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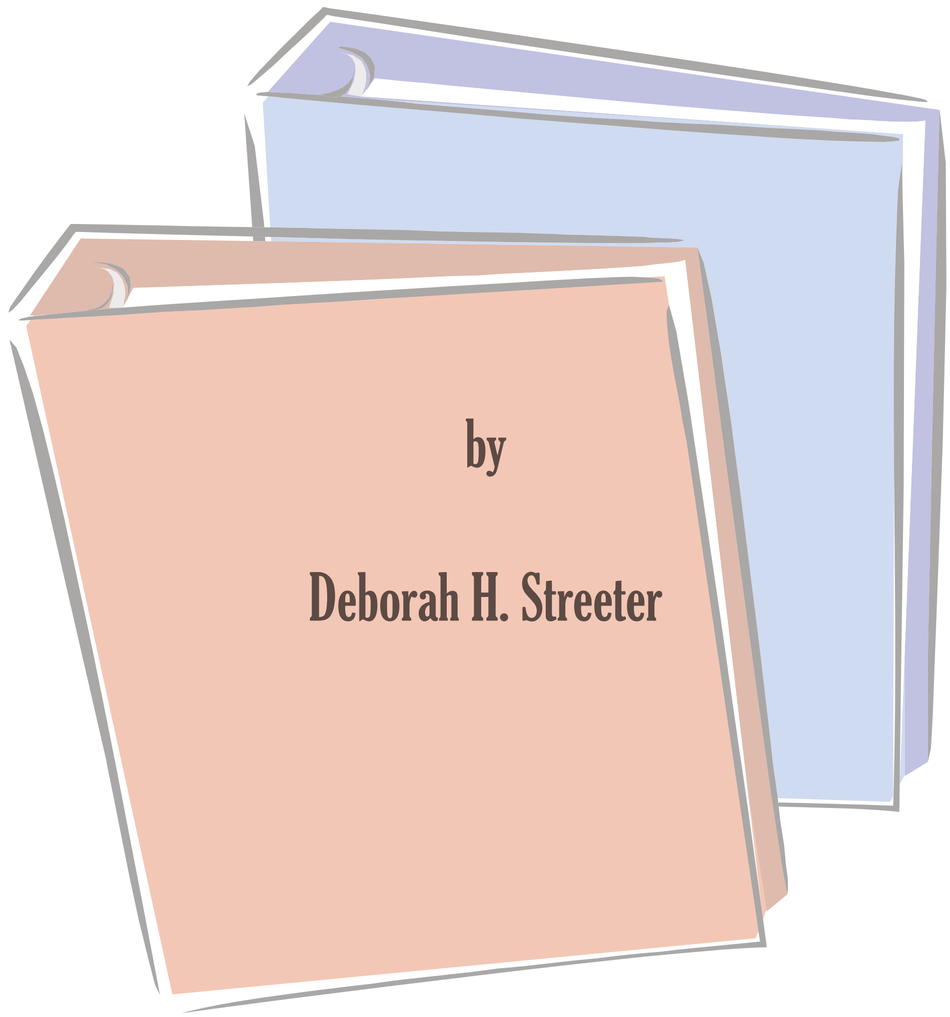
PRODUCING A BUSINESS PLAN FOR VALUE-ADDED AGRICULTURE



by

Deborah H. Streeter

Department of Applied Economics and Management
College of Agriculture and Life Sciences
Cornell University
Ithaca, NY 14853-7801

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For additional copies, contact:

Deborah Streeter
Dept. of Applied Economics and Management
Warren Hall
Cornell University
Ithaca, NY 14853-7801

E-mail: dhs4@cornell.edu
FAX: 607-255-9330
Phone: 607-255-1611

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Issue #1: Introduction to Business Planning (or... It's Not About the Plan)

This Issue introduces the basic concept of planning as a process, not simply a document. It provides background for the other sections and explains how the publication will provide guidance to ag- and food-based entrepreneurs who are thinking about starting a value-added business.

The Ag- and Food-Based Angle on Business Planning

How is business planning different for people starting or running a food- or ag-based enterprise compared with other sectors? Many ag- or food-based businesses are derived from an existing farm operation or are started by someone connected to farming. That means that the entrepreneur may be more accustomed to focusing on production rather than marketing. After all, when selling a commodity like corn or wheat, the farmer is what economists call a "price taker" not a "price maker."

By contrast, when planning a new business that is centered on value-added products or services, knowing the marketplace is crucial.

Nobody Likes to Plan

For most people starting or running a business, writing a business plan does not come naturally. In fact, if you come right down to it, most entrepreneurs would rather just get on with starting the business. The optimism and drive of the entrepreneurial personality often pushes entrepreneurs quickly past the planning stage and into action. But most entrepreneurs who charged ahead (sometimes called "fire, ready, AIM!) admit that they paid a price for not doing more planning up front.

So don't be surprised if you have been procrastinating about writing your business plan; you're only human! In my experience, there are several things that are barriers to good planning. The first is time. Many entrepreneurs are trying to start a business while working full time at some other activity. The second barrier is psychological in nature. Without a clear idea of what a business plan should be, many entrepreneurs experience a sort of paralysis. The task, which suddenly seems to resemble a hated homework assignment from high school or college days, appears too large. Questions loom, such as:

- Just what is required?
- Do I have the special skills to write a plan?
- How long should it be?
- Should I pay someone to do it?

Using This Publication to Get Started

My goal with this series on business planning is to demystify business planning. I want to change your concept of just what constitutes a business plan. A plan is NOT just a document: it is a state of mind. In fact, it is virtually impossible to write a good plan unless you have been doing the right kind of thinking. So, the number one thing to accept is that even if you never put pen to paper, you can benefit by learning how to research and reason through a plan for your business. Start thinking about planning itself, rather than "the plan" or document.

A "mental plan" can be developed by thinking through the main aspects of the business idea, including articulating clearly the reason you are going into the business, who will lead the company, what the key advantages of the product/service are, how the business meets a crucial market need, and how you will execute the business and marketing strategies. In addition, this series outlines steps for thinking through how you will make money, asking yourself questions like:

- About how big is the market for the product/service?
- What are the primary sources of revenue?
- What are the largest expenses?
- Why will the business be profitable?
- Are there any important cash flow issues?

What Matters in Planning

Even in the most informal conversations with people involved in the business (your family, your partners, your funding source) you must be able to articulate your business strategy, explain how you will make money and pitch what is called the "value proposition" of your business -- that is, why customers will want to buy from you. Even entrepreneurs who managed to start a successful business without a written plan tell me that they did have a "mental plan."

A business plan is sometimes simply an internal document used by the business owner to envision the future and plan how to get there. In that case, a series of pages with handwritten bullets may be enough. On the other hand, if a business owner plans to approach others for funding (sometimes called OPM -- "other people's money"), a more formal plan will probably be necessary. However, even if you do need the document itself, a good business plan is very short (usually about 15 pages or less), focused, and concise. What is on the pages doesn't matter as much as the research and strategizing that is behind the work.

This publication will help you stay focused on the most important aspects of the business when writing up your concept and business model. The plan should be easy to read and nicely presented. Later sections will have more details on how to assemble the document and maximize the chance that it will be read and understood.

Overview of a Written Plan

Let's begin with an overview of what a written plan will look like. First, it is important to remember that a good plan is SHORT. Also, you will not be writing it in order (from beginning to end) but rather will be working on different parts of it and then assembling it.

When completed, a good, well-written plan is about 15-20 pages (without appendices). It begins with a ONE-page executive summary, in which you boil your plan down to an "elevator pitch," including:

- Information on why your management team is the right one to make this business succeed;
- Succinct proof that the market wants/needs the service/product;
- A clear explanation of your competitive advantage and how you will sustain it over time; and
- A brief summary of the economics of the business (story of how you make profits, how much capital you need, how it will be used and what are the important milestones).

The body of the plan expands on each of these points. The appendices to the plan include a full set of financials and any important additional materials essential to the plan (such as detailed information on market research, patents, drawings or descriptions helpful to the narrative).

Stepping back from the document, the process that leads up to the information in the business plan is:

- Thinking through some strategic questions:
  - ◊ Why do I want to go into this business?
  - ◊ What do I have to offer the business?
- Investigating and understanding the marketplace;
- Outlining and piloting the key operational aspects of the business;
- Assembling a team; and
- Working the numbers.

Even if you never put a pen to paper, you'll need to do these five things. Failure to do them is almost always expensive and risky. This publication offers advice on each part of the process. The results may end up as sections of a written business plan or remain simply part of your "mental plan" as the leader and visionary of your company, but the process will surely help you understand the key success factors and the risk factors you face starting a new business.

Frequently Asked Questions

Q: Should I have someone else write my plan?

A: There is no simple answer to this question. Getting professional business planning advice and writing assistance can be advantageous. However, having someone write your plan is not likely to lead to success unless you are heavily involved at every step along the way. You, the owner, are the only one who can do the heavy lifting in terms of defining your mission, choosing your business and marketing strategies, and shaping the focus and scope of the business. You can pay someone to do research or writing, but you cannot outsource the process.

There are many resources available to help with writing your business plan. For example, if you go to the website for BizPlanit.com (http://bizplanit.com), you will see a variety of services offered, ranging from developing a summarized business plan (simplified presentation of vision and business concept) to fully developed plans intended for private equity investors. Or, you can go through a referral service to find an individual to help you (for example, visit The Consultant Exchange at http://www.cx.com). There are also public sector entities (such as the Small Business Development Centers and courses through local community colleges) that can guide your work.

If you decide to hire a consultant be sure to:

- Ask for examples of previously written work:
  - ◊ How appropriate is the tone?
  - ◊ Is the document easy to navigate?
  - ◊ Is the writing, clear, concise and professional?
- Talk to others who have used the consultant:
  - ◊ Was the work done in a timely fashion?
  - ◊ Did the consultant focus on the needs of the business owner?
  - ◊ Did the final plan achieve the desired goal?
- Be very clear on deadlines and impose penalties for delays.
- Find out how they carry out additional needed research.
- Be sure the consultant understands your vision.
- Ask for several versions of the plan (pitch book, PowerPoint presentation, written plan).
- Reserve the right to proof and revise the plan.

Q: Is it okay to use Business Planning Software to write my plan?

A: The short answer is that if it helps you get started, then yes. This is especially true if your plan is intended primarily for internal purposes. Many software packages step you through a series of questions intended to help you think through the planning process. The program uses the answers to produce a written document. However, if the plan is to be used in seeking external funding, be aware that those in the investment community can easily spot a plan built on a template and it will have less credibility.

The best approach may be to build a rough draft with software and then carefully examine how well the template fits your individual case. You may be missing sections that are important to your business model. For example, if your business has a special relationship (on the input or output side) with an existing farm business, a standard template may not have an effective approach to discussing the relationship. The order of the presentation may not be appropriate for your audience, or there may be superfluous sections. A template, by nature, cannot anticipate your individual circumstances.

One place a business planning template can be extremely helpful is in creating your financials. The interlinked spreadsheets reflect the built-in relationships that must be coordinated in the way the business operates financially. However, you still have to build the financials "from the bottom up." Before entering information into standardized cells, you'll have to research and estimate many basic costs. If your business/service is related to a current farm operation, you may also need to adapt to reflect the way farm accounting differs from standardized small business accounting.

Getting Started

- Decide whether you need a written business plan or whether a "mental plan" will be adequate for current decision-making.
- Inventory what you already know and collect and organize any material or information that you currently have.
- Find out what help is available in your area (check local credit unions, SBDC offices, community colleges, private consultants).
- Choose some short-term goals and deadlines.

Common Mistakes

Entrepreneurs often:

- Spend too much time and money on a fancy document rather than investing in the work behind it.
- Decide that business planning is not needed because the markeplace moves too fast.
- Become wedded to the written document.
- Fail to edit and proof the written plan until it is short, concise, and error free.
- Think that the financials in and of themselves are the plan.
- Allow lawyers or accountants to provide strategic business advice outside their areas of expertise.

Additional Resources

There are so many resources (books, websites, brochures, government publications) on business planning it is easy to get overwhelmed. In this series, we will provide you with just a few selected resources on each topic, along with comments that explain why we find it useful. If you want to browse a collection of resources that address various issues of importance to agricultural entrepreneurs, there is an annotated list featured on Cornell's Entrepreneurship Education and Outreach site: http://eeo.aem.cornell.edu. Below I comment on some of my favorite general resources.

General Business Planning Tools

- **Small Business Administration website**
  http://www.sba.gov
  This is one of the best sources for free advice on small business planning. Included are many free spreadsheets, worksheets, and factsheets covering all aspects of starting a business. Although the materials, worksheets, and resources are not specifically

focused on agriculture, the tools found on this site have been widely used by entrepreneurs and are sound in terms of the focus and approach (note: this is not true of everything you will find on the internet about business planning!).

- **BizPlanIt**
  http://bizplanit.com
  The section labeled "virtual bizplan" on this site is an excellent guide on what to include in every section of your business plan. The straightforward explanations are accompanied by lists of common mistakes to avoid and section-specific tips.

- **SmallBiz.cornell.edu**
  http://www.smallbiz.cornell.edu
  This site provides guidance to small business resources available at Cornell University.

Specifically Related to Ag- and Food-Based Enterprises

- **Agriculture Innovation Center**
  http://www.aginnovationcenter.org
  Created by the Missouri State Department of Agriculture, this website has a wide variety of resources, including a list of possible value-added products. For each type of product, a description is provided, along with an extensive list of resources related specifically to that particular market niche.

- **"Tilling the Soil of Opportunities"**
  NxLeveL Training Network, University of Colorado. 1999.
  This course for agricultural entrepreneurs is aimed at individuals who have started or are thinking about starting an agricultural-based venture that is not tied to large-scale, commodity production. Session topics include:
  - ◊ Take Stock of Your Resources
  - ◊ Basic Equipment Required: Planning and Research
  - ◊ The Legal Terrain
  - ◊ Manage from the Ground Up
  - ◊ Plant It, Grow It, MARKET It!
  - ◊ Reap the Benefits-Marketing Strategies
  - ◊ Get Your Budgets In Line
  - ◊ Analyze THESE: Cash Flow and Financial Statements
  - ◊ Cultivate Your Money Resources
  - ◊ Harvest Your Future

  For information about this course, contact http://www.nxlevel.org/.

- **Ag Innovation News**
  http://www.auri.org/news/aginnews.htm
  Ag Innovation News is a newsletter published by Minnesota's Agricultural Utilization Research Institute (AURI) to inform the food, agriculture and business communities and the general public about developments in new ag-based products.

SECTION 2 - HOMEWORK FOR BUSINESS PLANNING

Issue #2: Know Why You are in Business - Mission Drives Strategy

This section explains the art of crafting a mission statement, including practical steps on how to get started and examples of various approaches. The focus is on explaining why defining mission is an important first step in planning and how different missions might lead to different strategy options in a business.

The Ag- and Food-Based Angle on Mission Statements

Many entrepreneurs in ag- and food-based businesses have ties to a farm business. The interlinkages between the businesses make it all the more important to be clear on your mission. Is the business secondary to the farm? Or is the intent to phase out of farming and move into the value-added business on a full-time basis? Does the mission of the business include continuing to keep ties to agriculture? Or would it be fine to eventually have a business that essentially buys raw inputs rather than producing them? Farm families are familiar with the creative tensions between lifestyle considerations (such as raising a family in a rural environment with animals and crop activities) and profit goals. So defining a mission statement will be especially important, if especially challenging, for ag- and food-based business owners.

How to Do It: Crafting a Mission Statement -- It's an Art, not a Science

Writing a mission statement for your business might seem like a step that is too formal or academic, but as with many parts of the business plan, it is the process, not the product, that matters. Here are some steps to get you started:

1. **Do the initial thinking.** Even if you never come up with a polished mission statement that you want to put up on your web page., you should try to answer the following questions at the beginning of your business and revisit them on a regular basis:
   - Why are you in business?
   - What basic beliefs or values drive the business?
   - What are the basic products and services?
   - Who is the target customer?
   - How do you add value?
   - What public image do you desire?

2. **Check out some examples.** If you are feeling writer's block, consider some mission statements of other companies in your industry or other companies that you aspire to be like. See examples that follow.

3. **Work with the management team (and employees, if feasible) to come up with at least 3-5 possible statements (more is better).** There is nothing quite as powerful as sitting down with some examples to elicit opinions and get the discussion moving. You will probably be able to eliminate at least one or more immediately, and that will help you narrow the choices and get focused.

4. **Live with it for a while.** Once you narrow it down, before you print a thousand business cards, try the mission statement on for a few

weeks or months. See whether it informs or confuses your customers, suppliers and employees. Then adapt and evolve it until it feels just right.

5. **Use it to guide your strategy.** The mission statement should:
   - Reflect the company's personality and core values;
   - Be simple and concise;
   - Sound exciting, and inspiring - a statement of your business' reason for being.

Unfortunately, there is no magic formula for writing a mission statement. On the other hand, that also means you have a lot of flexibility in writing one that fits you and your business.

Mistakes to Avoid

- **Paralysis (writer's block).** Just start writing. Start with bulleted answers to the questions listed in the "how-to" section. Get others involved in writing various versions. To encourage creativity, don't start judging the statements until you have generated enough to generate a good discussion.

- **Too many buzz words.** There is a wonderful website associated with the cartoonist Scott Adams' character Dilbert that generates a random mission statement by combining buzzwords. For example: "The customer can count on us to assertively simplify excellent products because that is what the customer expects." I hate to say it, but these comic results sound a little too much like some of the mission statements that are actually out there.

- **Too long. Keep it simple.** You can always elaborate if the statement turns out to be limited.

