Introduction to Entrepreneurship and Innovation

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CHAPTER 6

Writing a business plan

What is a business plan

Business Plan

- A Business Plan is a written narrative typically 25 to 35 pages long that describe what a new business wants to accomplish and how

It is a Dual-Use Document

- For most new ventures, the business plan is a dual-purpose document used both inside and outside the firm
- It is the last activity in the second step of the entrepreneurial process "developing a business idea".
- It should contain enough details to convince the reader, which is mostly gathered during feasibility analysis

Reasons for writing a business plan

writing a business plan forces a firm's founders to systematically think through each aspect of their venture

writing a business plan help in creating a selling document for a company, and presenting the venture to investors, suppliers, partners, and key job candidates

Who reads the business plan

- there are two primary audiences for a firm's business plan

Audience	What They are Looking For
A Firm's Employees	A clearly written business plan helps the employees of a firm operate in sync and move forward in a consistent and purposeful manner. Although it's true that marketplaces can and often do change rapidly, the process of writing the plan may be as valuable as the plan itself
Investors and other external stakeholders	**A firm's business plan must make the case that the firm is a good use of an investor's funds or the attention of others. The plan should be realistic and not overconfident**

Red flags in business plans

Red flags	Explanation
Founders with none of their own money at risk	*If the founders aren't willing to put their own money at risk, why should anyone else?*
A poorly cited plan	*A plan should be built on hard evidence and sound research, not guesswork. Sources of primary and secondary research should be cited*
Defining the market size too broadly	*A broad market shows that the true target market has not been clearly defined*
Overly aggressive financials	*Many investors skip directly to this part. Poorly reasoned projections or unrealistically optimistic ones lose credibility*
Sloppiness in any area	*Balance sheets should balance, and there shouldn't be language mistakes*

Guidelines for Writing a Business Plan

Structure of the Business Plan

- To make the best impression a business plan **should follow a conventional structure**, such as the outline for the business plan shown in the chapter.
- Although some entrepreneurs want to demonstrate creativity, *departing from the basic structure of the conventional business plan is usually* **a mistake**.
- Typically, investors are busy people and want a plan where they ***can easily find critical information.***

Structure of the Business Plan… cont.

- **Software Packages**
  - There are many software packages available that employ an interactive, menu-driven approach to assist in the writing of a business plan.
  - Some of these programs are very helpful. However, entrepreneurs should avoid a boilerplate plan that looks as though it came from a “canned” source.
- **Sense of Excitement**
  - Along with facts and figures, a business plan needs to project a sense of anticipation and excitement about the possibilities that surround a new venture.
- It must be long enough to provide sufficient information yet short enough to maintain reader interest.

Guidelines for Writing a Business Plan

Content of the Business Plan

- The business plan should give clear and concise information on all the important aspects of the proposed venture.
- For most plans, 25 to 35 pages is sufficient.
- There are many elements that may be put in a business plan. Each entrepreneur must decide which elements to include in his or her plan.

Recognizing the Elements of the Plan May Change

- It's important to recognize that the plan will usually change while written.
- New insights invariably emerge when an entrepreneur or a team of entrepreneurs immerse themselves in writing the plan and start getting feedback from others.

Types of Business Plans

- There are three types of business plans, which are shown on the next slide.

Summary Business Plan	Full Business Plan	Operational Business Plan
10-15 pages	25-35 pages	40-100 pages
Works best for new ventures in the early stages of development that want to ***"test the waters" to see if investors are interested in their idea***	Works best for new ventures who are at the point where they ***need funding or financing, serves as a blue print for company's operations***	Is meant primarily for an internal audience, works best as ***a tool for creating a blueprint for a new venture's operations and providing guidance to operational managers***

Section 0: Cover letter

A cover letter should include:

- Company's name, address phone number, date, contact information, website, Facebook..
- At the bottom… a reminder of confidentiality
- A table of contents and page numbers of sections and appendices
- Contact information should be included too in the business plan as they could be separated.

