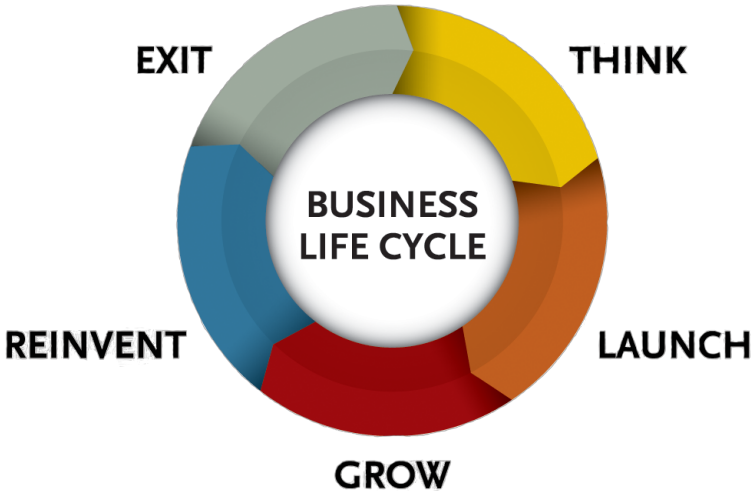
Alaska Small Business Development Center
SBDC UAA Business Enterprise Institute

# Alaska SBDC Tools

## Creating a Business Plan
## Extended Outline

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## What is a Business Plan?

A business plan is a written document describing the current activities of a business setting out its future aims and objectives and how they are to be achieved over a set time period.

A business plan usually contains a written discussion known as the plan narrative and a number-based section also referred to as the financial projections.

## Why create a business plan?

When it comes to success in business there is no substitute for intimate knowledge of the market you serve.

If you need money, you need a formal business plan- this is the entry ticket to the game.

If you don't need any outside capital, you should still want to collect as much knowledge as is available about your market and industry and a business plan is a great way to formalize this process.

## The 10 Questions You Must Answer

**Question #1:** What does the business stand for now and what will it be in the future?

> This question addresses the questions of mission and vision for the business. It should not only address what the business is but also what the business is not.

**Question #2:** What does success look like?

> This is about goal setting. If you don't know what success looks like than you can never find it. Goals should be set for specific timeframes. Ask yourself: "*What do I have to accomplish by the end of this year to achieve my definition of success*".

**Question #3:** What do you make?

> Every business must create value and ultimately make something. This is about the basic value proposition of the business.

**Question #4:** How do you make it?

> This question is about your craft, systems, and way of doing business. It addresses your inputs, processes, and outputs of the business.

**Question #5:** How do you sell it?

> While making something is about the creation of value, this question is about marketing or capturing value. Many entrepreneurs are great at creating value but many fail to capture it by dropping the ball when it comes to marketing execution. As management author Peter Drucker wrote, "There are only two functions of a business: Innovation and Marketing."

**Question #6:** Who are the customers?

This question addresses the people that the business serves. Most successful small businesses operate in turbulent and uncertain markets, catering to small niches of customers that a big business doesn't want to serve. By doing this, they are able to stay off the competitive radar screen of the big companies who can't afford to take huge gambles on such uncertain market segments.

**Question #7** What can your business contribute to the world that no one else can?

This is about the understanding of what your "one big thing" is. It involves a deep passion and understanding of what you can be the best-in-the-world at.

**Question #8:** Who will be the key players in your business?

Who are the people who will operate and grow the business and how will they be organized? This speaks to the organizational structure of the business, as well as its legal structure. Having a great idea is never enough. Great ideas are common- but the people who can successfully implement them are rare.

**Question #9:** How will you make a profit?

At the end of the day, a business must be profitable or it's not a business. You should be well versed in the revenue and cost drivers that make your business profitable. Without profits a company cannot grow and will never be anything more than just a lifestyle business.