- **Too focused on short-term goals.** You are trying to state your reason for being. Aim for a mission that will last beyond your current product cycle.

Examples

There are many styles of mission statements. Here are some examples you can use in your brainstorming session.

1. **Use of Bulleted Format**
   Example: Otis Elevator: The World of Otis
   - The world rides on Otis
   - Safety is our legacy
   - Exceptional service
   - A history of firsts
   - Quality
   - Getting the job done

2. **Combined Vision/Mission Statement**
   Example: Mc Donald's
   McDonald's vision is to be the world's best quick service restaurant experience. Being the best means providing outstanding quality, service, cleanliness and value, so that we make every customer in every restaurant smile. To achieve our vision, we are focused on three worldwide strategies:

   - **Be The Best Employer**
     Be the best employer for our people in each community around the world. See the McDonald's People Promise.
   - **Deliver Operational Excellence**
     Deliver operational excellence to our customers in each of our restaurants.
   - **Achieve Enduring Profitable Growth**
     Achieve enduring profitable growth by expanding the brand and leveraging the strengths of the McDonald's system through innovation and technology.

3. Single-Sentence Approach
Example: Agriculture-Based Industrial Lubricants (ABIL)
Our mission is to expand the market for crops grown in the United States by providing research and technology transfer leading to commercialization of environmentally-friendly industrial lubricants and greases.

4. Statement that Fits on a Brochure
Example: Hurd's Harvest Festival
Our Mission Statement:
"To provide everyone with a wholesome, memorable, fun-filled farm experience in a friendly atmosphere."

5. Statement that has Stood the Test of Time
Example: Agricultural Utilization Research Institute (adopted in 1988)
AURI was created to foster long-term economic benefit through increased business and employment opportunities to rural Minnesota through:

- the identification and creation of new markets, expansion of existing markets for new or existing commodities, ingredients and products;
- the development of more energy efficient, natural resource saving production practices; and
- the development of new uses or value improvements of Minnesota agricultural commodities.

How and When Mission Matters

To illustrate some important differences in how your reason for being in business matters, look at Table 1, a simple comparison between certain entrepreneurship elements as they relate to two particular cases: what we'll call a "life-long small business" and a "high growth" business. A life-long small business is a company that is started and nurtured with the idea that it will remain a size that is small enough to ensure owner control and large enough to support the household or house-

Table 1. How Different Missions Influence Various Business Decisions

Element	*Lifelong Small Business*	*High Growth Business*
Funding Strategies	• Unwilling to give up ownership control • Can tolerate moderate growth	• Requires large amounts of capital from investors who expect high growth rate
Funding Sources	• SBA-backed loans • Friends and family	• Friends and family sources limited to earliest stages • Venture capital, angels
Style and composition of management team	• Often family members • Expertise needed in working with employees, possibly low-wage employees	• Eventually requires highly experienced team, including high-powered sales ability, knowledge of large-scale operations and expertise in financial growth
Necessary characteristics of a marketplace for profitability	• Can run a profitable business with hundreds of customers (or even dozens, if the product or service is highly specialized with a premium service tag)	• Need at least thousands of potential customers; preferably millions
Staging of the business	• The initial pilot stage may be relatively close to the target size of the business	• Many stages, each funded at particular benchmarks and requiring additional growth capital
Revenue goals and tradeoffs	• Can accommodate non-monetary goals (willing to trade money for time)	• Monetary profit is the driving force.

holds that are associated with the business. On the other end of the spectrum is what we will call a high growth business, built with the intent to grow beyond the initial ownership and eventually reach a point where the original founders can withdraw their equity (for example, having the business acquired or going public).

Summary

The mission of a business drives the choice of strategy, and taking some of the steps outlined in this section should help you get started. Once you have a mission statement underway, you'll be ready for the tasks discussed in the rest of the publication.

Additional Resources

- **Mission Statement and Consensus Exercise**
  http://www.squarewheels.com/scottswriting/mission.html
  This is the very "homegrown" website of Dr. Scott Simmerman, an organizational consultant in South Carolina. The section connected to this link describes a simple but innovative means for getting people to talk about the mission statement.

- **BizPlanIt.com**
  http://bizplanit.com/vplan/mission/basics.htm
  This site has good descriptions of mission vs. vision statements. It also includes a section on Mistakes to Avoid.

- **Dilbert's Mission Statement Generator**
  http://www.dilbert.com/comics/dilbert/games/career/bin/ms.cgi
  A goofy site that can help break the ice if you have a group gathered to work on the mission statement. It generates "random mission statements" that consist of a string of buzzwords.

Issue #3: Know Where You Are Going-Understanding What Strategy Is and How to Get There

This issue is focused on defining and explaining the term "business strategy". The mission of the business, which was discussed in Issue #2, guides the selection of strategy. In this section, I explain how to get started working on your SWOT analysis (inventory of Strengths, Weaknesses, Opportunities and Threats), and I introduce possible strategic options for a value-added business. Issues #5-#7 continue this work by outlining the steps you will take to complete the SWOT analysis and carry out your market research.

The Ag- and Food-Based Angle on the Topic of Strategy

Entrepreneurs in ag- and food-based businesses face many challenges, ranging from increased competition from abroad to changing retail trade practices and environmental regulations. Entering such a dynamic marketplace without a good strategy is highly risky. Plotting an effective strategy involves getting to know your marketplace in great detail. This is especially important if you are moving out of a commodity-based business and into a value-added setting. In the pages ahead, you will learn about steps that will help you inventory yourself, your business and the marketplace. For ag- and food-based businesses, it is especially important to acknowledge that the strategy for the business is likely to be quite different from the one that characterizes any associated farm business.

Why Does it Matter?

The term "strategy" has become quite a buzzword over the last decade. You see the term popping up everywhere, on television ads for information technology firms, in front-page articles about new companies, and, of course, in websites and workbooks on business planning. But what does the term really mean for value-added businesses facing the changes in the current economy?

The word strategy was originally associated with warfare, referring to the science and art of employing political, economic, psychological, and military forces in order to outwit the enemy. When the term began to be used in the business world, it was most often used in reference to the domination of a marketplace. As in the military setting, formulating a business strategy is both an art and a science. Crafting an effective strategy involves both gathering data (the science) and making judgment calls (the art). Instead of a military enemy, the business strategist faces winning over the customer in the face of competitive forces in the marketplace.

The analogies with warfare are not without meaning. Strategy matters most in highly contentious situations, when stakes are high. Because change in our economy occurs at a faster and faster pace, most businesses are in highly competitive, contentious environments. In this section, you'll learn more about formulating a strategic framework for your business, while later chapters focus on the research and thinking required to tailor a strategy to your own operation.

Defining a Business Strategy

In their excellent article on strategy, Hambrecht and Frederickson call strategy **"the central, integrated, externally oriented concept of how we will achieve our objectives."** Let's take that definition apart and look at each piece.

Strategy as Focusing on Objectives

Management guru Steven Covey tells us always to "start with the end in mind." As was presented in Issue #2 of this publication, understanding the mission and vision of your business helps you to come up with your own specific objectives and goals. Any sound business strategy is designed to help you meet those objectives. Be clear on what you as a business owner wish to achieve, and as you formulate your strategy, as suggested below, be sure to check continually to make sure it matches your fundamental mission (and hence your goals and objectives).

Strategy as Central and Integrated

Consider how you approach a production problem. If you tried to remedy a problem of low yields by looking at just one dimension (say, pesticide treatment), you would be unlikely to solve the problem effectively. Only by considering all the possible causes (genetics, soil, pests, disease, etc.) and how the remedies interact might you come to an effective solution. Your business as a whole is no different. Hambrecht and Frederickson explain this by saying you need to answer the following questions:

- **Where am I going to be active?** (which products? market segments? geographic area? core technologies? value-creation strategies?)

- **How am I going to get there?** (developing or growing my own firm? collaborating with others? acquiring other businesses?)

- **How will I win in the marketplace?** (image? customization? price? product features?)

- **What will be my speed and sequence of moves?** (how will I stage my initiatives? what speed of expansion or diversification is appropriate?)

Use these questions to guide the formulation of a business strategy. Many of the answers will only come to light as you prepare and perform your market research (see Issues #5-#8).

Strategy as Externally-Oriented

One of the hardest things in business is to stay focused on the customer. You have probably heard the term "value-added" or "value proposition" over and over. What does it mean? Those terms refer to the fact that something is **of value if <u>and only if</u> customers are willing to pay for it.** It is easy to fall in love with a new variety, or creative packaging or product innovations, but the ultimate test is whether such things are perceived by the customer as valuable. Too often, businesses plow ahead with an approach and attitude that "we know what is best for the customer." Such an attitude ignores the power of the customer to say "no."

An externally oriented strategy also reflects the belief that in business every action has an equal and opposite reaction. In other words, if you attract a lot of customers, competitors will notice it and make a counter-move. It is crucial to understand not only who is currently in the market but also who has the potential to move into any market that you prove is lucrative. A difficult, but crucial aspect of strategy formulation is establishing a **sustainable competitive advantage**. This is often thought of as a barrier to entry that keeps others from invading your niche.

Finally, a strategy must take into account what is happening in the industry. Whether it is supply chain integration or environmental regulations, business owners have to be aware of the larger environment in which their business exists. Information technology has made it much easier to understand what is happening in the industry as a whole. Government statistics on industry are more easily obtainable and information about international markets is far easier to find. Thus, to craft a successful strategy, a business owner must remain externally oriented by understanding the customer, knowing the current and potential competition, and tracking trends and developments in the industry.

Strategy: How Do You Obtain Returns?

Taken together, the externally-oriented, integrated strategy will help you understand what Hambrick and Frederickson call "the economic logic" of the business - that is, "how do I make money?" They suggest four possible approaches to obtaining returns:

- Maintain the lowest costs through scale advantages;
- Maintain lowest costs through scope and replication advantages;
- Charge a premium price due to unmatchable service;
- Charge a premium price due to proprietary product features.

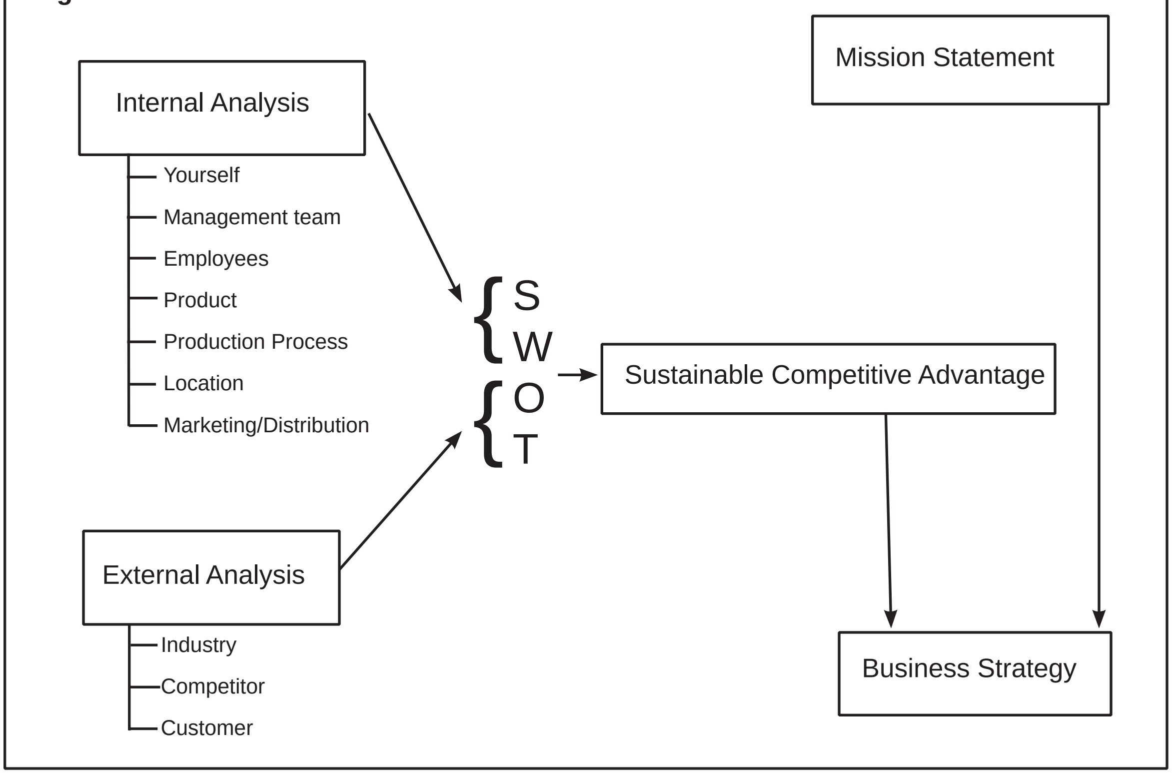
Hambrick and Frederickson suggest that once there is clarity about the mission and objectives of a company, that strategic analysis (looking at the industry, customers, economic, environment, competitor, internal strengths and weaknesses) will help point the way to an effective strategy in the marketplace.

The Steps for Getting to Strategy

Figure 1 illustrates the relationship of the business planning process to formulation of strategy. The specific steps are:

1. Develop a **vision/mission**.
2. Do an **internal analysis** to identify strengths and weaknesses.
3. Do an **external analysis** of industry, market and competitor analyses to identify the opportunities and threats and understand the driving forces in the marketplace.
4. Look for **key success factors, key risk factors**.
5. Find the **sustainable competitive advantage**.
6. Formulate the **business and marketing strategies.**

Figure 1



As discussed in Issue #2 of this series, your business strategy has to be grounded in the mission. Without a well-defined mission, an entrepreneur runs the risk of creating a business and marketing strategy that doesn't meet his/her original goals in starting a business. Whether or not you are starting a small business that will likely stay small or you are headed for a high-growth opportunity, you have to do all the steps to formulate a truly sound strategy. There are steps that you can do in an afternoon with a pad and pencil or steps that you can dig into over numerous weeks by carrying out extensive research. An entrepreneur's resources (time and money) will determine which of these approaches fits best.

What Do You Have to Offer the Marketplace? Looking Inward to List your Strengths and Weaknesses

Next, it is important to do a comprehensive, brutal, and frank inventory of the internal strengths and weaknesses (the SW of the so-called "SWOT Analysis" that lists the Strengths, Weaknesses, Opportunities and Threats) of your business. This includes looking at all elements of the business, starting with you, the owner. Make a bulleted list of any particular strengths you bring to the business or weaknesses and vulnerabilities that you see. Consider such things as background in dealing with uncertainty, special technical or operational expertise, sales/marketing experience, network of contacts, or special ties to the marketplace. Next examine the rest of the management team (see Issue #4 for How to Build the Right Team) for its strengths and weaknesses. Do you have a good, balanced team? Or if you are operating solo, what management skills are missing?

It is also essential to understand the strengths and weaknesses of your **employee base.** For example, do you have access to a low cost (or high quality) pool of workers? Is there stability in your workforce? Consider any special skills or training that your employees have, or list those things they lack. Looking ahead a little bit, consider whether they are equipped to provide top-notch customer service.

Examine the **features of the product or service** as you build the S&W of the SWOT. List as strengths any proprietary technology or innovations. Include the unique special features of your product/service (is it organic? cost-saving? highly reliable? have a unique taste?). You should also examine your **production process** and list any strengths and weaknesses. What is your **input cost structure** (for example, high volume/low price), and are costs vulnerable to change? Do you have flexibility in the production process (e.g., can you scale up or down relatively easily?). Your physical **location** may be a strength or weakness (close to consumers, employees, input providers, strategic partners), or you may have a virtual presence that gives you added flexibility.

Consider the pluses and minuses of your **distribution methods.** Do you have access to a special distribution channel? Do you have the potential for using technology to distribute your product or service more effectively? If you have a key customer list, count it as a strength. If reaching customers is still a question mark for you, put it in the weaknesses column. How will you obtain your key customer lists?

When you are finished making your list of strengths and weaknesses, you should have a very complete portrait of the business and all its resources. In examining the SW list, you may find that some weaknesses could be remedied, and you may find some things that you have listed tentatively under strengths for which you do not yet have documentation. It may be useful to mark any uncertainties with a question mark or other symbol; you'll need to revisit them as the business develops. For now, however, the internal inventory can help you:

- Base your business strategy on key strengths.

- Look for ways to use your strengths to erect barriers to entry.
- Be aware of the challenges your company faces

What Does the Marketplace Hold for You? Looking Outward to List your Opportunities and Threats

Once the internal inventory is completed, it is time to look outside the business to understand the opportunities and threats. The goal is to look for:

- Opportunities to reach underserved markets that are of sufficient size and with adequate buying power;
- Opportunities to capitalize on new trends or new technologies to establish a sustainable competitive advantage;
- Threats that equate to marketplace risk so that you can identify and understand your key risk factors.

Market research is a key to making an accurate list of opportunities and threats, because it allows the entrepreneur to understand crucial information about the industry, the competitor, and the customer. Issues #5-6 of this series are devoted to helping you ask the right questions in your market research and how to execute both formal and informal methods of market research.

What Strategies are Possible?

Issue #6 in this series is focused on helping you use the results of your inventory to determine the key risk factors, the key success factors and to formulate a strategy. For now, it will be useful to understand, in general, that the goal of formulating your strategy is to determine your sustainable competitive advantage, or how you will differentiate yourself from the marketplace.

In their book called *The Strategy-Focused Organization,* Kaplan and Norton argue that differentiation in the marketplace usually occurs in one of three ways:

- **Product leadership:** These companies focus on creating new products and being the first to market. One example would be the introduction of bagged lettuce.
- **Customer intimacy:** These companies create a strong bond with their customers and sell to meet their needs. An example might be a fruit grower with strong ties to the school food system, tailoring product packaging to that specific marketplace.
- **Operational excellence:** These companies deliver a combination of quality, price and ease of purchase that no one else can match. For example, companies that have tapped into the benefits of supply integration have been able to remain competitive in the ever-changing fruit markets.

