UPLAND DEVELOPMENT PROGRAMME IN SOUTHERN MINDANAO (UDP)

ENTERPRISE DEVELOPMENT MANUAL

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Enterprise development

1. Introduction

Enterprises can take many forms. They can be agricultural production enterprises, processing, manufacturing or service enterprises. While the mechanics of the enterprise may differ there are certain basic business principles which are basic to all enterprises.

The complexity of enterprises can vary considerably and this will influence the detail and complexity of planning necessary, the managerial and other business skills required, the capital requirements and a number of other factors. But the fundamental development process will be the same, just the detail will differ.

Officers involved with enterprise development need a framework within which to operate. This manual sets out to provide such a framework to guide them through the process.

In addition to advising on the mechanics of the development of an enterprise, enterprise development officers need to be able to make some assessment of business plans and of the people who are making them. Different types of businesses operating in different environments require different business skills and often different personal characteristics. The enterprise development officer or the people s/he is working with are very often the first people ideas are bounced off. They should have some insight into what is necessary to make an enterprise successful. This manual endeavours to help them in this area by giving an insight into the different generic business strategies that an enterprise might adopt and explaining the different requirements of these different strategic approaches.

It is said that there are only two certainties in this life - death and taxes. In enterprise development there are certainly no guarantees of success but there are steps which can be taken which can increase the chances of success or reduce the likely hood of failure. There are also warning signs of impending trouble and sometimes costly mistakes can be avoided. This manual outlines the steps in the business planning process which if followed are no guarantee of success but may sound the alarm bells.

Different sections are devoted to different aspects of the enterprise development process. It starts out to define what we mean by enterprise development and goes on to deal with an overview of the whole enterprise planning process and outlines the steps to be followed. It then deals with each of these in more detail.

2. An Overview of Enterprise Development

2.1. What is enterprise development

An enterprise is described as "***a business undertaking assuming risk for the sake of profit***" and from this comes the term entrepreneur - a person who organises, operates and assumes the risk of a business venture.

Development is the process of ***"bringing into being or growing the enterprise"***

In this programme we are primarily concerned with ***rural enterprise development.***

Rural is defined as ***of or pertaining to the country as opposed to the city; of or pertaining to people who live in the country; of or pertaining to farming, agriculture.***

It should be pointed out however that the same guiding principles govern enterprise development whether it is urban or rural. There may be issues peculiar to each situation but the basic business principles will be the same.

2.2. Enterprise development planning

Because we cannot control all factors in the environment in which a business operates, enterprise development carries an element of risk. The very definition of the word enterprise tells us that there is risk in enterprise development. Some enterprises will carry a higher degree of risk than others. By careful planning, good management and control systems and contingency planning risk can be reduced but never eliminated. The more information we have available about the technology required, market etc. the better the decision process should be and the lower the risk.

Therefore, the entrepreneur, when planning to develop a new or existing enterprise should go through a planning process. The culmination of this planning process should be the production of the *business plan.*

While the preparation of a strategic and business plan is no guarantee of success it is difficult to see how a business can succeed without one. Obviously there are many reasons why businesses fail and it is impossible to anticipate or foresee them all but there are a number of things that should be borne in mind when preparing a business strategy in order to reduce the likely hood of failure. Equally there are a number of characteristics which are found in many successful businesses which should also serve as a model.

2.3. The business plan

A business plan is, or should be a realistic view of the expectations and long-term objectives for an established business or new venture. It provides the framework within which the enterprise must operate and, ultimately, succeed or fail. While a comprehensive plan is no guarantee of success the absence of one is a pretty sure guarantee of failure.

The complexity of a business plan will vary depending on the scale of the enterprise. Large complex enterprises will require a high level and very detailed planning. Smaller enterprises will obviously require less detailed planning. But even micro enterprises such as an individual small farm will still require some level of planning. In the case of farm enterprises we call them *farm plans* but they still are business plans and will contain some or all of the same basic elements.

However, most plans follow a well-tried and tested structure and general advice on preparing a plan is universally applicable. This paper therefore sets out to outline a generic business planning process which can be adapted for specific enterprises and situations.

The preparation of a written business plan of course is not and end in itself, but is an important intermediate step in the overall objective of achieving the targets set out in the plan.

A formal business plan is just as important for an established business, irrespective of its size, as it is for a start-up. For an established business it also demonstrates that careful consideration has been given to the business's development, and for a start-up it shows that the entrepreneur has done his or her homework.