**Question #10:** What stands in the way of success and how will you overcome it?

This is about your future story- the enemy and how you will overcome it and ultimately win. Up until now, you have been addressing questions that concern your business model, which is essentially your business in a vacuum. But sooner or later, your business will confront internal forces or external competitors that will potentially keep you from achieving your goals.

Dealing with this reality is, in essence, your strategy.

# Determining Your Audience

## Who's the audience?

The business plan should be tailored for the audience to which the business plan will be presented. Different readers expect to see different things in a plan, so it is extremely important that you put yourself into their shoes before starting the plan.

### Writing the plan for a lender

Lenders are conservative. They need to see collateral to secure the loan and the financial projections you provide need to be very conservative. Also, make sure you break down your loan request into its essential elements. In other words, you should list out how much you need for equipment, inventory, supplies, signage, prepaid expenses, working capital, etc.

The most important thing a banker is looking for (after collateral) is the cash flow of the business. They want to see that your business has enough capacity to repay the loan amount. Your business plan should include these assumptions into the financial projections showing very clearly both the principal and interest payments being made back to the lender.

## Writing the business plan to attract an investor

If you are trying to secure equity, you cannot spend enough time on the executive summary of your business plan. This is the first thing, if not the only thing, that gets read by the equity investor.

The executive summary is your business plan in miniature form. It should contain the scope of the opportunity and the essence of the plan…all in less than a page.

After reading the executive summary and making the decision to read on, equity investors look to one section of the plan more than the rest: the management team. Savvy investors know than an experienced and well-rounded management team can make all the difference when it comes to success of the business. Your management team section should be very comprehensive, citing the background, education, experience, skill-sets, and responsibilities for every member of the team. Also, you should include all the outside professionals that you will utilize, such as your attorney, accountant, management consultants, etc.

Even well-put together plans can flounder because they fail to appreciate the crucial difference between entrepreneurs and investors. Entrepreneurs focus on the potential of an idea; investors focus on its risks. The key to raising capital is therefore lowering risk, not hyping the upside. The entrepreneurs who say how they'll reduce risk are the ones getting capital.

Of course, investors in growing companies understand risk is part of the equation, but they want to see evidence that an entrepreneur recognizes the risk factors facing the business and has taken steps to control them. That means addressing questions about market risk, financial risk, and technological risk- stressing not the dazzling upside but the return investors can reasonably expect, weighted against a limited and carefully defined set of risks.

If an investor likes what they see in the management team section, they will usually proceed to the financial projections. Obviously, one of the most important things an investor wants to see is what potential return there might be, weighed against the clearly defined risks. For this, they turn to the projected profits of the business. While your business plan need not discuss the amount of ownership you are willing to give up (that will be negotiated later) it should give the investor some idea of what returns they might receive from their investment in your business.

## Writing the plan for a management team

Writing a business plan for a management team is different than writing a plan for lenders or investors. People in an organization have to understand how a company is supposed to be different and how it creates value compared to its rivals. This can be accomplished through the use of a focused business plan.

The fundamental task for managers is decision-making. Therefore, a business plan tailored to this audience must help them answer the big strategic questions:

- Who are we and what do we stand for?
- What are we not? What are the trade-offs we must make?
- Where are we headed?
- How do we create value differently from rivals?
- What does success look like?

What must we accomplish and by when? How detailed a business plan needs to be with respect to the management strategy and tactics depends on the structure of the business. A business plan is usually used to convey the mission, vision, and goals of a business. There might also be some discussion about the broad strategies employed. But business plans usually don't get down to the small, day-to-day tactics of the business- this is instead the role of a work plan.

The management team should be able to use the completed business plan to develop their own tactics and work plans. On the other hand, it shouldn't try and make decisions for them- that's their role and function. Instead, it should guide them with respect to big picture strategy and goals giving them the autonomy to make decisions and trade-offs as day-to-day issues arise.