Summary

When you have gone through the steps outlined in this issue, you will have a better idea which of these general strategies fits best for you. In Issue #6, we'll take a look at how the findings you come up with in doing the homework tasks of business planning (determining your mission, building your team, doing market research, completing the SWOT analysis) provide direction for the strategic choices you face regarding appropriate arenas of activities, the vehicles for getting there, the differentiation strategy, and the staging of the business. The goal will be to clarify the economic logic, or revenue model, for the business.

Additional Resources

- **The Strategy-Focused Organization.** Kaplan, Robert S. and David P. Norton. Harvard Business School Press, 2001.

- **"Are You Sure You Have a Strategy?"** Hambrick, Donald C. and James W. Fredrickson. *The Academy of Management Executive*. November 2001. 15:4. pp. 48-59.

- **MeansBusiness.com** http://www.strategyandcompetitionbooks.com/Strategy-and-Competition-Books/All-the-Right-Moves.htm
  The link listed here is to a resource that is part of the website created by a company called MeansBusiness. The site allows you to purchase, in an ala carte mode, portions of material from the popular business press. The resource associated with the link above references sections of a book called *All the Right Moves, A Guide to Crafting Breakthrough Strategy*, by Constantinos Markides.

Issue #4: Building the Right Team

In this issue I address the important topic of the management team. After explaining why the leadership in the company is crucial, I outline the elements that are needed in a strong team. The discussion includes comments on how and where the management team is featured in the business plan.

The Ag- and Food-Based Angle on the Management Team

Many so-called "agripreneurs" are family-based businesses. Doing business with relatives is a common experience in farm business culture. However, ag- and food-based businesses should be especially careful in crafting and managing the family member relationships that are intermingled with the business. Entering new markets, with the accompanying risk of failure, requires the entrepreneur to make sure all members of management have extremely clear expectations ahead of time about the vision, scope, direction and leadership structure of the business. In addition, it may be necessary to explore adding management expertise from outside the family in order to get special expertise, or access to new markets, or other resources.

Why the Team Matters

New businesses are usually born (or evolve) during a time of great optimism and hope, of excitement mixed with fear. Starting a business is also a time when many entrepreneurs decide to invite a partner or co-owner along for the ride. Partners can share risk, reduce the workload, and provide resources (for example, cash, expertise, network connections). But partnering with the wrong people can lead to disaster and broken relationships.

Most people who lend to or invest in new businesses will state that the most important success factor is the management team. In fact, it is common to hear investors say they prefer a great team with a mediocre idea to a mediocre team with a great idea. Even if a business is not going to require outside investors, this wisdom still has meaning for every entrepreneur. Leadership of the company is crucial. If potential investors look at the management team and say "wow!', you can be sure they will be anxious to find a way to evolve the project, even if they hate the idea you brought to them.

The Management Team and the Business Plan

Choosing the management team is part of the homework for business planning. For very small startups, it may not be feasible or desirable to add others into leadership positions. But the planning process must include a clear understanding of why that choice is made, what might change in the future, and how current leadership will manage to cover all the strategic, operational and financial operations of the company.

A written business plan has a special section featuring the people involved in making the company successful. A common mistake entrepreneurs make is burying the resumes in the back of the plan somewhere. In fact, the management team and any other people providing leadership or guidance (such as an advisory board or special consultants) should be featured prominently in the plan. You'll find a worksheet at the end of this series to use as a tool for starting background thinking and writing to complete the management section of the plan.

Building the Right Team

Keyword = Balance

Wherever you look in the management literature, almost every piece of advice written about management teams includes the word "balance." Most experienced entrepreneurs confirm the need for the top leaders in a company to serve as both the visionary and the operational manager - tasks that draw on so many different skills that it is rare to find them in a single person. While the creation of the business is usually best done by a "big picture person," the long-term sustainability of the business depends on effective management of the "small details."

Although most experts agree balance is needed in management, they also agree it is hard to achieve. During the bootstrapping stages of a new company, the entrepreneur usually does everything from taking out the garbage to making the highest level strategic decisions, and typically develops a strong sense of control over every aspect of the business. When it is time to grow, the entrepreneur must accept that additional management skill will be healthy for the company, even though it will require him/her to give up some control. At that point it is necessary to set aside ego considerations and do a ruthless inventory of the entrepreneur's own qualities and abilities in order to identify what is missing and how those gaps may affect the success of the company. Sometimes a good mentor can be a big help with this task because of the ability to bring an objective outside perspective.

Ironically, if you succeed in creating a balanced team, you automatically set into motion a level of "creative tension" in the workplace. Leading a company with people who are different from you can be a challenge. The entrepreneur's job is to keep everyone focused on the same set of goals, despite differences in backgrounds, approaches, and working styles.

The Portfolio of Management Talent

As a whole, the management team needs a portfolio of talent including: vision, successful sales and marketing ability, people management skills, financial expertise and operational competence. A very common dilemma seen in startups is that a founder or founders have a strong focus in one area (i.e., marketing) at the expense of other functional areas (for instance, operations or finance). For example, an entrepreneur can become so involved with the product innovation that he/she loses sight of the company's market potential.

Using Advisors to Balance the Portfolio

You can look beyond the core management team for resources that provide the right portfolio. For example, you can build up management expertise by assembling an outstanding advisory board or board of directors. When picking the people to serve on the board, look for mentoring ability and needed expertise. Don't add members to the advisory board that are a carbon copy of your own competencies. Members of the board should have the qualities of a good mentor as well as both the motivation and the availability to guide you in strategic decision-making. For example, a good board member might be someone who is excited about your concept or product and is also a major customer. Beyond their mentoring capacity, board members should also have special expertise in some area such as finance, operations, or marketing. Remember, you are working on balance, so pick members whose talents are complimentary to your own. Be careful to make sure that each board member adds a needed dimension.

Finding and recruiting members for the board is a dilemma for many startup entrepreneurs, especially if they are young. Building the right board of directors is primarily a networking task. There is a lot of work in pitching your idea to each potential member. In fact, it may be necessary to have a short written business plan or at least an executive summary to show to prospective board members in order to get the right people involved. Alternatively, the funding entity may dictate who they want added to the board.

Before you get locked into a board of directors (which legally every incorporated business must have), consider putting together an advisory board. In the very earliest stages of the business, the addition of an advisory board to support your core management team is a signal to the investor that you recognize the value of the experienced perspectives afforded by a strong advisory board. It also shows that you have the initiative and salesmanship to formalize mentoring relationships.

Using Employees and Consultants to Balance the Portfolio

Finally, you can balance the company's human resources by hiring the right employees and picking appropriate key consultants for the business. For example, your team of consultants should cover areas such as: legal issues, accounting, information technology, human resources benefits. When choosing consultants (see Recommended Resources below), be careful to select an individual or firm with experience working with small companies that have goals similar to yours. Ask each consultant for a list of references that includes other startup businesses and call their references. Remember, if you move toward growth and/or acquisition or IPO, you will need to think about "graduating" to a different team of consultants.

Caution on Partnering with Friends and Family

Businesses are often started by best friends or even spouses working together. Choosing to partner with someone you know and trust is, of course, very appealing. But if leadership is not clearly outlined from the very beginning, the result can be disastrous because expectations of each founder may not be well understood by the others. In addition, there is a lot of room for misunderstandings about equity and ownership. If a friend, colleague or relative helps out in some way on the "ground floor" of your business and expects "sweat equity," there will be heartbreak and feelings of betrayal if those expectations are not met. Set clear expectations from the very beginning of the relationship with everyone who is involved with your new business. Do not hold out vague promises for profit sharing and equity. Wait until you have a clear plan about how employees or others might participate in the success of the business.

Writing About the Management Team

The precise format and content of the management section of the business plan will be covered in Issue #9, Putting it on Paper. The Management Description Worksheet found at the end of this issue will help you prepare for the task of describing the leaders who will be implementing your business strategy. See Additional Resources for some ideas on how the actual company can be structured from a legal standpoint.

Summary

I placed the discussion of the management team early in this series in order to emphasize its importance and to encourage you to think about some of the key issues early on in your business planning process. In reality, building a team will be done in parallel with many other startup activities. Even if you are an owner-operated business that intends to stay relatively small, the leadership team discussion is important, especially the issue of finding ways to complement your abilities and competence through advisors and/or consultants.

Additional Resources

For Deciding About Structuring Your Ownership

- **Foley and Lardner**
  http://www.foleylardner.com/FILES/tbl_s31Publications/FileUpload137/1024/handbook_entity_2002.pdf
  This is a document covering how to choose your business entity. The Foley and Lardner site is packed with handbooks and guides related to legal issues for startups.

- **CitiBusiness**
  http://us.citibusiness.com/

  and

- **Small Business Network**
  http://www.americanexpress.com/homepage/smallbusiness.shtml?aexp_nav=smbustab
  These two sites, by Citibank and American Express, respectively, contain a wealth of practical advice for startup entrepreneurs. The Citibank site has a section I recommend called "Business Builders" that includes advice on structuring the business. The Small Business Network has an "Ask the Advisor" feature where you can ask questions and get feedback.

For Help Choosing and Managing Small Business Consultants

- **"Guide to Entrepreneurship Services."**
  Leonard Bisk. Published as part of the *Entrepreneur Magazine* series.
  This is a wonderful practical guide to selecting the right consultants. It includes tips on hiring and managing consultants and is aimed at the practicing entrepreneur.

For Guidance in Assessing Personal Management Abilities

- **Prentice Hall Website**
  http://www.prenhall.com/scarbzim/html/check1.html
  This site is intended to support one of the best entrepreneurship texts out there: *Entrepreneurship and New Venture Formation*, by Thomas W. Zimmerer and Norman M. Scarborough (1996). The checklist on this site can help entrepreneurs understand their own readiness to take risks and can serve as a starting point for a discussion between partners about what they each offer to the management team.

For Help in Writing the Management Section of the Business Plan

- **BizPlanIt**
  http://www.bizplanit.com/vplan.html
  This site has great advice about each section of the business plan, including information about typical mistakes entrepreneurs make when writing their plans.

- **Management Description Worksheet**
  If you or your management staff do not possess experience in the business you are undertaking, you can still create a strong management section that will help you sell your business concept to the reader. Many skills sets can be transferred from unrelated work quite successfully. It is often simply a matter of realizing the skills you possess so that you can highlight them. This worksheet will prompt you to create a list of relevant skills and experiences that may not currently be apparent to you. Use the list you generate to create your Management Description.

1. List all of the responsibilities you had in your last work experience, whether it was another entrepreneurial venture or a job working for someone else. When you are making this list, do not only enumerate the tasks that were part of your job title, think about what responsibilities you assumed because they came naturally to you. These may be things as simple as the ability to crystallize ideas in meetings or manage project teams.

2. For each responsibility, determine how those skills can be applied to your business. Once you have this information, you can create a description of your skills for your business plan.

Prior Responsibility	Application to Current Business

3. If you are young and do not have much work experience, turn to life experiences to generate a list of skills that will help you run your business. Maybe you are the leader in your family who always planned the family vacation, or the one at school who everyone always turned

to for the most efficient way to organize things. Generate examples that demonstrate others' recognition of these skills, such as awards, positions held in student societies, family responsibilities, etc.

4. Now, determine how these skills will help you run your business. Use these conclusions to create a description of yourself for your business plan.

Skill	Application to Business

Issue #5: Doing Market Research - Part 1: Know What You Are Looking For

In issue #3, we introduced the concept of the SWOT Analysis (Strengths, Weaknesses, Opportunities, Threats) and elaborated on how to do an internal inventory to arrive at defining Strengths and Weaknesses. This issue focuses on getting prepared to explore the Opportunities and Threats part of the SWOT analysis. Specifically, we discuss the questions that need to be answered by market research with regard to the industry, competition and customer. Issues #6 and #7 serve as a guide to research methods and key sources of information.

The Ag- and Food-Based Angle

For ag- and food-based enterprises, framing the right research questions is crucial. Ultimately, your market research will confirm or contradict your perceptions of what constitutes "value-added" and your sustainable competitive advantage. Because so many ag- and food-based businesses are founded on product innovation or relatively new approaches, it is especially important that market research be well-oriented.

Before You Start Researching, You Need to Know the Right Questions

You may have heard the saying that if you don't know where you are going then really any destination will do. In doing market research for a new product or service, it is easy to get overwhelmed by information, especially if you don't start with a very clear idea of what you need to know. This issue is focused on helping you frame the right questions, so when you do your market research you get meaningful data (see Issue #6 the "how-to" aspects of market research).

The OT in SWOT

Market research involves continuing work on the SWOT Analysis, this time focused on uncovering the Opportunities and Threats that were discussed in Issue #4. The focus is an external one, as opposed to the internal inventory of Strengths and Weaknesses. To complete the SWOT analysis, the entrepreneur needs to understand the environment in which the business will be operating. The goal is to uncover or refine possible unfilled market niches, to understand existing and potential competition and to become deeply acquainted with the customer.

Entrepreneurs often underestimate the power of competition. In addition, they frequently fall in love with their own business ideas and lose the ability to be objective about what truly adds value for the customer. Market research is a means of performing a "reality check" on a business idea. While in the next issue we'll discuss where to find information on the market, in this issue, let's focus on what you need to know. Think of this as a way of saving valuable time (one thing almost all business owners have too little of) because it allows you to carefully focus your inquiry.

Remember, the longer term goal in formulating your business strategy is to discover your own sustainable competitive advantage. You really cannot do that without knowing the actual needs of the user and who else in the marketplace is striving to meet those needs.

Getting Oriented for Effective Market Research

Performing market research is a bit of a treasure hunt. Like most hunting, it is not necessarily highly structured and can be quite messy. The discussion below divides the hunt into three categories of information: Industry, Competitor, and Customer. Be aware that in practice, when you search for information on any of these three areas they are often intermingled and inter-related.

What You Need to Know About the Industry

In his excellent book on entrepreneurship, Rob Adams makes the case that building a successful business depends on (among other things) something he calls "execution intelligence," referring to "the ability of a particular group of people, in a particular place and time, to make a company thrive." Adams suggests that to have execution intelligence the management must have adequate "domain knowledge" as well as experience growing a business in a fast-paced and competitive environment. Understanding the market space in which you operate raises your ability to make good initial choices and to interpret changes that occur in the industry. For example, here are some things you should know about your industry before formulating your business strategy:

- **What are the key trends and technologies that are influencing the industry?** The goal is to position your company for future growth. Are you jumping on a bandwagon? Are you acting as an innovator or first-mover? Are there trends in the industry that point to increased and/or stable demand for your product or service? It is also very important to see if technologies (especially information technologies) are impacting the industry. Are they lowering costs? Increasing ability of firms to service customers? Opening access to new markets? A key question is whether technology will be lowering the barriers to entry (increasing your competition) or whether you can position yourself strategically to use new technologies to keep people out of the market niche you plan to inhabit.

- **Is the industry growing, stable, or in decline?** Of course, it is ideal to create or develop a business in an industry that is growing, but there are also market opportunities when industries go through change. Either way, you need to be aware of the industry trajectory and how it might impact your business over time.

- **How big is the marketplace?** How much money is spent in this sector? An angel investor I interviewed told me that most of the people who come to see him don't know how many zeros to put after the first digit when estimating market size. During your industry research, try to find various estimates of the total size of the market. It will help you judge whether your plan to target a certain percentage of the market is realistic. In addition to the size of the market, you need to understand what economists call "effective demand," or customers with a willingness to buy and the appropriate income.

- **Are there any new laws or regulations which are bringing changes?** This item may be especially important for ag- and food-based businesses given the environmental and food safety issues that can impact the sector.

What You Need to Know About the Competitor

It is not uncommon to hear an entrepreneur say "I really don't have any competition." Nothing could be further from the truth! Whether or not someone nearby produces the precise equivalent of your service or product, you are always competing for other uses of the customer's dollar. And most markets are truly global now, so there are probably competitors well beyond your local area that you have not yet discovered. Claiming that there is no competition simply will sound naive to those who might fund the business.

An inventory of the competition is designed to help identify **opportunities**, niches with weak competition, where you can get in and stay in the marketplace. In addition, competitor analysis can lead to discovery of successful strategies you may wish to mimic, or unsuccessful approaches to avoid. In identifying competitive **threats**, the entrepreneur should consider both existing and potential competition. Here are some of the things to look for:

- **Who is (or might be) your competition?** You should be able to list the names of the top competitors, along with an inventory of their strengths and weaknesses (as viewed by the customer).

- **Who is the customer in the competitor's market?** If the marketplace is segmented, who is serving whom? Why is each competitor successful in a particular niche?

- **What type of facilities and product/service characterizes the competition?** It's important to know about location, size and capacity of the competition. In addition, what is the competitor's product mix? How much do they charge and what items make up their product/service line? If possible, it is also useful to understand their unit cost, capital investment and key suppliers.

- **Who does the competition employ?** Since the entrepreneur will be competing in the same labor pool, it is important to know the employee base of the competition. What are typical levels of fringe benefits/compensation and is there an active labor union? In addition, it is helpful to understand the leadership team of competing companies, including the managers and the board of directors.

- **What is the strategic direction of the competition?** Are there plans for new products or new initiatives? Press releases and/or websites can be a good source for picking up the apparent strategic direction of the competition.

- **What is the image of the competition in the eyes of the customer?** Knowing the corporate image and reputation of the companies who form your competition can be crucial in formulating a successful strategy.