An important element of the planning process is that in the course of preparing the plan there will be some questions that can not be answered at least with certainty. The planning process does however highlight these areas and will alert management to the need to pay particular attention to them in the future. General Dwight Eisenhower, the Supreme Commander of the Allies in Europe during World War II and later U.S. President, once said *"it is not the plan that is important but the planning"*.

The planning process forces managers or entrepreneurs to understand more clearly what they want to achieve, and how and when they can do it. Even if no external support is needed, a business plan can play a vital role in helping to avoid mistakes or recognise hidden opportunities.

For many entrepreneurs and planners, the process of planning (thinking, discussing, researching and analysing) is just as, or even more, useful than the final plan. So, even if you don't need a formal plan, think carefully about going through the planning process. It could be enormously beneficial to your business. During this planning phase opportunities may be identified for adding value or possible pitfalls spotted.

So even in very small enterprises the planning process should be followed.

The plan serves a number of functions:

- Helps management to clarify and to focus on issues which will affect their business' development and prospects.
- Provides a logical framework within which a business can develop and pursue business strategies over the next three to five years.
- Serves as a basis for discussion with third parties such as shareholders, agencies, banks, investors etc.
- Offers a benchmark against which actual performance can be measured and reviewed.

2.4. Strategic plan

For a business to plan and operate effectively it must have a basic business strategy which will provide the framework within which it will plan and operate. Before the development and production of a business plan the entrepreneur must have a strategic plan. This strategic plan will address such issues as:

- ***What*** is to be accomplished
- ***Where*** it will focus
- ***How*** resources will be deployed to achieve the strategic objectives

2.5. Skills in rural areas

In the rural areas in which UDP will operate the level of business skills is low. The steps and processes outlined below might be regarded as unnecessarily complicated, detailed or tedious. There might be an inclination to suspend or dispense with the normal planning process and business principles. This would be a mistake. Obviously the more complex the enterprise the greater the level of detail and planning required and small rural enterprise plans may be somewhat shorter than for other enterprises. But every business should have a clear idea of what it is about and where it wants to go (strategy), how it is going to do it (business plan) and how it will deal with unexpected developments in its operating environment (contingency planning).

In fact the lower the business skills levels the greater the risks of failure therefore the greater the need for careful planning.

This manual sets out:

- to define what we mean by enterprise development
- outline the strategic planning process
- describe various generic business strategies
- provide guidelines:
  - on preparing a strategic plan
  - preparing business plans
  - financial planning
  - managing working capital
  - cash flows
  - generating and developing business ideas
  - preparing
    - marketing plans
    - production plans
    - budgets
- contingency plans

In the following sections, we discuss the preparation of a strategic plan as well as present ideas for preparing outline and detailed business plans. Bearing all this in mind an outline of a business plan is presented below. Where there are suggestions for the length of the different sections, one page does not necessarily mean that it must be a full page.

Certain words or phrases, such as vision and mission, have increasingly found there way into business literature and culture. The reader is urged not to be unduly concerned or overawed by these terms. Very often it is just putting a name on something we have always known intuitively, even if we could not or did not bother to put a name on it.

2.6. The stages in the planning process

A number of stages will be gone through in the planning process. It is useful to first start out with a short strategic plan to be followed by a more detailed business plan. In the preparation of the business plan a number of steps should follow in order to come up with a logical plan on which to base investment decisions.

Strategic plan
Market research
Finance

3. Strategic Planning

Strategic Planning

3.1. Introduction

For a business to plan and operate effectively it must have a basic business strategy which will provide the framework within which it will plan and operate.

Boyd and Walker define a **strategy** as:
A fundamental pattern of present and planned objectives, resource deployments, and interactions of an organisation with markets, competitors and other environmental factors.

This definition suggests that a strategy should specify:

- ***What*** is to be accomplished
- ***Where*** it will focus
- ***How*** resources will be deployed to achieve the strategic objectives

A well defined strategy will have five components:

- **Scope:** this refers to such things as the number of products and the market segments the business will operate in
- **Goals and objectives:** this refers to desired levels of accomplishment on one or more performance dimensions
- **Resource deployments:** every organisation has limited resources, therefore you must decide how resources are to be obtained and allocated
- **Identification of a sustainable competitive advantage:** how is the organisation going to compete? Can it gain some advantage over the competition or at least be as competitive?
- **Synergy:** synergy is more important in large organisations but even in very small businesses there should be synergy between the objectives and the organisations particular strengths.

We will now examine some of these in more detail.