A cover letter should accompany a business plan sent to an investor or other stakeholders. The cover letter should briefly introduce the entrepreneur and clearly state why the business plan is being sent to the individual receiving it. if a new venture is looking for funding, a poor strategy is to obtain a list of investors and blindly send the plan to everyone on the list. Instead, each person who receives a copy of the plan should be carefully selected on the basis of being a viable investor candidate.

Section 1: Executive Summary

- The executive summary is a short overview of the entire business plan
- It provides a busy reader with everything that needs to be known about the new venture's distinctive nature.
- An executive summary shouldn't exceed two single -spaced pages.
- Should be written last. The plan itself will evolve as it 's written, so not everything is known at the outset.

Key Insights

- **In many instances an investor will ask for a copy of a firm's executive summary and will ask for a copy of the entire plan only if the executive summary is sufficiently convincing.**
- **The executive summary, then, is arguably the most important section of a business plan.**

Section 2: Industry Analysis

• This section should begin by describing the industry the business will enter in terms of its size, growth rate, and sales projections.

• Items to include in this section:

o Industry size, growth rate, and sales projections

o Industry structure (how concentrated or fragmented)

o Nature of participants (are they innovative or conservative)

o Key success factors (most industries have 6-10 key factors to succeed against competitors … then differentiate in 2-3)

o Industry trends o Long-term prospects

Key Insights:

• Before a business selects a target market it should have a good grasp of its industry—including where its promising areas are and where its points of vulnerability are.

• The industry that a company participates in largely defines the playing field that a firm will participate in.

Section 3: Company Description

• This section begins with a general description of the company.

• Items to include in this section:

o Company description

o Company history (where the idea came from: LuminAid example, TOMS shoes example)

o Mission statement (why do you exist, what do you aspire to do)

o Products and services, positioning

o Current status and milestones o Legal status and ownership o Key partnerships (if any)

Key Insights

• While at first glance this section may seem less important than the others, it is extremely important.

• It demonstrates to your reader that you know how to translate an idea into a business.

Section 4: Market Analysis

Market Analysis

- The market analysis breaks the industry into segments and zeros in on the specific segment (or target market) to which the firm will try to appeal.
- Items to include in this section:
  - Market segmentation and target market selection (new way of segmenting?)
  - Buyer behavior
  - Competitor analysis
  - Annual sales and market share

Key Insights

- **It's important to include a section in the market analysis that deals with the behavior of the consumers in the market.**
- **The more a start-up knows about the consumers in its target market, the more it can tailor its products or services appropriately. (for example who takes decision to buy)**

important

Section 5: The Economics of the Business

The Economics of the Business

- This section addresses the basic logic of how profits are earned in the business and how many units of a business's profits must be sold for the business to "break even" and then start earning a profit.
- Items to include in this section:
    - Revenue drivers
    - **Contribution margins**
    - Fixed and variable **costs**
    - **Operating leverage** and its implications (Microsoft and pharmaceutical companies example)
    - Start-up costs
    - Break-even chart and calculations

Key Insights

- **Two companies in the same industry may make profits in different ways. One may be a high-margin, low-volume business, while the other may be a low-margin, high-volume business. It's important to check to make sure the approach you select is sound.**
- **Computing a break-even analysis is an extremely useful exercise for any proposed or existing business.**

Contribution margin

Amount per unit of sale that's left over and is available to contribute to cover the business's fixed costs and produce profit

Sale: 100$
Costs of goods sold (labor & materials, etc.): 40$
Gross margin (contribution margin): 60$

extra

Operating leverage (affects breakeven point and pricing strategy)

The more operating leverage a company has, the more it has to sell before it can make a profit.

In other words, a company with a high operating leverage must generate a high number of sales to cover high fixed costs, and as these sales increase, so does the profitability of the company.