- **How quickly can the competition react?** If an entrepreneur is successful, it will provoke a reaction? What are the capabilities and flexibility of the competition to respond?

Knowing the information outlined above is crucial for understanding how you will distinguish yourself in the market. Your business and marketing strategies must take into consideration the market niche, customer base, product mix, employees and leaders within the competition.

What You Need to Know About the Customer

Rob Ryan, a pioneer in the high-tech industry, founded Ascend Communications in 1989, and throughout the nineties provided firms with the infrastructure they needed to keep up with the rapid growth of the Internet. Even though his book on startups is aimed at the high tech industry, the insights are valid for anyone starting a company. One of the first questions he asks any entrepreneur is "how many customers have you talked with?" Without firsthand knowledge of your customers, he argues that your business planning process will lack credibility.

In a similar vein, according to Rob Adams, market validation is the central activity for reducing the risk of starting a business. He has a mantra that goes "solve the pain, solve the pain, solve the pain." What he means is that it is crucial to understand what will motivate (or block) the customer from choosing your product or service. Only if the customer is experiencing a "pain" that you can solve will he/she shell out the money to buy your product. Are you offering desirable qualities (e.g. organic) or meeting special needs (e.g., food safety)? Are you saving the customer money or time? In other words, what is the value proposition for the customer? To understand what value you are adding to the market, you need to answer the following questions:

- **Who are your potential customers?** In order to identify a niche, clarify your product concept and fashion an effective marketing strategy, you have to be able to quantify your customer base and understand their purchasing behavior. Estimating demand is also critical for building your financial model of the business (more about this in Issue #9). How many are there? What are the demographics (such as age, sex, marital status, income levels, education levels, occupation, cultural, ethnic or racial backgrounds)?

- **Where are your customers located?** Strategic choices such as how to deliver the product or where to locate the business depend on knowing the location of your customer base. In order to implement an effective promotional strategy and estimate how much it costs to acquire a customer, you need to know the regional characteristics of your target market. If you are using information technology to reach a broader audience, what are the characteristics of the virtual market?

- **What pain is your customer feeling** (and how much will they pay to relieve the pain)? In the quest to define your competitive advantage, you have to understand what the customer defines as value added. Accordingly, it is important to know if they are dissatisfied with the competitor, whether they have a positive reaction to your idea/concept, and whether they have a need or want that you can fill. What is the willingness to pay? The goal is to understand what motivates the customer to put money down on the table to get a service or product.

Summary

Formulating your questions for market research prepares you for the research tasks outlined in Issue #6 of this series. In order to step into the research arena well armed, review the questions asked above and decide which are most relevant for your own situation. In particular, if you think about a prospective partner, funding source, or customer, where do you think you need to establish credibility? What is the information that is most uncertain? Issue #6 will help you determine the most cost effective approach to answering the relevant questions.

Additional Recommended Resources

- **A Good Hard Kick in the Ass**
  Rob Adams. Crown Business Publishing, 2002.
  Although this book is focused on high-growth, high-tech businesses, it is an excellent source of advice for most entrepreneurs. Adams focuses on the importance of knowing your customer, having execution intelligence, and properly staging your business.

- **Smartups: Lessons from Rob Ryan's Entepreneur America Boot Camp**
  Rob Ryan. Cornell University Press, 2002.
  This volume is also based on high-tech business but has a wealth of tips for anyone starting a business, especially in the area of knowing your customer base.

- **Small Business Administration's Online Women's Business Center**
  http://www.onlinewbc.gov/docs/market/mk_research_proc.html

This site features practical guidance on market research, outlining seven steps.

- **Small Business Town**
  http://smbtn.com/businessplanguides/bplan3_marketing.shtml
  This is an excellent collection of on-line guides for market research, emphasizing a practical approach and identifying current sources of information.

- **HowStuffworks.com**
  http://biz.howstuffworks.com/market-research.htm
  This site contains lessons on market research and some excellent links on market resources.

Issue #6: Doing Market Research - Part 2: Know How and Where to Look

In this issue, the focus is on matching a method of market research to your own particular needs and resources. Using the questions developed in Issue 5, I discuss the costs and benefits of doing primary and secondary market research and provide a guide to on-line resources that relate to the value-added markets. More information about doing surveys and focus groups is found in Issue 7.

The Ag- and Food-Based Angle

Many of the methods and sources of market research may be new to ag- and food-based entrepreneurs. For example, if the business is connected to a farm business, data sources currently familiar to the business owner may be commodity prices, weather information, or government reports on supply and demand. To explore a consumer product or a business-to-business company requires more in-depth research on the marketplace (customers, competitors), and the value-added entrepreneur must cultivate a new awareness of where to find such information. In addition, techniques such as surveys and focus groups may also be new to the ag- and food-based entrepreneur.

Start with the Right Questions

When talking about doing market research, experts often urge entrepreneurs to "do your homework!" Putting aside any negative associations most of us have with the word homework, the analogy is a good one. Market research is definitely hard work! And it serves as the basis for the initial strategy choices in a new business just as homework prepares students for tests. Relating to the work outlined in Issues #3 and 5 of this series, market research is intended to help you do your SWOT analysis by exploring the opportunities and threats that are in the marketplace.

In school, when you sit down to do your homework, the first step is checking the assignment book to see what questions you are supposed to answer. No matter how perfectly you might answer the wrong questions, the teacher rarely gives you credit. For the entrepreneur, there is no "assignment book." Although in Issues #5 of this series we outlined a general list of what is important to know, the precise questions that must be researched are different for every single new business. Research must be guided by the vision/mission of the business and by the initial work on the SWOT analysis.

Market research should provide critical information about the competition and the customer, and what is unknown varies tremendously from business to business and from individual to individual. For example, an entrepreneur who is considering creating a product line in response to current demand may know the customer very well, but not much about the competition. Other prospective small business owners may know an industry inside and out, but may not have much direct contact with customers. To further complicate things, the entrepreneur always has resource limitations, since so many aspects of the business compete for time, money and human resources. Finally, the process of researching a market is rarely a well-defined, linear pathway. Explorations of market data inevitably lead the researcher in unanticipated directions.

We suggest the following initial approach to market research:

1. **Decide on your budget and timeframe**. Estimate how much money you can spend and also how much of your energy you can devote to market research.

2. **Draw up an initial list of questions.** Divide them into 3 categories: 1) urgent and important, 2) important, and 3) other. To determine what is in the urgent and important category, ask yourself: Do I need to know this information right now? Will

it help reduce the initial risks in starting my business? Will it change my decision-making at the earliest stages of the business? Do those who might fund the business expect me to have this information before they will commit support to the project? If the information is not urgent, consider whether it belongs in the important category, which includes questions that must eventually be answered to run the business. Ask yourself: If I get this information after the start of the business will it still be useful? How will it help guide on-going strategic decisions? Will those who help finance my business expect me to know this information eventually? Put remaining questions in the other category, which includes things you might like to know but that are not going to influence your decision-making. Doing this sort of "triage" with your questions will help focus your market research efforts.

3. **Plan the staging of your market research.** This can include outlining various stages of work, including research that occurs before opening day, research within the first 6-12 months of operation, and research that will be ongoing as your business operates over the years.

With a good list of questions and a general timeframe, you are ready to start your homework.

Choosing Methods for Market Research

Market research can include what is called **primary research** (information that you generate from your own efforts and firsthand sources) and **secondary research** (information gathered by others, such as the government). For example, it is quite common to use secondary research to get the "big picture" about the customer base, the industry trends, and perhaps a list of competitors, but to rely on primary research to find out about specific customer needs and wants, or details such as detailed information on competitors.

Choosing the right mix of primary and secondary research depends in part on the questions that are on the "urgent and important" list, and also on your budget constraint. As a general rule of thumb, primary research is more time consuming and expensive but can provide useful detail. On the other hand, secondary information is more widely available (and thus less expensive) but typically does not have a level of detail that helps with critical strategy decisions. How you choose the portfolio of primary/secondary research depends on whether your most abundant resource is time or money.

Thus, if you have **Money but not Time**, you might consider:

- Hiring a research company to generate primary data (note: you still have to decide what questions need answering);
- Contracting on a short-term basis an individual who can carry out some of the research tasks for you;
- Buying private sector data (such as the Gardiner Reports if you have a technology-related company);
-

If you have **Time but not Money**, consider:

- Doing customer survey work yourself;
- Working with a local librarian to explore secondary sources of information (government statistics, industry trade magazines);
- Involving other members of the prospective management team;
- Working with students from a local college on a market research project.

Create a System

An important "best practice" in market research is to establish a system for how you will keep track of information. It can be as simple as a set of file folders or index cards or as complex as a computerized database, but create some structure for storing the information you collect. In particular, you want to write down where you found the information, what year it was published, and any important details about the source.

Next, let's consider specific methods for gathering market information.

Secondary Sources

The process of obtaining secondary information has been changed profoundly by the Internet. For example, it is now easier than ever to obtain government information, with many departments offering the option of downloading numerical data or written reports essentially for free. However, don't be fooled into thinking that everything is on the Internet. It is still absolutely crucial to visit a bricks and mortar library to explore everything that is available. In looking for secondary data, consider some of the following sources:

- **Industry and Trade Associations**. There is a trade association for just about everything you can imagine. Many associations also publish newsletters, magazines, or bulletins with useful information for entrepreneurs. Many associations are also providing information online (note: most will have a url that ends with .org). As a starting place, look in the **Encyclopedia of Associations**, a volume you should be able to find in the reference section of your library. There is also an on-line source for looking up what trade associations exist: the Gateway to Associations (http://www.asaenet.org/Gateway/OnlineAssocSlist.html). Reading association publications can provide some interesting background about key trends and concerns characterizing the industry. It can also be an interesting source of information about the competition. Even the advertisements in trade magazines can provide interesting information for the entrepreneur trying to get acquainted with a new industry.

- **General Internet Searches**. Using an Internet search engine (such as **Google**, **Dogpile** or **About**), you may be able to turn up thousands of "hits" that match keywords such as your product category or industry designation. However, searching through the list returned by the engine can be frustrating and time consuming. Be careful to verify the credibility of any source you pick up this way. One thing that is very interesting is to see if you can locate any competitors through general searching. The results can tell you such things as: whether the competition has a strong internet presence, whether competitors are reaching out beyond local markets, what pricing is standard among your competitors.

- **Guiding Your Search with Commercial Databases**. There are an increasing number of subscription-based services that are intended to help guide your searching of digital resources. Databases such as Lexis-Nexis and Dialog allow you to search on-line archives of articles from popular press to scholarly journals. If you live near a university that has a business school, its library is likely to subscribe to such services. You may find access through your public library as well.

- **Government Sources**. Most government agencies provide some data online. For market research purposes, some of the key online sources are:

  ◊ **FedStats** - (http://www.fedstats.gov/) - a guide to 100 Federal Agencies. A good place to start searching if you have a clear focus on the market sector.

  ◊ **Bureau of Labor Statistics** (http://

www.bls.gov/home.htm) - wage data, demographics, industries-at-a-glance.

◊ **U.S. Census** (http://www.census.gov/) - demographics, economic data and links to state-based statistics and international statistical entities.

◊ **Bureau of Economic Analysis** (http://www.bea.gov/) - national and international economic data.

- **Information on Industries and Public Companies**. If your competitors are public companies, there are many ways to access relevant data. Most involve some charge, but some are free. For industry information, it is helpful to start by looking up what is called the Standard Industrial Classification (SIC) for your product or service. There are lookup services, such as the one found at http://www.express-advertising.com/sic_lookup.html. The SIC codes are being replaced over time by a new system of classification called NAIC, which can be determined by the lookup service at http://www.osha.gov/oshstats/sicser.html. Once you know the relevant code, here are just a few examples of places you can look for information on your industry:

◊ **PRARS** (http://www.prars.com/ibm/ibmframe.html);

◊ **Report Gallery** http://www.reportgallery.com/);

◊ **Carol.com** (http://www.carol.co.uk/) and **Wall Street Journal** (http://wsj.ar.wilink.com/asp/WSJ1_search_eng.asp) For free sources for annual reports;

◊ **SearchSystem** (http://www.searchsystems.net/index.php) - a site with free copies of public records.

◊ **Hoovers On-Line** (http://www.hoovers.com/) - comprehensive list of industries studies available for sale.;

◊ **Bizminer.com** - (http://bizminer.com/) - market research reports, industry analyses, local area vitality profiles for sale;

◊ **Moody's Industry Review**. New York: Moody's Investors Service, 2000. Management - Ranks companies in 140 industries by 12 financial criteria, including size, profitability, and stock characteristics. Its objective is to provide key financial information such as operating statistics, rankings within each industry, stock exchange information, long-term debt, price earnings ratio, and operating profit margin. Look for it in your public library (not available online).

◊ **Standard and Poor's Industry Surveys**. 3 volumes. New York: Standard & Poor's Corp., 1999. Print resource that includes an analysis of major industries, these quarterly reports give detailed information on 52 large industries, including trends and analyses of market share.

◊ **Plunkett** (http://www.plunkettresearch.com/) - provider of business and industry information, market research, trends analysis, statistics, company profiles and executive mailing lists.

◊ **Business.com** (http://www.business.com/) This is a business search engine and directory that has a section devoted to agriculture and another one to food.

◊ **Zapdata.com.** (http://www.zapdata.com/) This is the Internet service of D&B® Sales & Marketing Solutions, with a comprehensive virtual data superstore. Registration is required but requires no fee. Some reports are provided without charge, others are on a fee basis.

- **Local Information**. If you are looking for information about local markets, you might want to check the following sources:

  ◊ **Cooperative Extension** (find the closest office at http://www.csrees.usda.gov/Extension/) - this agency associated with USDA may have reports, data, or bulletins that relate to your product or service.

  ◊ **Chamber of Commerce** (find the closest office in your phone book) - Often a local Chamber of Commerce will feature statistical data about the area and will have a list of businesses that may be helpful in checking out your competitors.

Secondary sources of market information are good for getting the big picture and understanding the trends and technologies that might affect your product or service. Rarely, however, will secondary sources alone be adequate for making good decisions about a business strategy. To gather more intimate knowledge with a more focused content, it is necessary to do some primary data collection.

Primary Sources of Data

There are formal and informal ways to gather primary data. First, let's look at some of the informal methods and then consider statistical surveys and focus groups.

Informal Techniques

- **Use the phone book**. This is a source that is commonly overlooked by entrepreneurs but can help you see who is in the market and how they are advertising.

- **Get on the phone**. One entrepreneur we interviewed said that she would set a goal every day to spend an hour on the phone, talking to potential customers. By setting a goal and a time limit, the task of gathering information may seem less daunting. You can also try e-mail, but person-to-person contact with customers is very important for building your own credibility and as a means for understanding what customers want and need.
  ◊ Talk directly to customers
  ◊ Talk to the competition
  ◊ Talk to the competitor's customers.

- **Do a trial run at a farmers' market**. Farmers' markets provide a wonderful testing ground for new markets.

- **Check out credit reports**. You can buy credit reports on your competition as a means of finding out the financial health of the company. You can search online for available reports at the Dun and Bradstreet site (http://smallbusiness.dnb.com/).

- **Research by "walking around".** There is no substitute for visiting your competitor. Whether it is exploring the website of a virtual company or making a trip to the bricks and mortar site of your competition, you can use the time to check out pricing, observe customers, and evaluate the niche and image of the company.

- **Visit or participate in a trade show**. Trade shows offer an opportunity to observe competitors and customers at the same time.

- **Examine** the competitor's website, brochure, and sales literature.

- **Try a simple website**. The Internet provides an opportunity to experiment in the marketplace, by offering new products on a trial basis. You can add new products to an existing website or try and introduce your product through another individual's "catalogue-type" website. However, this type of dabbling in the market will only give you good information if the website is designed to be picked up in common searches. This type of informal primary research may belong in the category of activities you do after the doors are open.

Formal Techniques

Two common approaches to collecting primary data on the market are administering surveys and conducting focus groups. The details on how to carry out each type of research are covered in Issue #7 of this series. For now, the important point is that gathering data using these techniques takes time and money, so it is crucial to narrow down just what you are trying to find out. It is a discouraging experience to go to the trouble of surveying your customers or competitors and then discover you don't really have enough information to answer the central question or to make the key decision. Thus, once again, it is all about WHAT you ask, not just who or how you ask.

To drill down to the key strategic question you are trying to answer, ask yourself: Where is my biggest credibility gap? For example, you might have a proven technology for a product that is clearly demanded by customers, but are unsure about the right distribution method. On the other hand, you might have access to a good distribution network, but are unsure whether your innovative product features are going to be well-received. Spend time thinking through the key strategic question that will drive your survey or focus group work. You may need to involve others to help you define the central question. Remember, when doing formal research, you can either get information about a broad range of topics without going into depth, or you can go into depth on just one or two topics; rarely can you achieve both depth and breadth.

Summary

This issue outlines the differences between primary and secondary research and gives you a few places to get started. Because market research is like a treasure hunt, it can be frustrating and time-consuming. It is important to keep the list of "important and urgent" information (things that will change your decisions early in the startup process) posted somewhere prominent, so you can pull yourself back from the inevitable wild goose chases. But good market research usually leads to some unexpected finds as well, so keep an open mind.

Key Meta Resources for Market Research

- **Small Business Administration**
  http://sba.gov/starting/indexresearch.html
  This site lists a few key resources and also link to the on-line reading room maintained by the SBA.

- **Entreworld**
  http://entreworld.org
  Follow the menu to Starting Your Business/Market Evaluation. You'll find a great list of links to all kinds of advice on market research.

- **Small Businesstown.com**
  http://smbtn.com/businessplanguides/bplan3_marketing.shtml
  The free online guides at this site are excellent and provide practical advice along with step-by-step explanations.