3.2. Scope

To provide a sense of direction a business must have a clear mission statement which clearly defines the scope of the organisation. It answers such questions as:

- What is our business
- Who are our customers
- What kind of value can we provide these customers
- Who should our customers be in the future

Theodore Levitt writing in the Harvard Business Review argues that a firms mission should be defined as *what customer needs are to be satisfied and what functions the firm must perform to satisfy them*. Remember while technology and products may change over time that basic needs tend to endure. For example, if we were going from Davao to San Francisco three hundred years ago we would have gone by sailing ship, one hundred years ago we would have travelled by steam ship, tomorrow we would most likely go by air. The technology has changed but the basic need, travel, has stayed the same. If a firm defined its mission as transporting people by sailing ship it would have most likely gone out of business when steam ships arrived. If on the other hand it defined its mission as providing long distance passenger transport it would have been more likely to change with the times and perhaps be still in business.

Mission statements should not be confused with value statements (see below) - the former should be very hard-nosed while the latter can deal with 'softer' issues surrounding the business. The following table contrasts 'hard' and 'soft' mission statements.

Hard	**Soft**
What business is/does Primary products/services Key processes & technologies Main customer groups Primary markets/segments Principal channels/outlets	Reason for existence Competitive advantages Unique/distinctive features Important philosophical/social issues Image, quality, style, standards Stakeholder concerns

Compare the following statements:

Hard Statement	**Soft Statement**
X Corp. designs, develops, assembles and	Our mission is to enhance our customers'

markets systems for data base management. These systems integrate its proprietary operating system software with hardware supplied by major manufacturers, and are sold to small, medium and large-sized companies for a range of business applications. Its systems are distinguished by a sophisticated operating system, which permits use without trained data-processing personnel.	business by providing the very highest quality products and services possible. Our customer support strategy is based upon total, no-compromise customer satisfaction and we continually strive to offer a complete package of up-to-date value added solutions to meet our customers' needs. We value above all our long term customer relations.</TBODY>

3.3. Objectives

Confucius said that "*for one who has no objectives nothing is relevant"*. Formal objectives provide decision criteria and benchmarks against which performance can be measured. To be useful therefore objectives should be specific and measurable. Each objective should have the following components:

- A *performance dimension* or attribute sought
- A *measure* or *index* against which progress can be allocated
- A *target* or *hurdle* level to be achieved
- A *time frame* within which the targets should be achieved

3.4. Development

A firm can develop in a number of ways and develop products for different markets but it should have some strategy on how it is going to achieve these development objectives. The figure below gives some examples of different strategies the firm might use by different combinations of existing or new products and markets.

Primary product and market combinations include:

	Existing Products	**New Products**
Existing Markets	Lowest risk	Moderate risk
New Markets	Moderate risk	Highest risk

Other development strategies might concern diversification which could relate to forward or backward vertical integration.

3.5. Generic business level competitive strategies

Porter defines three distinct business strategies that firms pursue to achieve competitive advantage:

1. Overall cost leadership
2. Differentiation - building customer perceptions that the product is superior in some way (features, design, service etc)
3. Focus - avoiding direct competition by concentrating on a market niche not being currently served

Miles and Snow identified another set of business strategies:

- Prospectors - develop new products and are the first into the market, and are typically active in the introductory and early growth stage in the market life cycle
- Analysers - typically watch out for products which have been developed by others which they can further develop and capture a major share of a growing market. Usually prominent in the late growth stage and early maturity stage of the market life cycle.
- Defenders - firms that have established a strong market position and now want to defend it. Active in the mature and declining stages of the market life cycle
- Reactors - firms with no clear strategy who just react, usually too late, to actions by others

Harper and Boyd have combined elements of all these by sub-dividing analysers and defenders into low-cost and differentiated.

These different types of strategies require different functional strengths and a business with certain weaknesses will be less able to implement some strategies than others.

The strategy a business follows is dependent on the strengths of the firm and its management. Prospectors must have good R & D, marketing and manufacturing strengths. Low cost defenders on the other hand must be strong in manufacturing, distribution and cost control. To pursue these generic business strategies requires different management talents. Prospectors and analysers need to be risk takers and able to delegate considerable autonomy to the various functional departments. Defenders will be risk averse and delegate little and pay great attention to detail.

To be successful a firm must follow some strategy that is compatible with the strengths of its management. Specific strategies should be in line with the generic strategy being followed. A firm can not really follow two different generic strategies at the same time. For example it can not or at least it would be very very difficult to be the cost leader (low cost strategy) and at the same time be the quality leader (differentiated strategy).

