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Introduction

Importance of a Business Plan

Why a plan? Because any activity with an objective needs one. This is so even when things are sure to go as "planned". In a situation where one has to deal with uncertainties (like in a business), planning helps minimize excess costs or excessive divergence from the desired result. For the entrepreneur, remember that:

- Luck isn't all there is to a business' success.
- You don't engage in a business without any reason. There's always a goal to be reached. Well, the business plan is your roadmap to that goal.
- A plan will tell the businessman whether or not the enterprise is working for him, rather than holding him captive.
- A plan establishes benchmarks in performance. When the business is under-performing, the businessman will know.
- The systematic and formal process involved in its preparation will prevent good ideas from lying dormant, or being completely forgotten.
- Once finished, it will serve as a manual for operations.
- Preparing a business plan does not entail much additional work. It simply formalizes what data and ideas the entrepreneur already has.
- When studying a successful business in hindsight, the oft-mentioned word is adequate planning.

Who Else Will Benefit From Your Business Plan?

- Operations. Now that we've mentioned it, every component of a business requires some form of planning. Plans for marketing, finance, production and hiring will all emanate from the business plan.
- Affiliates and Related Parties. Your affiliated businesses can adjust to, or profit from, your business' future situation.
- Suppliers. Knowing what your plans are will help suppliers ensure a proper and timely delivery of essential inputs to your business
- Your Customers. Customers don't buy accidentally. They too plan ahead. Ask them what they think of your business plan and it will save you a lot of marketing work in the future.
- Prospective Investors and Partners. They only see the "now". The plan will inform them of your business' history, present condition and future prospects. It will facilitate the often tedious chore of "due diligence".
- Incidentally, a well-researched and presented business plan is one the best medium for corporate advertising. Except for bottom line figures, there's no better way to convince prospective shareholders and funders.
- Bankers. You don't need to agonize on how your various expenditures will be funded. Tell them your plans and let them design the various modes of financing – well into the future.
- Competitors? Of course they'll benefit! Hide it from them. They can know all there is to know about your business at present and it won't matter much. Let them peek into your business plan and they'll stay ahead forever!

Explanation for the Plan Format

This planning kit was designed to facilitate the preparation of a business plan. We chose a tabular format for simplicity. It is not a writing exercise. What the reader expects to see is a well-researched and well-laid out scheme to generate income. Reserve paragraphs and text for explaining points in relation to the tabulated information.

Most of the terms used are generic, allowing even non-business course graduates to comprehend the format requirements. In addition, the tabular format follows a standard sequence. This will make it easy for third parties such as investors, bankers, lawyers and regulators to pick out relevant information.

The tables given are generally those for manufacturing operations. To adapt the format to a specific business, users are free to add, omit or modify components.

Executive Summary

Business Profile

Give the Business name, address and contact media (telephone, fax, e-mail address). A start-up business may not have all details required. However, provide available details of the plan. This includes the business' legal form (example: single proprietorship).

For both start-ups ongoing businesses, briefly describe the primary mission statement. The mission statement need not be specific but must be short and easy to grasp. It must also be realistic. Explain what the business does, for whom and why. Also, mention where the business is and where it wants to be in the future.

Example of a general mission statement:

> To become a leading internet service provider not just in the Philippines but in the Asia-Pacific region.

Or, it could focus on basic, time-defined objectives:

- To partly meet the growing demand for internet access by small businesses and individuals wanting to set up a home-office.
- To begin operations by 2001 with an acceptable capital structure
- To achieve sustained annual profits beginning in 2002
- To realize payback on investments by 2005

Key business activities, products and services must be spelled out directly. Some businesses may be so specialized and obscure that it will require pages to explain fully. For brevity, just state how the business generates revenues, why customers require your products/services and how you plan to serve your customers.

Lastly, mention items of concern such as the current status of the industry or a critical aspect of the operation.