- **Food Marketing Institute**
  http://www.fmi.org/facts_figs/resourcelist.htm
  This site has a great list of institutes and associations related to food.

- **Researchinfo.com**
  http://www.researchinfo.com/
  This site has a listing of resources for mar-

ket research, including links to an archive of research software (including software for building questionnaires) and a directory of research companies.

- **Fuld Co**.
  http://www.fuld.com/
  This is a private company that performs competitive intelligence. The website has excellent articles and suggestions about doing competitor research. Check out the list of sources for competitor information.

Tools

- **OffStats**
  http://www.library.auckland.ac.nz/subjects/stats/offstats/
  A free service to help find statistics on the web.

- Here are several sites that allow you to create surveys online:
  - ◊ **iNet Survey** (http://www.inetsurvey.com/)
  - ◊ **Surveykey.com** (http://surveykey.com/)
  - ◊ **Zoomerang** (http://www.zoomerang.com)
  - ◊ **SurveyMonkey.com** (http://www.surveymonkey.com)

Farmers' Markets

http://www.cals.cornell.edu/agfoodcommunity/afs_temp3.cfm?topicID=272
For information on how to get started in farmers' markets, check out this website created by Cornell's Community, Food, and Agriculture Program.

Other

- **New York State Data Center** (Online database) http://www.empire.state.ny.us/nysdc/
  This resource is the product of a cooperative program between the U.S. Bureau of the Census and the New York State Department of Economic Development, Bureau of Economic and Demographic Information. It provides broad access to statistical series for and about New York's population and economy. It is constantly being updated to include new items. It also includes a directory of state data affiliates resources, as well as links to other data resources.

  The population data include census information on towns, cities, and villages and are hence extremely relevant to the local marketing research that the business owner needs to do. Even more valuable are the economic portions, and especially the reports on personal income. All reports can be viewed, or downloaded.

- **More Business**
  http://www.morebusiness.com/getting_started/primer/d992205228.brc
  This site primarily features motivational pieces for the entrepreneur, but has an excellent short item with lots of suggestions for informal selling ideas for startup businesses. It also has an essay on getting free publicity at the related url: http://www.morebusiness.com/getting_started/primer/v4n2.brc.

Issue #7: Doing Market Research -- Part 3: Using Surveys and Focus Groups to Research the Market

This issue is focused specifically on two techniques for primary market research: surveys and focus groups. In previous issues (#4, #5), I emphasized the importance of asking the right question when doing market research. In this issue the discussion is about: 1) how to choose between using a survey or a focus group, 2) the logistics and details of carrying out each type of research, and 3) important resources for entrepreneurs considering primary research.

The Ag- and Food-Based Angle

Many ag- and food-based business are focused on consumer products. In such cases, the use of surveys or focus groups can be extremely useful. If the business involves direct marketing or a farmers' market, you may have an easy forum for conducting customer surveys. If your customers are mainly located in a relatively small geographic region, it may not be too difficult to pull together a group for a survey.

Surveys vs. Focus Groups: What is the Right Method?

In Issue #6 of this series, we discussed resources for market research and the choices between primary and secondary data, and between formal and informal methods. In the case of formal methods, including surveys and focus groups, the case was made that it is very important to focus on WHAT you are trying to find out. Now let's consider the differences between focus groups and surveys to help distinguish WHEN it makes sense to choose each method.

Conducting a survey involves talking to at least dozens and probably hundreds of your customers. A survey can help you gain perspective beyond the small inner group of people that were likely involved in your product development stage. If a survey is conducted properly (see the "Operational Details - Surveys" section for more on this), then you can make generalizations from your findings to a larger population. Because it involves communicating with a relatively large group of randomly selected potential customers, a survey should be used when you need to validate the market.

By contrast, a focus group involves talking to a small group (8-12 people) of highly qualified individuals. By qualified, we mean that they are a subset of your prospective customers who have special knowledge or characteristics. For example, you may want to gather a group of people who you view as potentially ideal customers by virtue of age, family composition, gender or other demographics. Or, you may want to gather a group of industry experts, with special knowledge of your consumer base. Because focus groups involve talking intensively to a small group of people, they should be used to do activities such as brainstorm product features, react to marketing materials and branding approaches, and so on. You can never use focus groups to generalize on a statistical basis. They are used to connect with a small and specialized group and are not necessarily representative of the population as a whole.

Sometimes, if there is adequate time and money, surveys and focus groups are used in conjunction with each other. After conducting focus group work, it may be clear what questions should go on a survey. Or surveys may raise issues that are best addressed in the in-depth format of a focus group.

Operational Details - Surveys

Types of Surveys

The various options for administering surveys are shown on Table 2, which provides details on the pros and cons of each technique along with some tips. In all cases, it is important to remember

Table 2. Various Types of Surveys			
Survey Type	***Pros***	***Cons***	***Tips***
Mail or Written	• Some see them as easy • Don't need to administer one by one • Can target a broad group • Can make use of targeted mailing list	• Can result in low response rate (5-15%) • No chance to clarify, follow up • No controls for accuracy • Expensive	• Unwilling to give up ownership control • Short and clear • Put easy questions first, delicate questions at the end • Test your instrument
E-Mail	• Easy to reach many customers at once	• Hard to get a random sample • Anonymity is an issue	• User-friendliness is a crucial issue • See Additional Resources for free software to design web-based surveys
Phone	• High response rate • Can clarify, follow-up • Can be used for other purposes (networking) • Can reach a large geographic range	• Time intensive for the interviewer • Must be short • More difficult to avoid bias • Requires good phone presence	• Be sure you have a script • Decide ahead of time how you will record • Limit to 5-10 minutes • Start with the easy questions • Identify who you are • Test your instrument
In-depth, in-person	• Can take advantage of key contacts • More opportunity for open-ended questions • Can tailor the interview more to respondent • Get both audio and visual cues about respondent	• Very resource intensive • Usually depends on pre-existing network or contact with respondent	• Use personal contacts and networks to find ideal respondents • Schedule the time beforehand with the respondent • Make sure respondent is aware of the nature of the interview • Choose a non-stressful time of day

that the quality of the survey depends on a list (called a "frame") from which you choose your sample. It is desirable to choose a sample without a built-in bias if at all possible. (Note: It is beyond the scope of this Issue to discuss all the statistical ramifications of sample selection, but a more in-depth discussion is available in the sources listed under Additional Resources). If you have adequate financial resources, consider hiring a market research company to design and administer your survey. Another option is to check with local community colleges or universities to see if there is a program where students in marketing courses help local businesses with survey work.

Designing the Survey

Start with writing down the key strategic question(s) you are trying to answer. The number one mistake people make in writing a survey is that they do not focus carefully on crucial questions, but get lost in detailed inquiries whose answers are not useful to the strategy of the business. Write the **survey questions** to answer the key strategic question(s).

What is a key strategic question? Use two decision rules in finding the right questions and using them to guide your survey design:

- Is the answer to the question crucial to deciding on the business strategy? If so, it qualifies as a key strategic question.

- Is the answer available elsewhere (i.e., without asking survey respondents)? If so, do not use the survey to answer the question. **Note**: You normally do not put key strategic questions directly on your survey. However, it represents the underlying question you are trying to answer. The survey questions break it down to "answerable pieces."

- Start with a list of things you want to know before finalizing your business strategy. To generate the list, ask: "Why do I want to do in this survey?"
  Example: Imagine you are thinking about starting a gift and flower delivery business in a small college town, aimed at the student population. Part of your concept is to deliver flowers on a scheduled basis to individuals who want to spruce up their apartments, dorms, or houses. The "contract" service is a new idea. In addition, you are going to carry a line of beautiful gift items, but you are not sure what to include in your inventory. Before formulating your business strategy, here's a possible list of questions:

  1. How many students are there and what is their purchasing power?
  2. Do students care enough about their surroundings to order flowers?
  3. If they do or would buy flowers, how often would they do so and how much would they pay?
  4. Would buying flowers on a scheduled contract be an appealing concept?
  5. Is there a niche for a gift shop in the town?
  6. What types of gifts does the student population look for?

Now, scan the list to eliminate those questions that can be answered with another data source. For example, number 1) could be answered easily with information available on the local Chamber of Commerce Web Page. Numbers 5)-6) might be investigated more easily by looking at the competition. Next, see if the remaining questions fall into a broad category. For example, in this case, the broader key strategic question is: Will the concept of contract flower delivery work?

Generating Survey Questions

Focusing on the key strategic question, make a list of questions you would need to ask in order to answer the strategic question in a detailed fashion:

- Who buys flowers? Men? Women? What age and student status?
- Why do they buy flowers? Or: Why don't they buy flowers?
- Do the potential customers like the idea of regular flower delivery?
- Where do the potential customers live and with how many other people? Would it be feasible and desirable for roommates to combine resources to buy the contract?
- If the contract idea is appealing, how often would the customer want to buy flowers? What type?

Now write the actual survey questions, following the guidelines below:

- Keep each question clear and simple. Your writing style should be understandable to a wide range of individuals.
- Check the question for potential ambiguities.
- Be as direct as possible, without being offensive. Avoid questions relating to age, occupation, race and gender unless they are crucial to your findings.
- Put the question in a format that is easy to answer by using categories and check-off boxes or answers that can be circled.

- Make sure if you have categories, they are mutually exclusive and collectively exhaustive.
- Don't ask a question that provides useless information. Collectively, the answers should provide you enough information to make a strategic decision. For example, it could help you choose a promotion strategy, design your customer service, or decide for or against a certain market segment.

Designing the Survey Document

The physical (or virtual) document you design as a survey instrument can make or break the success of your survey. The layout must be simple, clear and easily followed (especially if the survey is administered by mail and not in person). For example, your paper document should make use of:

- Large font, easily read;
- CAPS, different fonts, and italics to clarify the question, the instructions, and where and how the responses are to be recorded;
- Lots of white space
- Use of categories to simplify things for the respondent;
- The shorter the survey, the greater the probability that each respondent will answer every question, so choose your questions carefully and design your instrument efficiently!

You should test the survey with a small sample and then do a final review before sending it out or administering it in person.

- Review the key questions you are trying to answer with the survey. Make sure you drill down to the root question.
- Revisit the method you are following to administer the survey. Is there time to mail the survey and get it returned? Will it be effective to do an in-person survey?
- Scrutinize each and every question to make sure it contributes to the key questions of interest. Ask yourself, "When I know the answer to this question, will I have learned something I could not observe by myself and something that is truly important to the issues I have identified?"
- Make sure that the questions are not ambiguous and that you will be able to interpret the results accurately.

Administering the Questionnaire

You must be sure that you ask the "right people" the questions on your survey. Administering the survey on a group of people who would never be in your target market (broadly construed) is a waste of energy. With appropriate funding, you might be able to conduct a random sample. More often, you will be stuck using a "convenient sample." Surveys might be administered on the street where many potential customers pass by, or in front of the competition, in order to catch customers as they exit. Remember, if the sample is too small, or poorly selected, it will hurt the credibility of your plan.

Reporting the Results in Your Business Plan

Many entrepreneurs fail to include the details of the market survey in the plan. The reader will want to know how the survey was administered, how many respondents answered, and some of the demographics of the surveyed population.

- Put key insights and useful graphics in the text of the plan to support your arguments that the market for your product/service is adequate. Consider visual ways (such as pie charts, graphs, and/or tables) to communicate the information to the reader quickly.
- Put the details of the survey (not the surveys themselves, but the spreadsheet with the results) in a well-labeled Appendix and reference it in the text of the plan.
- Remember that if you do not have a random sample, you cannot test hypotheses about the larger population or make infer-

ences in a quantitative way about the larger population. Instead, your survey provides some general feedback from a specific audience you have identified.

Additional Resources for Survey Work

- **Creative Research Systems**
  http://www.surveysystem.com/sdesign.htm
  This is a company specializing in survey design and implementation and its website includes a good basic discussion of survey design, including discussions of how samples can be biased and the pros and cons of various survey techniques.

- **Survival Statistics**
  http://www.statpac.com/surveys/
  This site is actually an advertisement for a book called Survival Statistics, but it includes a wonderful tutorial on all aspects of survey design.

- **Product Development Consulting, Inc.**
  http://www.pdcinc.com/tips/tip01.html
  PDC is a product development consulting company, and this part of their site is dedicated to tips for interviewing.

Here are several sites that allow you to create surveys online:

- **iNet Survey** (http://www.inetsurvey.com/)
- **Surveykey.com** (http://surveykey.com/)
- **Zoomerang** (http://www.zoomerang.com)
- **SurveyMonkey.com** (http://www.surveymonkey.com)

Operational Details - Focus Groups

Defining a Focus Group

A focus group is an approach to market research that involves an in-depth guided discussion with a small number (8-12) participants. Although the findings are not statistically valid, conducting a focus group makes sense when you:

- have a very clear idea who your desired customer is and would benefit from conversation with some ideal customers;
- are refining your product idea and want to have a brainstorming environment;
- are trying to evolve ideas for advertising;
- are trying to surface key issues for your ideal customer and will need to probe to find hidden feelings and motives;
- wish to clarify a niche by asking some "what if" questions.

Focus groups cannot help you quantify market demand or test a hypothesis (from a statistical point of view). Focus groups are held over a 1-2 hour period, and the facilitator's goal is to maximize the benefit of group dynamics. In other words, the focus group should produce different results than you would achieve from talking to each participant individually.

Logistics

As with survey work, the success and value of focus group efforts depend on how you prepare. Clarifying the goal of the focus group is the first step. Selection of participants is important, and typically in order to get 8-12 to participate about 15-20 people should be invited. In most instances, participants are offered an incentive, which at a minimum should be a meal and more often involves a cash payment (perhaps $100 or a gift certificate).

To run the session, one person is designated as a facilitator. The facilitator should have a script prepared and perhaps some introductory materials. It is important to limit the questions or areas of inquiry to about 3-5 items in order to leave time for an in-depth, wide-ranging conversation. It is useful to have participants fill out a general information form as they arrive so you don't have to waste time gathering data during the session. An additional individual should be present to take detailed notes.

If participants are willing, a tape recorder or video tape can be used for documentation. Running a focus group session is an art as much as a science, since the facilitator must listen and guide the conversation and encourage participation from all who are present. This requires a sort of quiet leadership, accompanied by the ability to curtail or control any dominant member of the group who may be closing off responses from others.

In addition to a facilitator, you will need someone to take notes during the experience (it is too hard to facilitate AND take notes). If the participants are willing, you can videorecord or taperecord the session, but it's a judgement call about whether this will constrain the conversation.

Here is a checklist of questions to answer before running a focus group:

- Who belongs in the study?
- How will you get them to participate?
- What are the main issues?
- Who will run the group?
- What questions will be asked?
- How will you record the answers?
- How will you use the answers?
- What will be the limitations of your findings?

Reporting the Results in Your Business Plan

In writing up your focus group results, you should make the composition of the group(s) clear and highlight the issues that were raised. Carefully explain the implications of the results for your marketing or product strategy. As with survey data, you should provide all materials from the focus group and written summary of the session in a labeled appendix that is referenced in the text of your business plan.

Additional Resources for Focus Group Work

- **Center for Urban Transportation Studies**
  http://www.uwm.edu/Dept/CUTS/focus.htm
  This site includes step-by-step instructions, including how to create a discussion guide and tips on selecting participants.

- **National Institute of Health**
  http://irm.cit.nih.gov/itmra/weptest/app_a7.htm
  This site includes very detailed and well organized instructions for conducting an online focus group.

- **Management Assistance Program for Nonprofits**
  http://www.mapnp.org/library/evaluatn/focusgrp.htm
  This site includes step-by-step instructions for carrying out a focus group.

- The Focus Group Research Handbook [Hardcover]
  By: Holly Edmunds, Holly Edmonds

- Focus Groups: A Step-By-Step Guide [Spiral-bound]
  By: Gloria E Bader, Catherine A. Rossi

- The Focus Group : A Strategic Guide to Organizing, Conducting and Analyzing the Focus Group Interview [Hardcover]
  By: Jane Farley Templeton

Issue #8: Putting It All Together... Using What You Know about Yourself and the Market to Formulate Strategy

In this issue, it is assumed that you have gathered lots of information and materials associated with the activities outlined in previous issues of this series. Now it is time to figure out what everything means in terms of formulating a particular strategy for going forward with your business. The components of the Business and Marketing Strategies are outlined and strategy options are discussed.

The Ag- and Food-Based Angle

Strategy is a word associated with warfare. In value-added businesses, the war is over the consumer's dollar and so strategy is focused on meeting customers' needs and wants in a way that is making the best use of the company's strength. For ag- and food-based businesses, the emphasis on the end use may be quite different from what is typical in commodity-based markets more typical of the traditional farm business.

Putting It All Together

Previous issues of this series explained the homework an entrepreneur must do for business planning. In this brief issue, the focus is on what to do with the results of all that work. Not surprisingly, it entails returning to the SWOT analysis (Strengths, Weaknesses, Opportunities, and Threats). Although you may continue to gather material and do research throughout the business planning process, it is important to recognize when you have enough to make your first attempt at formulating an effective strategy.

A starting point is to set aside uninterrupted time (perhaps an hour or two) in a setting where you can spread out all the materials you collected, the drafts you have written, and the results of any primary or secondary research you have conducted. If at all possible, spend some time alone with the materials first in order to organize everything and then begin to involve any partners or advisors you think might be helpful.

As always, stick to management guru Steve Covey's guideline of "keep the end in mind." You are attempting to find a business strategy that uses your strengths to exploit a profitable opportunity, and that avoids your weaknesses and builds a barrier to the threats in the marketplace.