## Creating your Mission and Vision

What is the difference between mission and vision? Though the terms are often used interchangeably, there is a vast difference between a mission and a vision. While the two concepts play off one another they work in very different ways. Let's look at how these two terms differ.

### What is your vision?

- A vision is a specific future destination.
- A vision is a dream with a deadline.
- It should change over time.
- It must say "yes" to some ideas and "no" to others.
- It's about what the future might be, could be, and shouldn't be.
    - Example: "To put a man on the moon before the end of the 1960's."
- Vision is about stimulating progress…
    - Urges continual change
    - Impels constant movement
    - Expands possibilities
    - Revolutionary change

To construct your vision, ask yourself… what big, audacious goal(s) do you want to try to achieve five years from now? What does success look like in five years? In five years' time, how should your business be different than it is now?

### What is your mission?

- Mission is about preserving the core
- Provides continuity and stability
- Fixed stake in the ground or the horizon
- Limits possibilities
- Conservative act

To construct your mission, remember… A mission statement should be somewhat timeless. It should apply to not only today but possibly even twenty to fifty years from now. It should put forth a general direction or heading stating what it is that you stand for. In essence, a mission can never really be achieved- it should be ongoing. If it can be achieved and completed, then it is a vision not a mission.

You should think of you mission as your true north heading on your compass.

Using your own metrics of success, what must you accomplish in five years for you to consider yourself successful?

## Setting Goals and Objectives

### What are goals and objectives?

Objectives clarify what it is you are trying to accomplish in specific, measurable goals. For an objective to be effective, it needs to be a well-defined target with quantifiable elements that are measurable. Whereas your vision statement is expansive and idealistic, and the mission short, powerful, and memorable, your objectives are designed to focus your resources on achieving specific results.

The purpose of well-defined objectives is to cause meaningful action. What do you need to accomplish? What targets will you aim for? Most objectives can be broken down into the following general headings:

- Financial
- Marketing and Sales
- Operations
- Human Resources
- Research and Development
- Manufacturing
- Personal

To create a solid objective, you must:

- Describe the activity required.
    - Example: Introduce new products…
- Describe what will happen and when.
    - Example: a book by 6/30 and a CD-ROM by 8/15

You can then wordsmith these pieces into a complete objective:

"Marketing Objective- Introduce a book by June 30th and a CD-ROM by August 15th."

### Developing your goals

Think back to your vision statement once again. If you recall, your vision statement looked five years into the future toward a specific destination. Now, think about the activities you need to accomplish this year in order to move toward that destination. You should create 5-7 objectives that are critical to arriving at your envisioned future.

## The Structure of the Business Plan

### Structuring your plan

There are no required formats for a business plan, and with good reason. There is, however, a fairly common structure that most business plans use as a skeletal framework. In order to provide context to the scope of your business plan, you should identify the time period for which the plan will focus. Be it one year, two years, three or more; this time constraint is necessary in order to provide context or your thinking and decision making.

### The two business plan tests

A business plan is, at heart, a story- a story that explains how a business works. When a business plan doesn't work, it's because it fails either the **narrative test** or the **numbers test**.

- The narrative test asks, "Does the story make sense?"
- The numbers test asks, "Does the story add up?"

A business plan is therefore usually broken down into two sections: A written section typically called the *plan narrative*, and a numbers section typically referred to as the *financial projection*. The financial projection is simply a numerical representation of the business itself, as well as the marketing strategy as it is presented in the plan narrative.

The two sections must be completely entwined.