Key Management Personnel

Get full value from your key man's credentials. If a director or manager has distinguished him/herself in business or in other fields like public service and the academe, say so. Give the names and addresses of the business' key managers and advisors. State each one's role, experience and degree of ownership/control in the business.

Business Environment I

Trends in the Market and the Economy

For start-up businesses, the two important questions that an industry study must answer are:

1) **Is it easy to enter the industry as a competitor?**

2) **Is it easy to exit once you're in?**

The factors that could influence your answer to question #1 are Government regulations, large capital requirement, a fully served market and undue advantages enjoyed by the erstwhile major players. For question #2, factors could include difficulty in disposing of acquired assets or doing so will jeopardize affiliated businesses.

Other than knowing what barriers to entry and exit there are, give other issues that will have an impact on your business' profitability and growth. State how you plan to respond to these issues.

Market Segmentation

Companies do not sell products and services of uniform price and quality. This price-quality variance comes about when businesses of different sizes and capabilities attempt to differentiate themselves from the rest of the players. Knowing how your market is segmented is the first major step towards a successfully realized business plan.

Having done that, know what type of customer avails of the goods and services in your chosen segment(s). And then comes the hard part. Try to estimate the size of your segment in terms of units sold and in Pesos.

Sales and Marketing Plan I

Planned Differentiation from competitors

In the table titled “Planned Differentiation from Competitors”, the first column asks you to enumerate the major competitors in the various segments. Describe whether or not that competitor is the sole player (monopolistic), one of a few (oligopolistic), or if the competition is leveled and fair (many buyers-many sellers).

In the second and third column, enter available data regarding each competitor. When available, mention figures like total asset value, annual sales and percentage to total sales within the segment. Give the main reason why that competitor has attained the status of market leader within that specific segment.

Lastly, explain how you plan to differentiate your product or service from that competitor (last column). While the usual differentiation techniques revolve around price, quality and type of customer, businesses can also differentiate themselves through things like mode of delivery, allied products, geography and financing.

Customer Analysis and Selling Strategy

The next table (Customer Analysis and Selling Strategy) asks how buyers behave within your chosen segment. For each product or service, explain the type of buyers (by age, gender, income, profession or location). Mention also their main buying criteria. Finally, write your expected sales revenues and the selling strategy that will enable you to attain those revenue levels.

Sales and Marketing Plan II

Advertising and Promotion

The first table asks for your advertising and promotion strategy. As an example, a frozen meat manufacturer will have as his advertising strategy various media to educate and inform the public on matters like freshness, hygiene, and buying convenience. His strategy in promoting his product will probably include: 1) print ads on high-end weekly publications and trade magazines; 2) add-on features to other high-end products like credit and discount cards; and 3) sales discounts, whether progressive (dependent on buying frequency) or for stock reduction (large discount on the last 30 minutes of each selling day).

Projected Sales

This will now summarize the results of your sales strategy. Show how your sales will behave in the future, in terms of units sold and Peso value.

What will cause sales to grow or contract in the future? External factors might include: increased income, population growth, price changes, new products and substitutes. Internal factors involved may include pricing, quality, related product/service offerings and credit terms.

<u>Are the above projections optimistic? Realistic? Pessimistic?</u>

Operating Plan I

Location of Facilities

When describing your operations, it’s not enough to describe the physical layout. Explain the “why’s”. For instance, your decision to invest in parking area for customers is rooted on your marketing plan. Or maybe, your decision to locate the factory near the supply of raw materials instead of near the buyers is due to cost considerations.

Leasehold Improvements

Make this table as comprehensive as possible. Describe the status of your present fixed assets, their value net of depreciation and shortcomings (if any). And then, list down your planned acquisitions. Mention the relevance of each, the latest date when it can be acquired, cost to acquire and planned financing.

Operating Plan II

Suppliers and Sources

For each supplier, give the product offering, the normal volume of deliveries and the selling terms. Mention other peculiarities of each supplier (other businesses served, condonation of past due payables, etc.)