Formulating Strategy

Mission-driven Strategy

Issue #2 of this series emphasized the importance of writing a mission statement and using it to guide your strategy. During your strategy session, be sure to keep the mission statement visible to all involved, and for each strategy ask the qualifying question: "If we follow this strategy, can we achieve our mission?"

Organize Your Materials

Pull out everything you have collected, including any notes, whether they are on a legal pad or on the back of an envelope. Start a list with a simple heading.

Key Finding	Implication for the Business	SWOT

Try to boil down each piece of the material to a key finding or two. For the moment, don't worry about the order of things. For example, perhaps you are looking at a 3-page industry report. But the key finding is: Information technology is transforming the industry by changing the management of the supply channel. Next, articulate what the finding implies for your business. Using the previous example, the implication for the business is: We'll need to implement state-of-the-art technology in order to be an effective part of the supply chain. Finally, mark how the finding fits into the SWOT analysis. Again, using the example, you might say that if your startup team has technological know-how, it is a strength. Or if another leading company has recently implemented proprietary software, you might view that as a threat.

Build Your SWOT

Once the general list is completed, work on sorting the findings and creating a SWOT analysis.

The top two quadrants help you define your approach to the market. The bottom two quadrants remind you that your strategy must be sustainable. What are the barriers to entry? How will you continue to operate in the face of a competitive reaction?

Components of a Business Strategy

Following the framework of Hambrecht and Frederickson, your strategy must answer the following questions:

- **Where am I going to be active?** (which products? market segments? geographic area? core technologies? value-creation strategies?)

- **How am I going to get there?** (developing or growing my own firm? collaborating with others? acquiring other businesses?)

- **How will I win in the marketplace?** (image? customization? price? product features?)

- **What will be my speed and sequence of moves?** (how will I stage my initiatives? what speed of expansion or diversification is appropriate?)

Putting together your business strategy requires thoughtful debate about each of these dimensions. Using the results of your SWOT analysis, go through each question, providing answers in

Strengths	**Opportunities**
Weaknesses	**Threats**

bulleted format if that is easier. When completed, this "homework" will be the backbone of the business strategy section that is the centerpiece of your business plan.

Components of a Marketing Strategy

Once the sustainable competitive advantage is clearly outlined in the business strategy, it is time to turn attention to the marketing strategy. As a guide, consider what is called in marketing theory the "Four Ps" in your business plan (but don't use that term in your business plan because it sounds too much like a textbook).

1. Product (features, benefits, warranties, components, packaging, branding, models, sizes, product life cycles and new product development);
2. Placement (distribution method, sales territory, warehousing fulfillment, electronic download, shipping);
3. Price (price point, discount options, distribution and retailer markups);
4. Promotion (advertising, sales model (personal and/or mass marketing, public relations, brochures, point-of-sale displays).

Although many of the details of the marketing strategy will need to be adjusted once you have some operational experience, you should have an initial plan for each part of the marketing strategy.

Summary

Crafting your Business Strategy (and the related Marketing Strategy) is the central task of your business planning process. Don't be surprised if it is challenging! Most successful entrepreneurs admit that their early strategies were only partly successful and that they had to adjust and revise in response to the realities they found in the marketplace. Nonetheless, a strategy that is mission-driven and based on a thorough review of the SWOT will increase the chances for a startup company to survive.

Additional Resources

- **The Strategy-Focused Organization.** Kaplan, Robert S. and David P. Norton. Harvard Business School Press, 2001.

- **"Are You Sure You Have a Strategy?"** Hambrick, Donald C. and James W. Fredrickson. *The Academy of Management Executive*. November 2001. 15:4. pp. 48-59.

- **MeansBusiness.com** http://www.strategyandcompetitionbooks.com/Strategy-and-Competition-Books/All-the-Right-Moves.htm
  The link listed here is to a resource that is part of the website created by a company called MeansBusiness. The site allows you to purchase, in an ala carte mode, portions of material from the popular business press. The resource associated with the above link references sections of a book called *All the Right Moves, A Guide to Crafting Breakthrough Strategy*, by Constantinos Markides.

Issue #9: Can You Make Money? The Financials for Your Plan

This issue emphasizes the importance of creating financials "from the bottom up," or basing them on details at the consumer end of the equation and not starting with revenue targets. It also explains the homework needed before a full set of financials are created (for example, estimating sales, calculating breakeven). Finally, it explains the details of what belongs in the written plan and discusses expectations of investors.

Ag- and Food-Based Angle

It is not unusual for an ag-based business to be derived from a traditional farm operation. As such, it might be relatively easy to finance a new venture using current farm assets. In turn, such internal financing may make it tempting to skip a careful analysis of how and when the startup business will become profitable. However, given the opportunity costs of capital (i.e., the money could be in a risk-free investment environment, drawing modest interest rates or re-invested in the current business), it is very important to create a financial model of the startup business that will help define the level of profitability and any cash flow issues that must be accommodated.

Financials for Startups - Smoke and Mirrors?

As soon as an entrepreneur starts to work on the financials for a new venture, it becomes apparent how much is not known. How many customers can be expected? How often will they buy? Which products at what rate? How will costs of production vary over the first few years? The answers to most of these questions for a startup business owner are simply educated guesses. Of course, it is desirable to show that a company will have profits over time, so the financial statements for a startup are usually crafted in a way that makes the future look rosy. That's why investors often accuse startups of "smoke and mirrors" when it comes to the financials. That leads to the question of why even bother with financials? The answer is: because it is about the process, not necessarily the spreadsheets themselves. Even though a good financial model is based on estimates, this Issue is focused on how to go beyond smoke and mirrors to come up with your financial statements.

Bottom-up Financials

Financials are called "top-down" when you pick a target level of sales or profitability and then backwards engineer the underlying data until it adds up to the target. Financials are called "bottom-up" when you start with the underlying assumptions and then build the financial model around those clearly stated assumptions. If work on the financial part of the business plan is done from the bottom-up, then there is value to the process of creating the statements. Because the bottom-up approach begins with estimating sales, the entrepreneur must ponder (and perhaps do additional research) on the customer base. Calculating sales also puts you in touch with the realities of queuing issues (when demand is bunched up at certain times of the day or week), seasonality, and possible segmentation of the marketplace. It requires you to think through the smallest details of each sale (when, where, how much, how often) and then to think about what the aggregate picture looks like.

On the costs side, a bottom-up approach requires careful research and documentation. Calling vendors, getting price quotes, forecasting changes -- all these activities help the entrepreneur have a more realistic idea of what it will cost to produce and sell a service or product. In addition, estimating costs involves understanding what people are needed to run the business and what payroll costs will be. Even for experienced business owners, the cost side can hold some surprises once you start from the bottom up.

Scope of This Issue

It is beyond the scope of this issue to describe each building block of the financial statements and how they fit together in terms of spreadsheets and the final statements that go in the plan. However, there are excellent sources that include such step-by-step directions. In addition, commercial software programs (such as BizPlan Pro) are designed to help with the actual mechanics of the financial section of the business plan. Unless you have appropriate experience and credentials in the area of finance, you should check your work with a good accountant before finalizing the business plan. The remainder of this issue will help outline key components of the financial section, how to write about financials, and mistakes to avoid in working on this part of the business plan.

Getting Ready to Build the Financial Model

The financial model of your business tells the economic story of your business. Some entrepreneurs think that investors focus only on profitability. The truth is that bankers, investors, and potential partners/alliances are looking for whether your model for making money is logical and well researched. The following discussion describes a few key components, including why they are important, how to do the calculations, and suggestions for how to get started.

1. Figuring out Startup Costs

- **Why it is Important:** The estimate of startup costs defines how much money must be raised to open the doors of the business.

- **How it is Calculated:** Opening a business for the first time requires certain outlays of cash which make up the bulk of your start-up costs. You can find checklists in various resources (see Additional Resources), which includes such items as:

◊ Payroll expenses (prior to startup)
◊ Legal/professional fees
◊ Remodeling
◊ Licenses/permits
◊ Equipment
◊ Insurance
◊ Equipment and supplies
◊ Advertising/promotions
◊ Rent and utilities.

Notice that these are all payments for items before the first day the door is opened, and you'll need to tailor the list to your particular company. Many experts (including the Small Business Administration) also recommend that you have on hand at least three months' worth of operating costs, which constitute a contingency fund. If your sales cycle turns out to be longer than anticipated, or other unexpected surprises drain your cash flow, the contingency fund is intended to give you staying power. It is notable that many new businesses start out without enough funding, which means that success can be as fatal as failure, since in a cash flow crunch it's possible to have paying customers lined up but no cash to create the product or service.

- **Getting Started:** Make a list of costs that relate to your particular business. Research costs and keep track of sources. The cost of most items on the startup list are fairly easy to quantify, but calculating the contingency funds depends on figuring out your operating budget.

2. Estimating Sales

- **Why it is Important:** Your sales estimates will receive a lot of scrutiny. After all, they are the basis for many other calculations. Investors like to see sales estimates that start from the bottom-up (how many customers per day? per week? per month?

purchasing which products?) so they understand your customer profile and whether you have a well-researched knowledge of your core customers.

- **How it is Calculated:** To get total sales, you will aggregate the purchases by each customer over a given period of time.

- **Getting Started:** Obviously you need to work on this from both sides: How many customers are there? How much does each one purchase?

- **How Many Customers?** Based on your market research, start by defining the customer profile, roughly estimating how many customers fall into each broad category. Decide the geographic scope of your marketplace and estimate the total number of each type of customers in the relevant area. Finally, and this is the big step, calculate what share of the market you think you can capture. Again, your market research provides the baseline for this work.

- **How Much does Each One Purchase?** Again, drawing from your market research (see Issues #5-#7), begin with a description (or even a diagram if that helps) of the buying process. Do people buy the product once a day? Once a year? Do they go to a store? Buy online? Out of catalogues? If you have many products or services, group them into broad categories, or estimate a "typical basket" of products or services. Keep track of your assumptions, as you will be using them in writing up your plan.

  Putting this together looks like this:

  # customer type 1 *x* $$ of purchases *x* n time periods PLUS # customer type 2 *x* $ # of purchases *x* n time periods and so on.

  Although only the aggregate number goes in your business plan, building up the sales estimate from a realistic starting point will increase your credibility with the investor. The background spreadsheets go in an Appendix, and in your narrative you should explain how you went about estimating sales. You should estimate monthly sales for the first year, and then make quarterly or annual estimates depending on what your bank or investor requires.

3. Estimating the Cost of Goods Sold

- **Why it is Important:** The Cost of Goods Sold is used in calculating breakeven levels, since it reflects the cost of producing the product.

  The following relationship exists between sales revenue, gross margin (or gross profit), and cost of goods sold:

  Sales Revenue - Cost of Goods Sold = Gross Margin (amount available to pay fixed costs and return a profit).

- **How it is Calculated:** There are two methods.

  ◊ The **unit costing method**: Cost of goods = # units sold *x* cost per unit

  ◊ The **percentage cost method**, used in retail businesses where there are standard markups: Cost of goods sold = selling price *x* (100% - % gross margin desired), where gross margin = 100% - percentage of markup.

- **Getting Started:** If you are using the unit costing method, be sure to include all of the costs of producing the good. Consult the Additional Resources section for tips on where to look for industry standards.

4. Calculating Breakeven

- **Why it is Important:** Every business owner needs to understand the point at which revenues will cover all expenses. Investors will examine both the level of the breakeven and the timing (how many months or years before breakeven is reached).

- **How it is Calculated:** Breakeven can be calculated in terms of units or revenues:

  Breakeven units = Fixed Costs/(Unit Price - Unit Cost)

  Breakeven Revenue = Fixed Costs/Gross Margin

- **Getting Started:** When calculating fixed costs, include overhead expenses that don't change with the level of production (for example, utilities and telephone). The variable cost includes those costs which vary directly with sales. Consult the Additional Resources section for places you can look for industry standards on gross margin.

5. Estimating the Operating Budget

Before generating the necessary financial statements that are discussed in the section below, an operating budget must be created. Researching the estimates that are used in your operating budget is a critical aspect of getting ready to build the financial model. There are many worksheets available (see Additional Resources) to help you get started on this task, but the usefulness of your financials depends on the credibility of the estimates.

6. Forecasting Cash Flow

If a business does not have the cash to pay salaries, purchase raw materials, and cover its regular bills, the owner will be faced with closing the doors, even if the prospect of sales is very positive. Hence the expression: cash flow is king. Although this saying has become a cliché, we find in talking with entrepreneurs it remains one of the top challenges of running a business. Understanding the realities of how cash flows in and out of the business may be the most important part of the work you do on the financial model. The reality for many small businesses is that expenses will have to be paid before revenues are flowing in. How will this be handled in the business? What sources of cash are available and when will they be tapped? These are the fundamental questions answered in your cash flow statement. The Business Services site from BC-Canada has an excellent discussion on how you can get started estimating cash flow, starting with revenues and then working on disbursements (see Additional Resources).

Components of the Financial Model and Where It Goes In the Business Plan

Once the homework described above is complete, you are ready to generate the information that actually goes into the business plan. Following the section on Plan of Operations (see Issue #11), your plan will discuss the Funding Strategy and Financial Statements. Here are some of the issues discussed in covering the Financial Statements:

- **Sources and Uses of Funds**
  In a brief format, the plan shows where money is coming from (personal stake, equity investment, bank loans, etc.) and how it will be used. This is a checkpoint to make sure that all planned uses for funding are covered by some source of funding.

- **Discussion of Risks**
  It is appropriate somewhere in the financial discussion to address the risks facing the business. The American Express site (see Additional Resources) lists some of the potential risks to think about:

◊ Competitors cut prices
◊ Loss of a primary client
◊ Failure to meet sales projections.

Discuss only the risks you feel are central for your business and the provisions you have (such as your contingency fund) to deal with them.

- **Narrating the Data in the Plan and Discussing the Assumptions**
  The next part of the narrative should tell which financial statements and documents are located in the body of the plan and which are located in the appendix. For example:

  "The projected annual financial statements for the first three years of operation begin on page *xx*. The financial statements are followed by a breakeven analysis for the company and graphs showing... (etc). In the Financial Appendix, beginning on page *yy*, we have included a list of our underlying assumptions for our financial projections, a sales forecast schedule, a personnel cost schedule, and a detailed set of financial statements. The detailed financial statements show the first year by month and an annual summary for years 2 and 3."

  The fundamental assumptions underlying the plan should be discussed as well. The appendix should include a very detailed set of notes to accompany your financial model, but the narrative should address what you see as the central assumptions on which the model turns. If you do any sensitivity analysis (changing around key assumptions to see the results), the outcome should be presented.

Profitability Milestones and Discussion of Breakeven Analysis

When narrating the "financial story" of your business, think about how you can link certain milestones with your funding requests. For example, it is clear that some period of funding is needed to meet expenses until the breakeven point is reached. The breakeven can be discussed in words, but a graph is often used to portray the point in time when the business crosses the breakeven point. Beyond the initial need to carry the business through the breakeven point, the funding needed for growth should be synchronized with hitting certain milestones. In his book "A Good Hard Kick in the Ass," Rob Adams calls these milestones "value inflection points." For example, early on, two important inflection points are market validation and proof of a profitable business model. Regardless of the size of your project, your plan for funding must make sense in terms of how the business is expected to perform over time.

Pro-forma Statements

The financial statements that belong in the body of the plan, include the:

- **Income Statement** (also called the Profit and Loss Statement - shows the ability of the business to generate cash);
- **Balance Sheet** (shows the net worth of the business).

Cash Flow

These statements should be monthly or quarterly for the first year and annual from then on, depending on what is required by the bank or investor. If your plan is strictly for in-house use, be sure you do monthly projections for the first year so you have a better feel for whether you have enough resources to deal with any cash flow issues and that you have a realistic idea of profitability and breakeven.

Typical Mistakes

In reviewing business plans, working with entrepreneurs and talking with funders, we have experienced some of the following as common mistakes:

- Financials are not derived from the bottom up.
- Financials do not reflect statements made elsewhere in the plan (e.g. "we will succeed through exceptional customer service" but low-paid employees, no incentive and no training costs).
- No discussion of sales growth (simply following a linear growth pattern without explanation).
- Too much detail is included in the body of the plan (dozens of pages of spreadsheets are a turnoff for most readers - if supporting spreadsheets are important, include them in an appendix).
- Unrealistic return on investment for the industry (without any explanation or justification).
- Inadequate level of detail about assumptions and research.
- No allowance for a "warm-up" or lag period for revenues at the beginning of the business.
- No benchmarking of industry standards (see http://www.census.gov/csd/bes/).
- No allowance for contingency (SBA recommends 3 months worth of operating expenditures).
- Statements are amateurish - never checked out by business accountant .

Additional Resources

- **IBM's Guide to Financials**
  http://www.prars.com/ibm/ibmframe.html
  If you want to learn how to interpret financial reports, this site has a good tutorial.

- **Business Services, BC-Canada**
  http://www.smallbusinessbc.ca/workshop/cashflow.html
  This site includes an excellent discussion of how to create your cash flow statement, including step-by-step instructions on how to estimate sales. The description includes many numerical examples if you need help understanding any of the terms used in this Issue. You can also download a publication called Business Planning and Financial Forecasting from this related url: http://www.smallbusinessbc.ca/pdf/bpff2002.pdf

- **BizPlanit**
  http://bizplanit.com/vplan/financial/basics.html
  In the section called Virtual Business Plan, this site features a concise description of what goes into the financial section of the business plan and a list of common mistakes made by entrepreneurs.

- **American Express**
  http://home3.americanexpress.com/smallbusiness/Tool/biz_plan/fin/index.asp
  This site discusses the following aspects of the financials: risks, cash flow statement, balance sheet, income statement, and funding request. Each section includes an explanation of the topic and tips for preparation.

