Provide at least quarterly forecasts.)
- What is the company's inventory policy? (i.e., is EOQ used? What basis is used for establishing inventory levels?)
- When and how much will the company produce? (Provide at least quarterly forecasts that reconcile to shipping and inventory projections.)
- What is the company's raw materials outlook? (List suppliers, terms, advantages, disadvantages, product, and anticipated changes.)
- How does the company's physical plant relate to the production schedule? (For each location, list uses, current value, any applicable financing, layout, advantages/ disadvantages, and anticipated changes. Also include a separate list of idle facilities and plans for them.)
- How does the company's equipment relate to the production schedule? (List major equipment in use/to be acquired, cost, condition, value and any related financing. Also, make a separate list of idle equipment.)
- What is the company's labor outlook? (For each job category, list projected need, expected turnover, personnel availability, compensation and training requirements, and any expected union involvement.)
- For each product/product line, include sales price, direct and indirect costs, and variable and fixed costs to facilitate the determination of profitability and break-even point.
- Do opportunities exist to reduce costs, increase flexibility, or otherwise improve the company's production process?

Service

Service businesses seek profits from opportunities to offer accommodations or professional time. The distinguishing feature of a service business is that its output does not get placed in inventory. The advantage is that a service business can show great flexibility in responding to consumer demands.

The disadvantage is that each opportunity is short-lived. Profit is determined by the cost of providing a given service capacity, price, and consumer utilization of that capacity. The following questions will assist in preparing a service company's business plan:

- How closely does your company's capacity correspond to sales forecasts? (Plot this comparison at least quarterly.)
- What would it cost to change capacity, either temporarily (i.e., to cover seasonal demand fluctuations) or permanently?
- Do opportunities exist for increasing capacity through more intensive use of existing capacity? (e.g., increase hours of operation, increase employee skill level, etc.)
- What is the company's "break-even utilization factor"? - How much of current capacity must be utilized to cover the cost of providing that capacity? - Defined as:

$$\frac{\text{Fixed Capacity Expense}}{\text{Customer Revenue} - \text{Customer Expense}}$$

OR

$$\frac{\text{Cost per Capacity Unit}}{\text{Customer Rev/Unit} - \text{Customer Exp/Unit}}$$

- What is your company's expected utilization factor? (as a ratio)
- Do opportunities exist for increasing your company's utilization factor? (This usually means using existing capacity to provide new/different services.)
- Does your company's pricing policy maximize profit? (e.g., raise prices to meet seasonal demand increases.)

Retail

A retail operation depends on attracting customers to buy goods/services that are usually produced or offered by other companies. The following questions will help to address certain demands specific to retailers:

- How does the location of your store(s) suit your company's overall strategy? (For each location, note advantages/ disadvantages including traffic patterns, parking, character of locale, floor space, appearance, cost, etc.)
- How well does your company's image support its business strategy? (Make sure that location, merchandise quality, manner of display, service, credit policy, and pricing are consistent with each other and the overall business strategy.)
- What pricing policies will your business follow? (Must be consistent with strategy.)
- What will be the policy on customer service? (List the services competitors provide and the related costs. Determine what services are necessary to compete in your market. Then list the related cost of customer services to be provided and determine consistency with strategy and reasonableness of expected costs.)
- How will your business approach advertising? (Indicate form of advertising, expected results, and cost. Compare with competitors.)
- What is the company's inventory policy? (i.e., is EOQ used? What basis is used for establishing inventory levels? How are goods to be purchased determined since they must match strategy and customer tastes/demand?)
- How adequate are the company's sources of supply? (For each supplier, list name and location, product, prices, discounts and credit terms, advantages/disadvantages, and anticipated changes.)

Exporting

Selling abroad may require modifications to your market research, product, pricing, and promotion. The choice of distribution method (indirect vs. direct) is very important and involves different costs and benefits. Answering the following questions will help to incorporate information specific to exporting into your business plan:

- Which of your company's products are most suitable for exporting? Are modifications to the product necessary before it meets foreign standards, preferences, etc.? Does the product have little or no direct competition in foreign markets?
- How much control do you want over the marketing of your company's product in foreign markets? (Indirect selling leaves exporters with less control over pricing, advertising, and other marketing matters than direct selling. Exporters usually want more control over the marketing of new products.)
- How much will your company's export operation cost? (Although it reduces the amount of control over the selling of product by an exporter, using indirect selling also reduces costs by eliminating direct selling costs like overseas personnel, market research, packaging, shipping, etc.)
- How will you price your company's products in export markets? ("Marginal cost" pricing is most realistic - this method sets the direct costs of producing and selling an export as a floor under which prices cannot be set without incurring a loss. This floor should take into account costs for export personnel, market research, credit checks, shipping, insurance, etc.)

Supplemental material

To strengthen your case with outside investors, the following documents may be included — as appropriate — in appendices to the business plan:

- Market analysis data
- Exhibits outlining expected timing of product development, hiring or other significant corporate events
- Product specifications, photographs, brochures
- Samples of advertisement
- Organization chart and list of job responsibilities
- Detailed resumes or biographical sketches of owners and managers
- Personal financial statements, tax returns, and credit reports of owners
- Copies of contractual agreements
- Commitment letters from major customers, suppliers, and lenders
- References (either letters or contact names) from lawyers, accountants, suppliers, and banks
- Credit reports