Conversely, a company with a lower operating leverage will not see a dramatic improvement in profitability with higher volume, because variable costs, or costs that are based on the number of units sold, increase with volume.

extra

$$\text{Operating leverage} = \frac{\text{Fixed costs}}{\text{Total costs}}$$

extra

$$\text{Operating leverage} = \frac{\text{Fixed costs}}{\text{Total costs}}$$

Unit Information

	Low	High
Units	1,000	1,000
Selling price per unit	165.00	165.00
Cost price per unit	135.00	10.00
Contribution per unit	30.00	155.00

Contribution Margin Income Statement

	Low	High
Revenue	165,000	165,000
Variable costs	135,000	10,000
Contribution margin	**30,000**	**155,000**
Fixed costs	12,000	135,000
Operating income	**18,000**	**20,000**

Low operating leverage business

OL = Fixed costs / Total costs

OL = 12,000 / (12,000 + 135,000) = 8.163%

High operating leverage business

OL = Fixed costs / Total costs

OL = 135,000 / (135,000 + 10,000)= 93.103%

Benefits of Low Profit Margins

important

Having a low-margin business is a good way to sell more products or services to more people, or to sell multiple items to the same people.

Cost-conscious consumers are likely to compare your prices to others. If your prices are higher than the competition, you may still make sales with creative marketing, but it's unlikely you'll make the same volume of sales.

Similarly, if you're in a small market, setting low margins on your products may be vital. Suppose, for example, you owned a sandwich shop in a small town. You're more likely to get more returning customers every day selling at a lower price. Selling premium sandwiches at a higher margin may attract the same number of customers, but it's less likely they will return as often than if the price was more affordable.