- **Business Owner's Toolkit**
  http://www.toolkit.cch.com/tools/buspln_m.asp
  This site features examples of financials from different kinds of businesses.

- **Small Business Administration**
  http://sba.gov/starting/suchecklist.html
  A worksheet for estimating startup costs is included in this site. You can also find a complete downloadable startup kit that has valuable worksheets and explanation about

business planning at: http://www.sba.gov/gopher/Business-Development/Business-Initiatives-Education-Training/Business-Plan/

- **U.S. Census Bureau**
  http://www.census.gov/csd/ace/
  http://www.census.gov/csd/bes/
  These two sites have government-tracked data regarding business expenses (assets and expenditures).

- **A Good Hard Kick in the Ass**
  Rob Adams. Crown Business Publisher, 2002
  Although this book is focused on high-tech, high-growth companies, there are many concepts and aspects of advice that are applicable to businesses of any size. Chapter Four discusses funding, and even if you need only hundreds of dollars for a business (not thousands or millions), it is still valid to think in terms of achieving milestones (what he calls value inflection points) and understanding the importance of cash flow.

Issue #10: Funding Strategies - Shaking the Money Tree

Issue #9 was focused on helping the entrepreneur determine the **amount** of startup financing needed, and this issue continues the discussion by describing various **sources** of financing and how funding is typically **staged** over the life of the business. This issue is intended to acquaint the reader with the differences between loans and equity financing and sources for each type of financing.

Ag and Food-Based Angle

Most ag- and food-based businesses have products or services that are consumer-based and tied somehow to a farm business. As such, there may be a ready source (asset-based borrowing) of funding. Growth prospects vary, but many ag-based entrepreneurs have as their mission to create and grow healthy businesses to support a household or two, rather than creating a high-growth, venture-funded business. So it is important to identify various sources of money for ag- and food-based companies, aside from the venture funding that was so highly publicized in the dot-com era.

Debt vs. Equity

Beginning entrepreneurs often ask me if a bank will fund their businesses. My answer is that the bank may loan money (asset-backed loans) for your operation, but they are not in the investment business. So a starting point for our discussion is to distinguish between using debt (a loan to be repaid) and equity to get funds together for your business. It helps if we view the situation as a spectrum (ignoring instruments that combine debt/equity). Table 3 presents some of the important differences between debt and equity.

One thing that clearly emerges from looking at the table is that because equity investors are

Table 3. Comparing Characteristics of Debt and Equity Funding

Characteristic	***Debt***	***Equity***
Repayment terms	Fixed periodic repayment with interest	Repayment in future; set by negotiation; no repayment in case of failure (hence, higher risk)
Rate of return expected	Typically set in relationship to the primary lending rate	Depends on source • Family – highly negotiable • Community venture funds (20-50%) • Venture capitalists – double-digit returns expected, ranging from 50-100% for most aggressive investors
Frequency of payment	Typically monthly	Negotiable – deferred
On balance sheet	Liability	Stockholder's equity
Cost to entrepreneur	Comes from on-going cash flow, but is a deductible expense	Entrepreneur gives up ownership and therefore a portion of long-term income growth prospects
Participation in business	Minimal as long as payments are met	Variable – high in the case of angels and venture capitalists
Risk to source	Legal obligation to make payment	Risk shared by investor
Ownership implications	All ownership retained	Give up some portion of ownership

absorbing more risk, they expect a higher return and more participation in the business. In contrast, using debt to start a business is dependent on cash flow issues, especially early in the business.

Funding Strategies and Sources

Your choice of funding strategy depends on your mission and business strategy. A "lifelong small business" owner who wants to grow the business just big enough to support the households involved is likely to need cash to start or grow the operation, but is often unwilling to give up ownership in return. In addition, the business will not generate the rapid growth in income that outside investors require, so a "lifelong small business" would have trouble attracting big outside investors who expect a return in the double digits on their money. In such a case it is important to identify alternative means for raising money that do not involve diluting your equity in the business. For example, the business might be funded with an SBA-backed loan or by borrowing money from an existing business or from friends and family. In such a case it is crucial to understand the bank's expectations and/or how to structure borrowing to avoid problems. By contrast, "high-growth" businesses are aimed at large markets and must be funded adequately for scaling up the business. For high-growth ag- or food-based enterprise owners, it will be important to understand the steps in financing the business, the sources and tradeoffs of where to obtain growth capital, and the basics of venture-backed funding.

The reality is that most small businesses go through several stages of business funding. At each stage, you will consider the amount of funding needed, whether you are eligible for borrowing (usually requires an asset), whether you have achieved the right milestones and have the right profile for investors, and how much ownership you want to retain.

Next, let's examine three aspects of each type of financing: 1) the sources available, 2) expectations of the source, and 3) any special issues important to the startup entrepreneur.

Debt Financing

Sources

Sources for debt financing include:

- Commercial Banks
- Asset based lenders
- Factoring
- Trade credit
- Equipment suppliers
- Commercial finance companies
- Savings and Loan associations
- Government-backed lending (such as SBA and other government programs - see Additional Resources)
- Credit cards.

Expectations of Bankers

You probably have some kind of bank account and like the rest of us, you count on your bank to keep that money safe. Keep that perspective in mind when considering the expectations of a banker approaching a small business loan. The banker is responsible for choosing lending opportunities that are safe, or have a very high probability of repayment. Thus, the primary focus of examining the loan will be on the abilities of the manager/owner to run a profitable business and the ability of the business to generate enough cash flow to make regular payments. The New York Federal Reserve (see Additional Resources) describes this as the five Cs:

- **Special Issues**
  - ◊ Credit card debt
    Credit cards are a very expensive source of funds for a new business. They only make sense if there is a relatively short selling cycle and borrowing is covering a small gap in cash flow. Even so, remember that in most cases you will be paying double-digit interest rates.

Table 4. The Five Cs of Credit Application		
Criterion	***Description***	***What the banker looks at***

Capacity	Most critical – how will you repay the loan	- cash flow from business
		- timing of repayment
		- probability of successful repayment, based on:
		  - previous personal credit history
		  - previous business credit history
		- contingent sources of repayment

Character	Impression you make on the lender (this is subjective) with regard to trustworthiness	- review your educational background and business experience - references required regarding you as an individual, the business and your employees
Capital	Personal funds invested in the business (an indicator of how much you have at risk in the event of business failure)	- expect contributions from your assets - want to see that you are willing to take personal financial risk
Collateral	Guarantees, forms of security in the event of failure	- collateral expected - personal guarantee often required
Conditions	Intended purpose of loan (working capital, additional assets or inventory)	- also looks at the current economy and your industry for signs of health
Based on Federal Reserve Bank of New York website: The Credit Process, A Guide for Small Business Owners (http://www.ny.frb.org/pihome/addpub/credit.html#Lenders).		

◊ SBA Loans
Although the rules are outlined on the Small Business Administration website, http://www.sba.gov/financing/fr7aloan.html#general), to understand whether your business is eligible for an SBA-backed loan, it makes sense to visit with a local bank or credit union that is familiar with the SBA program.

◊ Staging of Debt Financing
The New York Federal Reserve Bank (see Additional Resources) organizes businesses into four categories and gives advice about appropriate funding sources, as shown in Table 5.

- **Common Errors When Borrowers Approach A Bank**
Bankers tell me that often business owners approaching them make some of the following mistakes:

◊ Are not prepared even with a simple written business plan with financials that have been reviewed by a qualified accountant;
◊ Don't realize that the management team and repayment ability are the top considerations;
◊ Mix up short-term and long-term debt -- most loans are asset-based and the life of the loan must coincide with a reasonable lifespan of the asset;
◊ No collateral or are unaware they will be asked to make a personal guarantee;
◊ Think they can borrow 100% of value of asset (usually 60-75%).

Table 5. Stages of Business and Appropriate Sources of Debt Financing		
Stage	***Description of Business and Milestones***	
Stage one	Startups	Informal investors, such as: • friends or relatives, partners • local development corporations • state and local governments offering low-interest micro-loans • private foundations offering program-related investments • credit unions featuring small business lending • universities with targeted research and development funds
Stage two	Businesses have business plans and product samples but no revenue	Same as stage one
Stage three	Businesses have full business plans and pilot programs in place	Commercial bank or other traditional lender
Stage four	Businesses have been in operation for some time and have documented revenues and expenses	Same as three

Equity Financing

Sources

Kevin McGovern, lawyer, entrepreneurship expert, and principal of McGovern Capital LLC, always tells me to think about funding in concentric circles. "You start with sources closest to you and work your way outwards," according to Kevin. The further you go from the center, the more control you give up, the more formal your plan is expected to be, and the higher rate of return is expected. Figure 1 is an example of the places you might look for financing from equity sources and how they differ in terms of ties to the founder and expectations regarding returns.

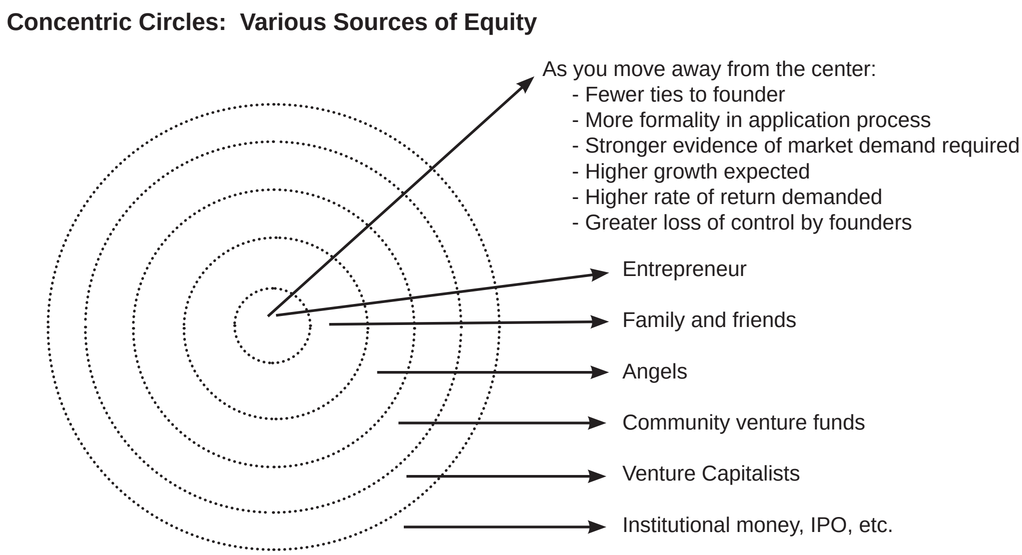
Personal Equity

The first place to look for funding is always the entrepreneur's own pocket. If your new business is a spin-off of an existing farm business, you may have the capacity to invest a fair amount. I am often asked "What percent of total funding should come from my pocket?" The answer depends both on your ability to put cash into the business and on your willingness to share ownership. If you want other investors to join, they will be expecting you to risk a reasonable amount of your own savings and wealth in the business. It is not so much the amount as it relates to the company, but more whether you have enough at stake to work diligently at making the business profitable.

Family and Friends

It is common for family and friends to be another source of funding for new companies. If you pursue this source, I urge you to make a formal agreement (simple, but FORMAL) so that expectations are clear on the investor side. I have heard too many stories about families that didn't realize that if the business went under they would not be able to recover even the principal they contributed to the company. I have also heard stories of entrepreneurs whose family or friends wanted more involvement than was expected. Get it down on paper.

Figure 2. Characteristics of Various Sources of Equity



Angel Investors

So called "angels" are wealthy individuals who enjoy investing in new companies. It is a diverse group, and although they have high incomes they may not necessarily be multi-millionaires. Typically angel investors are found through networking. The Additional Resources section has more information about on-line communities of angels.

Community Development Venture Funds

A relatively recent development in some communities is the establishment of community development venture funds. Typically, such funds look for local investments linked to employment and economic development. In the Additional Resources section, you'll find some examples. The best approach is to check your local region for such funds.

Venture Capitalists

There has been a lot of change in the venture community over the past decade. During the dot. com era, funds swelled and venture companies started doing larger, later-stage investments. The downturn in the economy and the failure of many Internet-based companies has resulted in a shake-out of companies. It is unlikely that in the startup phase venture capitalists will be interested in your project. However, many of their sites have good information about business planning and financial models.

What Equity Investors Expect

The first circles in the concentric circle model (yourself, friends and family) may not have well-specified expectations (although I encourage you to articulate them if at all possible). However, the rest of the players in the equity markets have very specific expectations.

The number one consideration of equity investors is the quality of the management team. That surprises many entrepreneurs, who expect investors to be more focused on the idea. See Issue #4 for details on how to build and present the individual or team who provided primary leadership to your company.

The second consideration is the size of the potential market. At the extreme, venture funding is only available for companies that have the potential for a huge market. Another way to look at it is the business must be "scalable" to a national and/or global marketplace. The further out from the center of the circle, the higher return is expected. Equity investors are buying into your business, and in the process they assume some of the risks of the business. Accordingly, they expect very high returns.

Special Issues

Staging of Equity Investment

As has been mentioned elsewhere in this series, the staging of your business involves a series of milestones (product development, acquiring customers, obtaining revenues, achieving growth targets). Equity funding should be coordinated with these milestones. Although you may hear the advice that it is better to try and raise one large amount rather than many small equity investors, the reality of who and how much is likely to be dictated by the stage of your company. You'll find entrepreneurs and experts who say not to give up any of your equity, and others who argue that as long as the pie gets large enough it doesn't matter what part of it you sell to investors. In the end, deciding on the pace and extent of equity investment is a highly personal decision.

How Much Ownership Do You Give Up?

One very difficult area for new businesses seeking investment is figuring out for a given equity investment how much of the company ownership is shared. Although the mathematical approach is to look at some sort of discounted cash flow model of expected revenues, the truth is that valuation is an art or a science and depends primarily on negotiation with your investors. The investor will be motivated to place a low valuation on the company so as to gain as much ownership as possible for every dollar invested. The entrepreneur, of course, is motivated to place a high valuation on the business.

Summary

Deciding where and how to fund your business is intricately linked to your business strategy. If you have a business that is a cash cow from the beginning, you may be able to afford to borrow money rather than give up equity. On the other hand, if your company requires a large upfront investment, has the potential for growth, and will not have adequate cash flow to meet loan repayments, you may be faced with seeking equity investment. I hope this issue is helpful in orienting some of your thinking as you plan for your own individual case.

Additional Resources

- **Cornell's Agriculture-Based Economic & Community Development**
  http://www.cals.cornell.edu/agfoodcommunity/afs_temp3.cfm?topicID=351
  This Cornell site lists funding opportunities for ag-based businesses. Examples are:

  ◊ **Grow New York Funds**
  http://www.agmkt.state.ny.us/GNYRFP.html
  This site tells about a special project for "agribusinesses in New York State" which are eligible for funding under certain conditions.

- **ACE-Net**
  http://acenet.csusb.edu/
  ACE-Net.org, Inc., incorporated in the State of Delaware, is pursuing 501(c)(3) status to conduct networking, educational, training and research activities for increasing access to the entrepreneurial capital marketplace. This site features on-line matching of businesses with angels. It is difficult to discern with any of these matching services what the success rate is, so I would be reluctant to rely only on virtual networks.

- **Community Development Venture Capital Alliance**
  http://www.cdvca.org/
  A good example of a fund with a community development spin, the CDVCA site features resources for entrepreneurs and the ability to join the virtual community or "shop" your business.

Issue #11: Writing Your Business Plan

This issue uses all the work discussed in Issues 1-10 and focuses on putting together the actual document. Based on seeing hundreds of plans reviewed by experts and investors, I give you advice on what readers like to see in terms of the look and feel of the document and the content of each section. A checklist is provided at the end for reviewing your plan once it is put together.

The Written Plan -- What Size? What Shape?

What comes after you settle on your mission and complete your homework? Do you need a large formal business plan? A one-page summary? The decision depends on how you plan to use the written document. If your plan is primarily for internal use, you may find it useful to write only a skeleton version of the plan. If you are using the plan to raise money, then more careful thought should be put into the physical document.

Even though funding sources do expect to see a written plan, there is some question about just what that document should look like. There are many sample plans available online, but one must ask the question about whether they are truly valid examples of good plans for funded companies. If you had an ideal plan that had been funded, you would be unlikely to agree to having it published on the Internet! Thus, the question remains, what about the physical document?

In his provocative book *Burn Your Business Plan*, Dave Gumpert states: "... in the recent years, an important perception gap has grown between what entrepreneurs are worrying about, and spending time on, and what investors really care about and consider in their investment decisions. Entrepreneurs have increasingly made the business plan and end in itself, and all the while investors have increasingly come to view the business plan as merely one part of a much larger process, and an ever-less-important one at that."

If we take this comment to heart, it means that it is extremely important to understand, for any specific context, what is expected in terms of the written business plan. The best way to find out is to ask the bank, private investor, or venture capitalist exactly what format is desirable. If you have a good relationship with the funding source, then you might even ask for an example of a plan that has been funded. Alternatively, offer three versions of your plan: a one-page summary, a 3-5 page letter format, or a 15-20 page business plan complete with financials.

Whatever size or shape you pick for your business plan, aim for a flexible format and presentation so that you can easily make changes. A business plan must be considered a "work in progress". We recommend against using a business plan template from commercial software if you are using the plan to seek funding. (Note: we do recommend such software for working on your financials - see Issues #9 and #10.) The reasoning is that investors can easily spot a plan that follows one of the standard templates, and it will give the impression that you have taken a cookie cutter approach. Finally, regardless of the size of your plan, you need to have the same information and background work completed. In fact, the most difficult plan to write is actually a smaller document, because it requires careful communication and very effective presentation to be credible and clear within such narrow boundaries.