### The plan narrative

The narrative of a business plan is usually broken down into three major sections:

- Business Description Section
- Market Strategy Section
- Management and Operations Section

### The Business Description Section

This section simply describes attributes about the business itself and should include:

- The Company
    - Company mission (the purpose)

    - Company vision (the big dream with a deadline)
- Business description
    - Current status
    - Future plans
    - The industry
    - Chief characteristics
    - Trends
- Product and service
    - Product and service description
    - Proprietary features
    - Future development plans

## The Market Strategy Section

This section documents all of the activities surround the most important function of your business: Marketing. It addresses the questions of what you sell and how you sell it. The Market Strategy of your plan should include:

- Market Analysis
    - Target market
    - Market trends and growth potential
- Competitive Analysis
    - Competitor profile
    - Market niche and share
    - Comparison of strengths and weaknesses
- Market strategy (cost, differentiation, focus)
    - Pricing strategy
    - Distribution strategy
    - Service and warranty policies
- Promotional strategy
    - Advertising
    - Public Relations
    - Personal Selling
    - Sales Promotions

## The Management and Operations Section

The Management and Operations section of your plan describes who will manage the business and how they will do so. It also describes how you produce the products you sell or the services that you deliver. This section basically details how the day to day operations of the business are conducted. The Management and Operations Section of your plan should include:

- A management team listing including their education, background, and responsibilities
- The ownership structure of the business (sole proprietor, partnership, S corporation, LLC, etc.)
- A strategic partner and supplier discussion

- A human capital and personnel needs discussion
- Insurance and risk management discussion
- A facilities overview

### The Risk Analysis

As a final discussion of your Management and Operations segment, you should demonstrate the risk factors involved. This means addressing questions about market risk, financial risk, management risk, and technological risk. Most audiences who read a business plan want to see evidence than an entrepreneur recognizes the risk factors facing the business and has taken steps to control them.

## The Financial Projections

As stated earlier, the financial projections section of the plan should be thought of as simply quantifying the effects of what was presented in the plan narrative. Although the projections are concerned with the future, don't think of the projections as merely a prediction. Instead, the projections should be thought of as goal-setting with respect to revenues and expenses. We cannot predict the future- this is precisely why planning is necessary- but we can make plans, set expectations, and establish goals. Your projections should include:

- A listing of required funds and their uses
- A sales forecast (at least monthly for the first year and quarterly for additional years)
- A variable cost of sales analysis
- A fixed expense operating budget
- A projected profit and loss statement
- And possibly:
- A projected cash flow statement
- A balance sheet
- A break-even analysis

### Your required funds

You should detail exactly how much money you need to make your plan a reality. Your listing should break these costs down into Fixed Assets and Working Capital.

Fixed assets are properties that usually have some sort of long-term value. Working capital is money that will be used to finance the short-term operations of the business.

### The sales forecast

For your sales forecast don't let the fear of prediction stop you from arriving at a projected revenue figure. Every business sells units of something- whether it be hours, projects, products, services, etc. Simply set goals for the numbers of units you believe you can sell, taking into account any seasonality factors. Finally, multiply these units by your average established prices. The result is your sales forecast in dollars.

Each fundamental assumption that you make needs to be documented in this section since the assumptions themselves can be more important than the final numbers.

### The variable cost analysis

Variable costs are those costs incurred every time a sale is made. They vary with sales. They are the direct costs associated with producing or selling your products and services. Variable costs per unit include:

- The cost of goods themselves (for retailers)
- Any direct labor associated with creating the product
- Any materials that go into the product itself

### The fixed-expense operating budget

Fixed expenses do not vary with sales and are usually tied to some contractual arrangement or indirect cost of doing business such as rent, salaries, loan obligations, insurance, and advertising. You should develop a monthly fixed expense budget for the year detailing these amount and when they occur.

### The profit and loss statement

A profit and loss statement, commonly called the "P&L," combines the revenue, variable cost, and fixed cost amounts in order to see if the business is operating at a profit or at a loss. This statement tries to line up all revenues and expenses to determine the profit potential of the business.

### Industry Aspects and Considerations

**The service industry:** The service industry fundamentally sells units of time or labor. A service is therefore perishable since it is directly linked to time. Excess capacity cannot be stored for later use; it must be used now or forever lost. This is true due to the fact that production and consumption cannot be separated.