Since suppliers are vital to your day-to-day operations, you must consider not just cost but also contingencies. What if your only supplier experiences work stoppage? What if it decides to sell to someone else? Are your alternative suppliers still cost-efficient?

Support Services

For support services, explain the nature and importance of each. Are they absolutely necessary? Which service can be dispensed with during hard times?

Human Resources Plan

Manpower Planning

This first table serves two purposes. First, it will inform other people how you invested in manpower resources in order to realize your business goals. The second is to quantify cost of investment in manpower. Salaries and wages are a major component of recurring expenses.

Administration and Policy

Enumerate your policies for human resources. Make sure they are consistent with the overall objective.

Profitability – The Income Statement

The income statement form given follows the standard format prescribed for manufacturing operations. The following are guidelines for accuracy in the preparation of an income statement:

1. Cost of Goods Sold (CGS) are the costs needed to sell a given number of units in one period. They include expenses directly related to production (direct labor, fuel and raw materials) and certain overhead costs during manufacturing. CGS generally varies, depending on level of sales. Depreciation of machinery and equipment is included here.

   Sales less CGS is gross profit. When gross profit is taken as a percentage of sales, it is called gross margin. This gross margin should remain constant over a period of 2-4 years. Changes in gross margin can be very significant. It is here wherein you must focus your cost-reduction efforts.

2. Operating expenses are mostly fixed expenses, meaning they stay constant regardless of sales levels. They include salaries of office employees, rent, utilities, fees, depreciation of office equipment, etc. While operating expenses may not be as significant as CGS, they remain fixed even if there are no sales during a period. That is why, <u>your break-even sales is where gross profits are equal to total operating expenses</u>.

3. When projecting interest charges, take the average of the beginning and ending bank loans for a period and apply the estimated interest charges. Include the probable amount of additional bank charges.

4. Always assume full application of income taxes. 35% of income after operating interest the general amount withheld.

Cash Budget

Perhaps you will notice that, when you're auditing a past accounting period, your cash balance changed but not in line with net income. The reason is simple. The income statement does not capture all cash receipts and disbursements during a period. To fully capture your cash transactions in a given period, you need to do a cash budget, both for past periods and for the future. Past period reports are called cash flow reports since they terminate with the actual ending cash level. In preparing a future cash budget, one can estimate his business' financing requirements for the near- to medium-term.

(in thousands of Pesos)	1999 (ACTUAL)	2000 (FORECAST)	2001 (FORECAST)
Cash Receipts from Sales	1,000	1,200	1,300
Add: Collections from past credit sales	200	300	400
Add: Other cash receipts for the Period (dividends from affiliates, interest income, sale of assets, etc.)	100	50	0
= TOTAL CASH RECEIPTS (TCR)	1,300	1,550	1,700
Cash payment for labor, fuel, raw material	600	636	650
Rent	160	175	185
Selling Expenses	100	134	145
Utilities	30	32	35
Payment for Past Purchases on Credit	25	27	30
Payment on Loan Principal	0	0	0
Interest Payments	50	60	65
Professional Fees	12	15	18
Personal Withdrawals	100	100	100
Purchase of Machinery, Equipment, Vehicles	200	400	500
Other Purchases, Payments, Investments	0	0	0
= TOTAL CASH DISBURSEMENTS (TCD)	1,277	1,579	1,728
= TCR – TCD = SURPLUS (DEFICIT)	23	(29)	(28)
Add: Beginning Cash	5	28	5
Add: Cash from borrowings, additional capital	0	6	28
= ENDING CASH	28	5	5

Explanation

It is important to mention the first assumption for the above example: the minimum required cash balance for any period. In the example, it is 5,000 pesos. Also, receipts from additional borrowings/equity are not included in total cash receipts but reserved for determining the “bridge” amount (second to the last line).

As seen for the year 1999, total cash receipts exceeded total cash disbursements by 23,000 Pesos. Because of this, the ending cash level in 1999 was 28,000 Pesos; well past the minimum amount. For year 2,000, however, disbursements are projected to exceed receipts by 29,000. Given the beginning cash level of 28,000 and the required 5,000 at the end, the business has to source at lease 6,000 in year 2,000.