Writing Your Business Plan

You can find a dozen examples of "standard outlines" for business plans (see, for example, those available at bplans.com or bizplanit.com, two of our favorite business plan sites). However, the truth is that no agreed-upon standard exists. The nature and purpose of your plan will dictate the order of presentation and only you can determine what will be most effective in any particular context. Below, we outline the elements that should be in your plan, regardless of the exact outline you follow.

1. Executive Summary

Definition

The Executive summary is a 1-2 page synthesis of your entire plan. It appears as the very first part of the narrative and is the front door to your plan. For many investors it may be the only thing they read.

Purpose

If you cannot articulate in a single page the focus of your business, your sustainable competitive advantage, the excellence of your management team, a proven market need, the signs of profitability and your funding request, then you can forget about the remaining 15 to 20 pages. Nobody who reads business plans on a regular basis will go beyond the Executive Summary if that single page is not convincing.

To avoid common mistakes, be sure to:

- Proofread your work for spelling and/or grammatical mistakes; careless errors communicate to the investor that you cannot pay attention to detail. One investor told me that he considers the plan an "ambassador for the entrepreneur."
- Keep the summary short; three pages is the absolute maximum, one-page is the ideal.
- Include a clear statement of what you need from the investors, how the money will be used, and what the investor can expect in terms of exit events.
- Organize your summary in short paragraphs, with concise language, and including bullets.
- Think about the summary from the reader's perspective; make sure the order of discussion is logical.

2. Table of Contents

Definition

The Table of Contents is a navigational tool for the plan, including numbering of all sections and appendices.

Purpose

Most readers of business plans will not simply start reading at the beginning and go all the way through the plan in order. Each reader has his/her own style and approach to reviewing business plans. Some may start with the Management Team section, while others quickly flip to the Financials. The Table of Contents will help the investor quickly find the sections of most interest to him or her.

To avoid common mistakes, be sure to:

- Keep the Table of Contents simple and clear with an easy-to-read format.
- Coordinate the headings in the Table of Contents with any tabs marking various sections.
- Number the pages for all sections, including the appendices.

3. Mission Statement

Definition

A Mission Statement is a short declaration of the business's "reason for being." It should portray a clear sense of the customer base, and the sustainable competitive advantage. The Mission Statement typically has a tone that is high-energy yet businesslike.

Purpose

Putting the Mission Statement at the beginning of the business plan is a way of setting the tone for the rest of the document. It is unlikely that an investor will spend a lot of time examining the Mission Statement, but it is still important because it shows whether the entrepreneur has a clear and focused vision for the business.

To avoid common mistakes, be sure to:

- Avoid using too much jargon, sometimes called "management speak" or "Dilbertisms" (see Issue No. 2 of this series for more details about how to write the Mission Statement).
- Keep the Mission Statement relatively short (half a page or so).
- Check the tone to make sure it is business-like (not necessarily humorless) even if your business has a social mission as well as a profit mission.

For more details on the importance of the Mission Statement to the business planning process, see Issue #2 of this series.

4. Business Description (also known as Business Profile)

Definition

Think of the Business Description as the "who, what, where, and why" section of the plan. It describes the company's legal entity and includes an explanation of any linkages between the new business and any existing businesses. In addition, it describes the location and the various products and services offered by the startups as well as explaining the customer base and the revenue model. The Business Description also showcases any proprietary technology and refers to relevant appendices if there are details about patent or intellectual property issues.

Purpose

After reading the Business Description, the investor should have a clear understanding of where the business is located, who its customers are and what product or service lines are offered. It helps the reader understand how the company will make money.

To avoid common mistakes, be sure to:

- Include the specific location of the startup operation (or explain where operations are being handled if it is a "virtual company").
- Paint a visual picture of how and why customers buy the products or services.
- Avoid excessive operational details; those belong in the Plan of Operations.
- Use bullet points and short paragraphs to break up the narrative.

5. Management Team

Definition

This section of the business plan informs the reader about the core leadership team for the business. It includes a narrative paragraph for each member of the management team, and may also include information about any advisors or special employees important to the startup of the business.

Purpose

Fundamentally, anyone who evaluates your business idea actually will be looking at the people behind the idea. The Management section of the plan is designed to convince the investor or prospective partner that the team has all the crucial elements to execute the business. Thus, it is important to show qualities of leadership, domain expertise and the ability to persevere in periods of high stress and/or difficulty.

To avoid common mistakes, be sure to:

- Include a short paragraph for each member of the team, placing the corresponding resumes in a labeled appendix.
- Stay focused on the relevant background of each team player, showing domain expertise, so-called "execution intelligence" (see Issue #4), qualities of perseverance and leadership.
- Avoid using hype; stick to proving competence by reporting experience and accomplishments.

For more details on the importance of the management team to the business planning process, see Issue #4 of this series.

6. Market Analysis

Definition

This section of the plan consists of your analyses of the industry, competitor, and customer.

Purpose

As a whole, the Market Analysis is designed to document the fact that there is a demonstrable need for your product and that industry and competitive forces are well understood. The investor wants to see: 1) both numerical and qualitative proof that consumers not only desire but are willing and able to pay for your product or service, 2) that competitors cannot easily replicate your proposed advantage, and 3) that you are starting a business that can be successful given the specific trends and general health of your industry.

To avoid common mistakes, be sure to:

- Report only relevant details of your research, leaving any additional findings for the appendices (note: to determine what is relevant, be guided by your SWOT analysis, which does not directly appear anywhere in your plan but should be embedded in the content).
- Relate the findings of each subsection to your specific business idea and approach (for example, you may want to have a textbox at the end of each section labeled "implications for the business" in which you summarize what your findings imply about your startup strategy).
- Use graphs, tables, and bullet points to break up the narrative and to clarify your key points.
- Show proof that you have spoken directly to your customers.
- Use a mixture of quantitative data and specific detail (for example, you might indicate the quantitative size of the industry and the number of consumers in your region and then go on to cite some details of specific conversations with consumers).
- When you are reporting on questionnaires or focus groups, keep only the relevant information in the narrative, saving the specific details for an appendix.

For more details on the importance of the Market Analysis to the business planning process, see Issues #3, #5, #6, #7, and #8 of this series.

7. Business and Marketing Strategies

Definition

The Business Strategy and Marketing Strategy are two related discussions, each of which is clearly linked to the market analysis. **The Business Strategy** is a straightforward discussion of the following questions: Where will the business be active? How is the business to be launched? How will the company win in the marketplace? What is the staging and sequencing of the market moves? The Business Strategy should be only a page or two in length since it is a high-level discussion of your plan for conquering the market. The Marketing Strategy section is longer, since the discussion covers price, product, place, and promotion strategies. (Note: For more information on the business and marketing strategies, see Issue #8 of this series.)

Purpose

The job of this section of your plan is to articulate clearly and convincingly your sustainable competitive advantage. Think of this as the centerpiece of the planning process. All your research and homework should lead directly to an understanding of how to tackle the market successfully, in the near term and over the long haul.

To avoid common mistakes, be sure to:

- Make a clear connection between your market analysis and the direction of your strategy.
- Emphasize how you, in particular, are set up to succeed in the business (that is, what resources, technology, networks, or other key resources do you control? What

barriers to entry can you erect?)

- Be clear that you understand that marketing strategy means more than just promotion.
- In the Marketing Strategy, keep your suggestions based on well researched options.
- Address your strategy regarding the Internet.

For more details on the importance of evolving a strategy in the business planning process, see Issue #8 of this series.

8. Plan of Operations (also called Operations Plan)

Definition

This part of the plan reports on important operational details. The content varies tremendously depending on the business. For service businesses, it is essential to explain customer acquisition, while for product oriented companies it is essential to explain who will supply the raw materials and how you will distribute the production output. If your business includes a strategy focused on logistics or customer service, you must show clearly in the Plan of Operations how you will execute these strategies.

Purpose

When investors read the Plan of Operations, they are seeking signs that you understand the operational realities of starting the company. Both on the input and output sides, it must be clear that you have well established channels. In addition, it is a checkpoint to see if you have facilities and processes well matched to the size and location of your initial target market. It can also be an opportunity to envision how the business can be scaled over time.

To avoid common mistakes, be sure to:

- Include a diagram of the flow of operations.
- Be specific about important details but do not waste time and space on areas that do not matter (for example, young entrepreneurs often put in elaborate hierarchical charts about management and employees when it is too early in the life of the business to have a complicated personnel structure).
- Include a layout of any retail operations.
- Discuss milestones and a timeline.

9. Funding plan

Definition

The funding plan narrates the execution milestones of the company and the accompanying funding goals that are required for growth. It shows the sources and uses of funds, and explains the current request for any loans or equity investment.

Purpose

This section of the business plan lays the groundwork for discussions between the entrepreneur and anyone else involved in financing the business. For example, it can tell the bank what loans are needed and what collateral is being offered. It can tell the equity investor, in general terms, what is being requested and what exit events can be expected. For more detail on structuring the Funding Plan for the business, see Issue #10 of this series.

To avoid common mistakes, be sure to:

- Indicate that you are raising enough money to start the business including an adequate safety net but without an unrealistic amount of extra cash.
- Be clear on who is lending money versus who is an equity investor (see Issue #10).
- Include monthly details for the first year and quarterly or annual reporting for the second and third years.
- Verify your work with an accountant or credible financial adviser.

For more details on the importance of the funding plan to the business planning process, see Issue #10 of this series.

10. Financial Analysis

Definition

The financial section of your plan reports your startup costs, breakeven analysis, and pro forma statements. It is accompanied by a short narrative explaining important assumptions you are making in your estimate of sales and pointing out key issues regarding profitability, for example when you first become profitable as a company and how you grow over the first three to five years.

Purpose

Although the financials for a new business are often considered to be "smoke and mirrors," they are an important basis for discussions with investors or bankers. What the funding community is looking for is a sign that you understand the financial realities of your business from the bottom up. For example, do you have realistic expenses listed for your startup costs and operating costs? Are your cash reserves big enough to survive dry spells due to seasonality or faulty assumptions regarding cash flow? The financials should make it possible to discuss "what if " scenarios so that if you are wrong about any major assumptions the implications for the business will be clear. (Note: there is great debate among professionals about whether or not to include what is called a scenario analysis, or a sensitivity analysis. Such an analysis is designed to show what happens under various assumptions, sometimes called the best case, least case, and most likely case. Check with whoever will be reading your plan to see what expectations they have about this type of additional analysis.)

To avoid common mistakes, be sure to:

- Justify your sales estimates and pattern of growth.
- Include adequate discussion and documentation of your cost estimates.
- Keep the narrative focused on key issues (sources and uses of funds, key assumptions, breakeven analysis, profitability milestones).
- Address the primary risks facing the business and how you are financially prepared to weather the potential storm(s).
- Inform investors, if you have any, of how they will eventually have an opportunity to "cash out" (the so-called "exit strategy").

For more details on the importance of the financial analysis to the business planning process, see Issue #9 of this series.

11. Appendices

Definition

The appendices to a business plan often include the details on financial assumptions, any additional information needed about market research, and perhaps information on patents or intellectual property rights or other details specific to certain businesses.

Purpose

Appendices can provide credibility by showing the degree of research done by the entrepreneur. They also help provide an outlet for material that would be too long to include in the narrative but that the entrepreneur wants to include for the reader. If such information is lengthy, consider simply bringing it along to any meeting or discussion regarding the plan.

To avoid common mistakes, be sure to:

- Label and number your appendices.
- Refer to every appendix somewhere in the narrative of the business plan.
- Be extremely careful about confidentiality issues when reporting on customer, industry, or competitor intelligence.
- Include enough information on survey or focus group work that the reader knows how and where the material was administered and what the results were.

- Ask your perspective reader if they would prefer to have the appendices bound separately from the plan itself.

Final Tips on Assembly of the Plan

It is tempting in this age of computers and color printers to create a very elegant look for your business plan. Is so easy to do graphics and color, use fancy fonts, and make use of specialized papers. However, the most important thing about your plan is the content, not the appearance. If faced with the choice, spend your time proofreading, organizing, and editing the contents rather than designing a fancy cover for the plan.

It is important for the plan to have a neat, businesslike appearance. This can be achieved very easily simply by following a clear format, using short, concise paragraphs, and by including bullet points and graphics that help to break up the text. If you bind the report, be sure that it can open to a flat position. This might seem like a picky detail, but I have heard repeatedly from the investor community that they will toss a plan into the garbage if it is not easy for them to lay it open on the table.

It is reasonable to create several versions of your document. For example, you might want to have an e-mail version, a 15-page version, and the full document version. Once you begin sharing the plan with others, expect that you will need to make changes and evolve the document. Because it is so dynamic, keep the plan in a format that is flexible for revision purposes.

Summary

When your plan is finished, here's a final checklist:

Figure 3.

Writing and Presentation

- ☐ Is the plan concise and clearly written (about 15-20 pages for the main narrative)?
- ☐ Is the language appropriate (i.e., professional and not too casual or wrong tone)?
- ☐ Is the plan free of hype (e.g., using words such as "extensive" and "extraordinary")?
- ☐ Is the spelling correct?
- ☐ Is the plan free of grammatical errors?
- ☐ Has the plan been proofread carefully?
- ☐ Is the plan internally consistent?
- ☐ Is it "easy to read" with short, concise paragraphs, logical wording and clear ideas?
- ☐ Are the pages numbered?
- ☐ Are the appendices clearly labeled with numbered pages for easy access?
- ☐ Are visuals used effectively (instead of litany of statistics)?

Content The final plan…

- ☐ has a convincing portrayal of the management team as the right people to execute the business plan
- ☐ describes a marketable idea that comes across in a credible way
- ☐ includes a discussion of a business strategy that is in line with the mission statement
- ☐ shows how the product or service adds value for the customer
- ☐ Includes credible evidence that the market wants/needs the product
- ☐ shows an understanding of the competition and how it relates to the niche being filled
- ☐ explains the sustainable competitive advantage
- ☐ describes the important elements of the plan of operation
- ☐ includes an appropriate discussion of the financials
- ☐ has a financing plan that makes sense
- ☐ has consistent and complete financials that are in synch with the narrative of the plan
- ☐ describes defensible strategy, including: economic logic, arenas, vehicles, differentiators, staging

If you can check these boxes, you have a solid plan, but remember it is still a work in progress. You'll need a wide variety of versions, ranging from a "pitch book" of presentation slides (if you are approaching private equity investors) to a full-blown printed copy with all the accompanying appendices. Business planning is a process, not just a published report with a fancy cover. But once you are done assembling your plan, you'll be well prepared for talking with people (investors, customers, partners) about the business and your strategies for success.

Additional Resources

- **Successful Business Planning in Thirty Days**
  Peter J. Patsula, ed. William Nowik
  http://www.smbtn.com/businessplan30days/
  Patsula has assembled an impressive website (called Small Businesstown.com) of resources for business planning. We like his many guidebooks (click the vertical tab marked "Guides" for a list), which cover an amazing range of practical topics faced by a new business. His book is also a very practical approach, especially designed to be down-to-earth and task-oriented.

- **Burn Your Business Plan**
  David E. Gumpert, Lauson Publishing Co., 2002
  Despite the title, Gumpert is in favor of business planning (just not obsessing about the document). This volume includes a good discussion of the things that investors like to see in entrepreneurial startups. The author discusses how to put together a presentation (even before finishing your plan), creating hard-hitting financials, using publicity to attract investor attention, and building a website to demonstrate your business model.

- **Bizplanit**
  http://www.bizplanit.com/vplan.html
  We love the Virtual Plan section of this website for a consulting group that helps entrepreneurs craft business plans. In the Virtual Plan, the authors define terms, point out basics, and provide information about common mistakes. The format is concise and the information is excellent.

- **Bplans.com**
  http://bplans.com
  This site markets BizPlan Pro and other related tools but contains a lot of wonderful free resources as well. There is a free on-line copy of *Hurdle: The Book on Business Planning*, as well as many sample plans (although all the plans seem to be created with the BizPlan template.)

OTHER A.E.M. EXTENSION BULLETINS

EB No	Title	Fee (if applicable)	Author(s)
2007-07	Dairy Farm Business Summary, Northern Hudson Region, 2006	($12.00)	Conneman, G., Putnam, L., Wickswat, C., Buxton, S., Smith, R. and J. Karszes
2007-06	Dairy Farm Business Summary, Western and Central Plain Region, 2006	($12.00)	Knoblauch, W., Putnam, L., Karszes, J., Hanchar, J., Moag, G., Getty, K. and Z. Waite
2007-05	Dairy Farm Business Summary, New York Large Herd Farms, 300 Cows or Larger, 2006	($16.00)	Karszes, J., Knoblauch, W. and L. Putnam
2007-04	A Bridge Across the Generations by New York FarmLink (video) 26:44	($9.99)	Staehr, A.
2007-03	An Overview of Dairy Marketing Cooperatives Operating in New York State		Henehan, B.
2007-02	Selected Economic Aspects of Water Quality Trading: A Primer and Interpretive Literature Review		Boisvert, R., Poe, G. and Y. Sado
2007-01	Smart Marketing: A Compilation of Smart Marketing Articles, January 2004 - October 2006		W. Uva
2006-20	New York Economic Handbook 2007	($7.00)	Extension Staff
2006-19	Lake Erie Grape Farm Cost Survey, 2001-2005		Shaffer, B. and G. White
2006-18	Dairy Farm Business Summary, New York Dairy Farm Renters, 2005	($16.00)	Knoblauch, W. and L. Putnam
2006-17	Farm Family Transitions	($15.00)	Richards, S. and G. Conneman
2006-16	Estate Planning for Farm Families	($15.00)	Richards, S.

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