Another strategic issue of a service-based business involves the variation in quality that exists through the delivery of the service itself. Unlike a product where the manufacturing processes can be tightly controlled to ensure certain tolerances of quality, a service is based on the hard-to standardize nature of human behavior.

The last major attribute that makes service-based businesses unique is their intangibility- there is little if any physical characteristics to the output. Many marketing professionals call this problem, "selling the invisible." Of course, there are many ways to make a service tangible with a little marketing imagination.

For a service-based business plan you need to focus heavily on the following three issues:

- How do you minimize the problem of excess capacity and perishability? What staffing levels do you need to deliver your service, and what is their maximum delivery capacity?
- What processes will you use to minimize service variations and maximize service quality levels?
- How will you market your service effectively since it can't be pictured in an advertisement or displayed in a store? What tangible cues will you use?

**The retail industry:** A retailer is an organization that purchases products for the purpose of reselling them ultimately to consumers.

Location may be the single most important factor in the consideration of what makes a successful retail business. As they say in the retail industry: Location, Location, Location. A business plan for a retail business must contain a thorough location analysis covering such issues as selling square footage, access, visibility, signage, costs, renovations, lease terms, traffic counts, area demographics, and so forth.

Emergence of new types of stores and expansion of product offerings by traditional stores has intensified retailing competition. Retail positioning involves identifying an underserved market niche and serving the segment through a strategy that distinguishes the retailer from others in the mind of the consumer. A retail business plan should discuss its positioning strategy in the marketplace.

Store image refers to the physical elements in a store's design that appeal to consumers' emotions and encourage buying. Merchandising refers to the inventory mix a store will provide and how it is displayed out across the store's floor plan. The marketing section of a retail plan needs to discuss both the image and merchandising strategies that will be employed.

The last critical consideration a retail business plan should address is the inventory requirements. You should detail how much inventory you have or will require at cost and in retail dollars. The retail industry usually works on several key inventory metrics including sales per square foot and inventory turns- which is the number of times the inventory walks off the shelf in a year. You should be aware of such metrics and present them in your business plan. Most trade associations collect and report such data.

**The manufacturing industry:** A supply chain is all the organizations that are responsible for bringing your products to market. A supply chain might be shallow say when a supplier sells raw material to a manufacturer which then sells direct to a consumer. Or it may be deep say when a sub-supplier provides a prime supplier with parts who then sells to a manufacturer to a wholesaler/distributor, to a retailer and so on. Your business plan should discuss in detail your supply-chain and ant coordination and communication issues related to its management.

The competitive environment in manufacturing has made high product quality essential to success. You should discuss any quality processes, programs, or certifications that you have or require in order to successfully compete in the global market place.

With regard to materials and labor you should present a discussion in your plan about its supply and availability as well as how the costs will be controlled. You should also present some details about what margins you are expecting, which is the calculation of taking price minus the cost of producing your product.

How you sell your products and take them to market is obviously as important as how you make them. Don't skimp on the marketing section and present only product production and manufacturing processes. Your discussion should include your sales and distribution strategy through such channels as sales agents, sales representatives, direct marketing tactics, distributors, or retailers. Make sure your plan discusses the pricing expectations that each channel member expects to realize as it moves from your business toward the consumer.

## The Most Common Business Planning Mistakes

**Mistake #1:** Not Disclosing Weaknesses

> It's a difficult aspect of writing a good business plan, but dealing with problems, obstacles, weaknesses is part of the planning function. Every business has weaknesses without exception and savvy investors do their due diligence in seeking these out. The best way of handing such issues is to just get them out in the open and to have a detailed action plan that effectively addresses these problems.