Having done that for 2,000, move on to 2,001. This time, disbursements will exceed receipts by 28,000. Given the beginning balance of 5,000 the business must borrow at least 28,000 to cover the deficit for that year and still have enough cash for the coming year.

Inputs to the Balance Sheet

Given the difficulties involved in the preparation of a correct balance sheet, particularly for small businesses, the plan format waives this as a requirement. On the other hand, third parties will require, at the least, information that will allow them to simulate a business’ financial condition (i.e., a balance sheet). The table given lists the minimum amount of information needed to do this. Users are advised to expand this list to include items like non-trade receivables, borrowings/lending to affiliates, deferred earnings and charges, etc.

Performance Indicators

It is difficult to establish performance indicators while still at the planning stage. The reason is difficulty in obtaining standards from existing players. Once in operation, past years’ indicators may be used for comparison.

After doing sales comparisons, analyze the business’ financial performance using the suggested ratios. Comparison may be done with those of competitors or, the business’ ratios in the previous years.

1. Net Profit Over Sales – Also called the net margin, it simply presents the net profit as a percentage of sales. This ratio should be treated as a “sudden death” indicator for a given period. Negative net margins (meaning a loss for that period) must be fully explained. Readers will also expect a reassurance from the businessman that a loss condition will be reversed in the future.

2. Gross Profit Over Sales (Gross Margin) – As mentioned earlier, the gross margin is one of the most important measures for a business’ profitability. This margin must be constantly monitored and compared in two ways: 1) with past year’s figure and 2) with available data within the market.

3. Net Profit Over Investments – Also called ROI, this is a rough measure of the returns from an business’ fixed assets. The argument here is that the acquisition of fixed assets such as machinery is what drives a company’s profitability. But since we know that cash position is often the primary concern for small businesses, we advise users to limit the use of this ratio for gauging planned capital expenditures.

4. Current Ratio – The ratio of current assets to current liabilities is a quick measure of a company’s liquidity for the near-term. Banks often require borrowers to maintain a certain current ratio level as part of their loan conditions. For financial planning, however, we advise businessmen to assess their liquidity in a more direct way (i.e. cash budgeting).

5. Average Age of Receivables, Inventories and Payables. These figures can be very useful for management. Knowing the average age of receivables, inventories and payables allows one to estimate cash surpluses and shortfalls.

   Still with financial projection, knowing the average age of an account is not sufficient. You must estimate the probable level at the end of the accounting period. To do this, monitor past ending levels as follows:

   a. percentage of ending receivables to sales – use this percentage to estimate ending receivables in the future given the forecasted level of sales.

   b. percentage of ending inventory to cost of goods sold – since CGS will be forecasted along with sales, use the percentage to forecast ending inventory.

   c. Percentage of ending trade payables to cost of goods sold – apply the percentage for estimating the ending level of trade payables.

6. Debt to Equity – Another “sudden death” indicator; the ratio of total liabilities to net worth is the quickest way to estimate long-term solvency and capacity to pay loan obligations. Monitor your business’ ratio and compare it not just to your competitors’ but to the level prescribed by banks and other lenders.

7. Interest Coverage – A more immediate indicator of debt payment capacity; your business’ interest coverage simply states how much income for the period is available to pay current interest charges.

Long-range Planning

The two tables given in this section ask for specific objectives for the business within a set time frame. A business’ future objectives is the main component of this plan. Besides these, the format already provides tools to determine the viability of those objectives. To recap:

1. Growth targets for sales and earnings must be determined and presented in the marketing and financial plan.

2. The physical means by which growth and other objectives will be attained must be spelled out in the operating, human resources and financial sections of the plan.

3. Anticipate the business’ cash position through budgeting. External funds should be applied prudently to cover shortfalls. Monitor the business’ financial indicators to prevent excess borrowing.

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