Benefits of High Margins

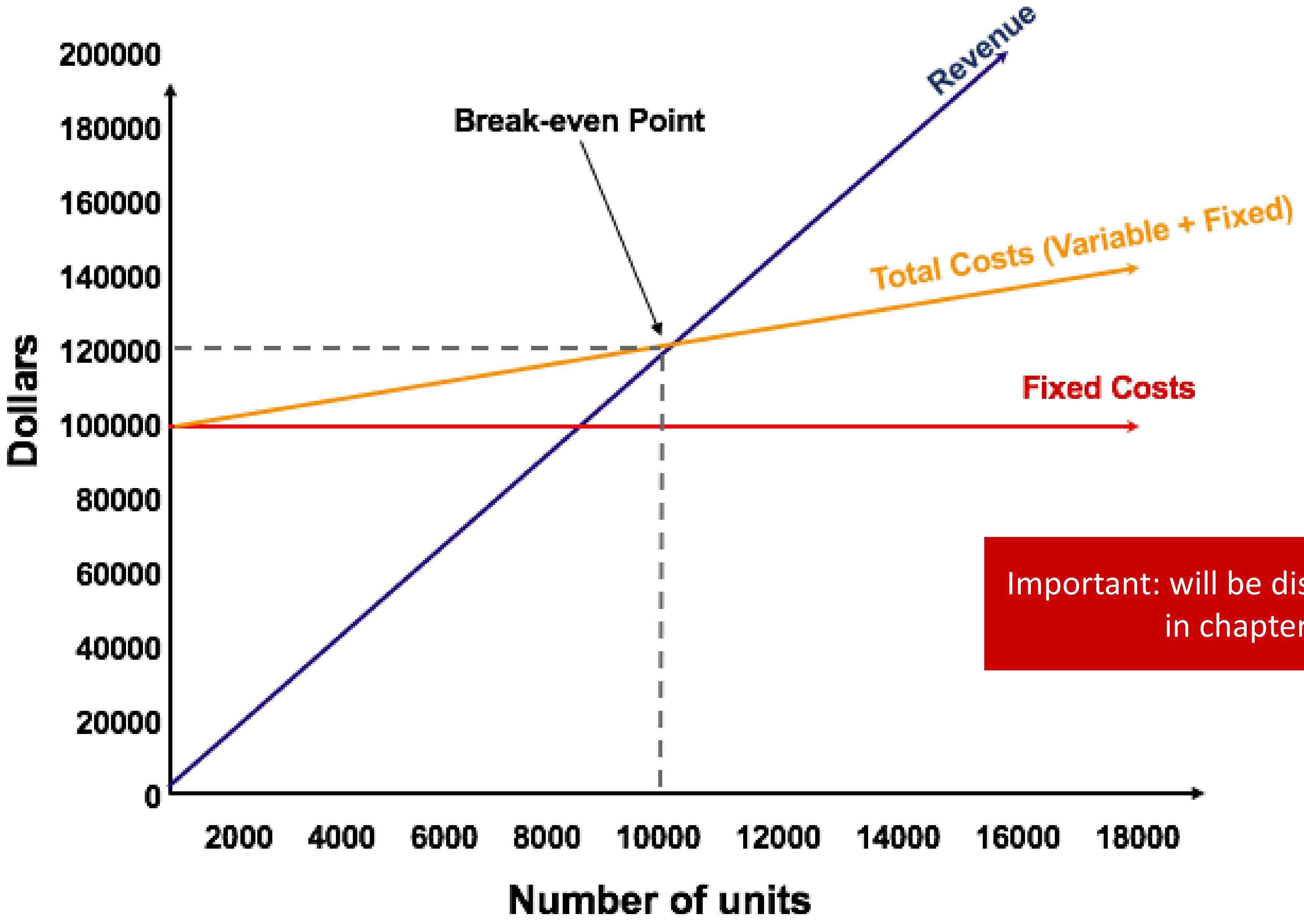
important

The first benefit of high margin goods and services is that you don't have to have a high sales volume in order to make a decent profit at the end of the month.

Looking at the sandwich shop, for example, if you were making a 50-percent margin on premium sandwiches, rather than a 5-percent margin on inexpensive sandwiches, you would only have to sell 10 percent of the number of sandwiches to make the same profit.

As well, if you weren't able to sell them all by the end of the day, the cost of discarding the left-over inventory would be much more manageable. Having left-over inventory of low-margin products can be catastrophic.

In many cases, a high-margin business comes down to the product or service itself. If you're selling luxury items, you should usually price your items at a high margin. Fewer people may be interested in what you're selling, but will be willing to pay a premium to get more than what your competition offers. Scarcity can also result in high margins. This has been the hallmark of many pharmaceutical products, especially when one company has the only medication that can cure a specific disease or ailment. The same can apply to services. If you were the only hairdresser or plumber in a 100-mile vicinity with a full schedule, you could sell your services at a considerable margin. However, in any situation where scarcity is no longer a factor, you will likely need to reduce those margins



Important: will be discussed again in chapter 8

Section 6: Marketing Plan

Marketing Plan

- The marketing plan focuses on how the business will market and sell its product or service.
- Items to include in this section:
    - Overall marketing strategy (positioning & differentiation)
    - Product, price, promotions, and distribution
    - Sales process (or Cycle) and specific Sales tactics

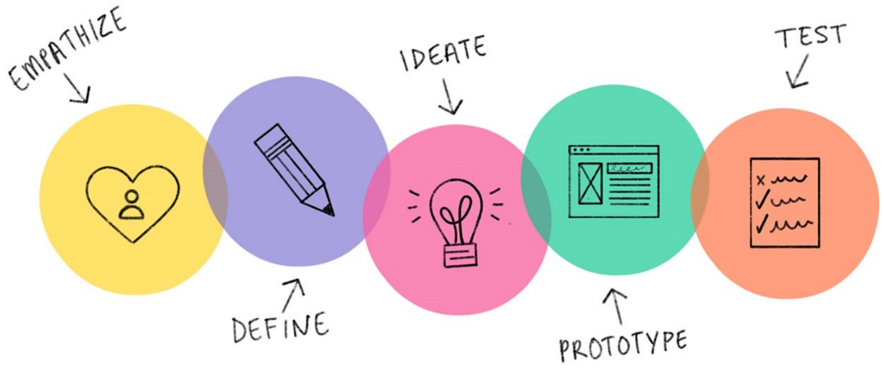
Key Insights

- **The best way to describe a start-up's marketing plan is to start by articulating its marketing strategy, positioning, and points of differentiation, and then talk about how these overall aspects of the plan will be supported by price, promotional mix, and distribution strategy.**
- **It's also important to discuss the company sales process.**