**Mistake #2:** No Distribution Strategy

> How your business takes its product and services to market is one of the most fundamentally important questions your business plan addresses. At all costs, resist the temptation to cover all bases by listing every possible channel possibility.
>
> Business planning consultant Daniel McGilvery says most business plans read something like: "We will market our products via internet, catalogs, distributors, value-added resellers, infomercials, wholesalers, direct mail, agents, direct field sales, telemarketing, retail outlets, and smoke signals in selected areas."
>
> What this tells the investor is that you really don't have a distribution strategy

**Mistake #3:** Lack of integration

> Many entrepreneurs make the mistake of not integrating the narrative with the numbers. For instance, if you site in your marketing plan the advertising media you plan to use and its associated costs and scheduling, this should show up in the exact same way in the financial projections. Another example: Stating in the plan narrative that you need a loan in the amount of $100,000 yet there are no loan payments being made in the financial statements.

**Mistake #4:** Competitive Analysis

The key word here is "analysis." Listing the name and address of your competitors is NOT an analysis. An investor is interested in knowing such things as:

- What you expect to see from your competitors near tern and long term.
- What is their strategic direction, their core competencies, and what makes them tick.
- Why do customers buy from them?
- How good are their marketing and sales efforts?
- What is their funding position?
- What are their weaknesses and how can they be exploited?

Failing to take your competitors seriously only hurts you and your business. Remember every business has competition- whether it is direct or indirect. Show a healthy respect for the incumbents while demonstrating a compelling and believable way to compete with them. If you downplay the competition or state that you have no competition it either means that there's no market or you don't know how to use a search engine.

**Mistake #5:** Failing to Address Risks

An entrepreneur likes to hype the upside while an investor likes to evaluate risk versus reward. If you need to raise outside capital you may need to subdue your visions of grandeur without boundaries and instead concentrate on the external future risks that could prevent your plan from being successful.

A clear analysis looking at market, financial, management, and technological risk and any action plans you have for overcoming these obstacles works best.

**Mistake #6:** Legal Problems

Savvy investors are always on the lookout for potential legal snags your plan may have such as:

- Was the product developed while you were employed somewhere else?
- Are there any employment contracts or non-compete agreements?
- Is there any possible patent or trademark infringement?
- Is there clear ownership of your product or service?

Full-disclosure of any of these issues is a must to avoid larger problems later on. See an attorney if you need advice on any such issues.

**Mistake #7:** No Sales Assumptions

Business plans that simply state a projected sales number without detailing the precise assumptions made to arrive at the forecasted sales levels are useless to investors. The assumptions themselves are often more useful than the final sales number anyway because

they break down the drivers of the company's revenue model. You should be able to provide some rationale for how your projections were put together. Chances are an investor will expect more than just your "best guess."

**Mistake #8:** Unrealistic Profitability

Lenders and investors usually have a number of companies that they fund in their portfolios. Here's a secret: A good majority of these companies are NOT wildly profitable. (In fact, many are losing money) It's hard to pull the wool over an investor's eyes about the profitability you put forth in your projections. They know the cold, hard reality of the competitive business landscape.

You should also know that most lenders subscribe to information services that summarize financial statement data that tells them the actual profitability of businesses in your industry.

In order to avoid this mistake, it pays to once again do your homework. Financial statement studies such as those produced by Dun & Bradstreet and RMA Financial Statement Studies can be found at your local library usually at the reference desk. Use this date and compare it to your projected financial statements. Know what the numbers say and be prepared to answer any questions about why your number may vary from those companies found in your industry.

**Mistake #9:** No Target Market

Most small businesses cannot afford to market to the general mass consumer and/or industrial markets- resources are just too limited. Failing to identify a particular customer niche that is being sought is therefore a major mistake many business plans make. Not only should the target market(s) be identified in your plan, but market research has to be included to demonstrate how this market segment has been identified.

**Mistake #10:** Over-diversification

Entrepreneurs get excited about their ideas and see numerous opportunities for marketing them. But you should try to focus the attention of the plan on one main opportunity for the venture.

A new or early-stage business should not attempt to create multiple markets nor pursue multiple ventures until it has successfully developed one main strength. Plans that present endless opportunities without focusing on any one of them just don't get funded.

***Cheat Sheet gathered from Small Biz U 2013***