Section 7: Design and Development Plan

Product or Service Design and Development Plan

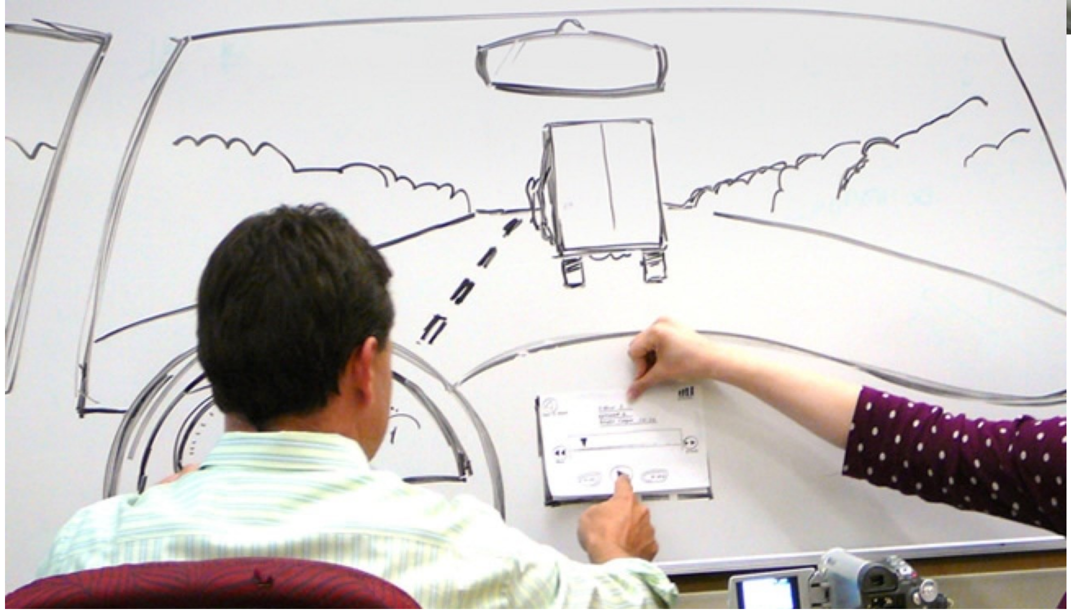
- If you’re developing a completely new product or service, you need to include a section in your business plan that focuses on the status of your development efforts.
- Items to include in this section:
    - Development status (current stage) and tasks (product prototype & virtual prototype)
    - Challenges and risks
    - Projected development costs
    - Proprietary issues (patents, trademarks, copyrights, licenses, brand names)

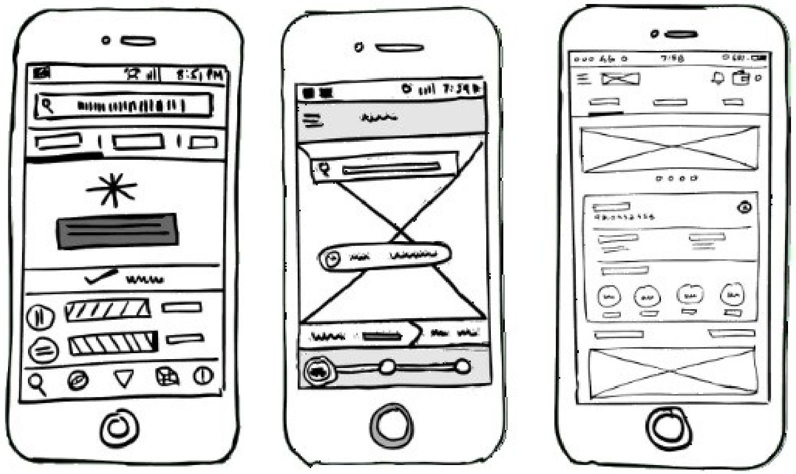


Key Insights

- **Many seemingly promising start-ups never get off the ground because their product development efforts stall or the actual development of the product or service turns out to be more difficult than thought.**

- **As a result, this is a very important section for businesses developing a completely new product or service.**





Section 8: Operations Plan

Operations Plan

- Outlines how your business will be run and how your product or service will be produced.
- A useful way to illustrate how your business will be run is to describe it in terms of "back stage" (unseen to the customer) and "front stage" (seen by the customer) activities.
- Items to include in this section:
    - General approach to operations
    - Business location
    - Facilities and equipment

Key Insights

- **Your have to strike a careful balance between adequately describing this topic and providing too much detail.**
- **As a result, it is best to keep this section short and crisp.**

Example: fitness center

Important: understanding front stage and backstage activities

Back Stage (Behind the Scenes Activities)	Front Stage (What the Members See)
• Staff selection	• Member tours
• Operations manual	• Operating hours
• Relationships with suppliers	• Staff assistance
• Relationships with city government	• Fitness classes and programs
• Development of marketing materials	• Fitness machines
• Employee orientation and training	• Workshops
• Emergency plans	• Monthly newsletter

Section 9: Management Team and Company Structure

Management Team and Company Structure

- The management team of a new venture typically consists of the founder or founders and a handful of key management personnel.
- Items to include in this section:
  - Management team (title, duties, responsibilities, previous experience & education)
  - Board of directors
  - Board of advisers
  - Company structure (organizational chart)

Key Insights

- **This is a critical section of a business plan.**
- **Many investors and others who read the business plan look first at the executive summary and then go directly to the management team section to assess the strength of the people starting the firm.**

Section 10: Overall Schedule

Overall Schedule

- A schedule should be prepared that shows the major events required to launch the business.
- The schedule should be in the format of milestones critical to the business's success.

Noteworthy or significant event

- Examples of milestones:
  - Incorporating the venture
  - Completion of prototypes
  - Rental of facilities
  - Obtaining critical financing
  - Starting production
  - Obtaining the first sale

Key Insights

- **An effectively prepared and presented schedule can be extremely helpful in convincing potential investors that the management team is aware of what needs to take place to launch the venture and has a plan in place to get there.**

Section 11: Financial Projections

Financial Projections

- The final section of a business plan presents a firm’s pro forma (or projected) financial projections.
- Items to include in this section:
  - Sources and uses of funds statement
  - Assumptions sheet
  - Pro forma income statements
  - Pro forma balance sheets
  - Pro forma cash flows
  - Ratio analysis

Important: will be discussed in details in chapter 8 and related task

Key Insights

- **Having completed the earlier sections of the plan, its easy to see why the financial projections come last.**
- **They take the plans you’ve developed and express them in financial terms.**

Presenting the Business Plan to Investors

The Oral Presentation

- The first rule in making an oral presentation is to follow directions. If you're told you have 15 minutes, don't talk for more than the allotted time.
- The presentation should be smooth and well-rehearsed.
- The slides should be sharp and not cluttered.

Questions and Feedback to Expect from Investors

- The smart entrepreneur has a good idea of the questions that will be asked and will be prepared for those queries

Presenting the Business Plan to Investors

Recommendation: Twelve PowerPoint Slides to Include in an Investor Presentation

1. Title Slide
2. Problem
3. Solution
4. Opportunity and target market
5. Technology
6. Competition
7. Marketing and sales
8. Management team
9. Financial projections
10. Current status
11. Financing sought
12. Summary

https://www.youtube.com/watch?v=clPPHKIja4o

https://www.youtube.com/watch?v=jYWF64Um7pw

Thank you