3.6. SWOT analysis

Before developing a business strategy it is necessary to have a clear understanding of the businesses strengths and weaknesses and in the case of new ventures this will be largely down to the strengths and weaknesses of the entrepreneur or management. Opportunities and threats which exist in the market place will also be important in determining the most appropriate strategy to pursue.

In the case of an existing venture an analysis of past aims and achievements will be the first step. Then review the current status of the business. For new businesses these steps are not possible but past experiences, education, skills etc will be important.

Some essential points which should to be observed during the review and planning process include the following:

- Relate to the medium term i.e. 2/4 years
- Be undertaken by owners/directors
- Focus on matters of strategic importance
- Be separated from day-to-day work
- Be realistic, detached and critical
- Distinguish between cause and effect
- Be reviewed periodically
- Be written down.

Strengths and weaknesses are essentially **internal** to the organisation and relate to matters concerning resources, programs and organisation in key areas. These include:

- Sales - marketing - distribution - promotion - support;
- Management - systems - expertise - resources;
- Operations - efficiency - capacity - processes;
- Products - services - quality - pricing - features - range - competitiveness;

- Finances - resources - performance;
- R&D - effort - direction - resources;
- Costs - productivity - purchasing;
- Systems - organisation - structures.

If a start-up is being planned, the strengths and weaknesses are related mainly to the promoter(s) - their experience, expertise and management abilities - rather than to the project.

The objective is to build up a picture of the outstanding good and bad points, achievements and failures and other critical features within the company.

The threats and opportunities confronting a company are essentially **external**, and can exist or develop in the following areas:

- The company's own industry where structural changes may be occurring (Size and segmentation; growth patterns and maturity; established patterns and relationships, emergence/contraction of niches; international dimensions; relative attractiveness of segments)
- The marketplace which may be altering due to economic or social factors (Customers; distribution channels; economic factors, social/demographic issues; political & environmental factors)
- Competition which may be creating new threats or opportunities (Identities, performances, market shares, likely plans, aggressiveness, strengths & weaknesses)
- New technologies which may be causing fundamental changes in products, processes, etc. (Substitute products, alternative solutions, shifting channels, cost savings etc.)

Against an uncertain and shifting background, the objective must be to identify and prioritise the key SWOTs in a one-handed manner (Don't say on the one hand ....but on the other hand.........)

Once the SWOT review is complete, the future strategy may be readily apparent or, as is more likely the case, a series of strategies or combinations of tactics will suggest themselves. Use the SWOTs to help identify possible strategies as follows:

- Build on strengths
- Resolve weaknesses
- Exploit opportunities

- Avoid threats

The resulting strategies can then be filtered and moulded to form the basis of a realistic strategic plan.

3.7. Differences between a strategic plan and a business plan

A strategic plan should not be confused with a business plan. A strategic plan will generally be a sort document whereas a business plan will be much more detailed and focussed. A strategic plan should be visionary, conceptual and directional in contrast to an operational plan which is likely to be shorter term, tactical, tightly focused, implementable and measurable.

A strategic plan must be realistic and attainable to allow the planner to think strategically and act operationally

A sound plan should:

- Serve as a framework for decisions or for securing support/approval.
- Explain the business to others in order to inform, motivate & involve.
- Assist benchmarking & performance monitoring.
- Stimulate change and become building block for next plan.

Characteristics of Successful Businesses

When developing strategies it is worth reflecting on the characteristics of successful emerging growth businesses. They are likely to display many of the following characteristics:

Sensibly financed (with prudent mix of equity and debt).
Strong cash position (with access to follow-on or contingency funds).
Offers above-average profitability (in terms of return on capital invested).
Aims for rapid growth in revenues (with profits lagging but in prospect).
Targets expanding, or otherwise attractive, market segments.
Develops a strong franchise or brand.
Devotes substantial resources to innovation (R&D, offerings or market).
Competes on non-price issues (e.g. quality, service, functionality).
Very close to customers and responsive to their needs.
Seeks specialist/leadership image with superior offerings.
Well managed with high-grade staff & good people-management.

3.8. Causes of business failures

Having looked at the characteristics of successful businesses it can also be useful when developing strategies to consider why businesses fail.

A venture is most prone to failure during its first three or so years of operation - the so-called 'valley of death'. A key to getting through these early years is to avoid the obvious mistakes. Generally speaking, businesses fail for significant and substantial reasons which are often very evident to outsiders. Insiders often fail to see them because of their closeness, determination and so on.

Basic reasons for failure include the following:

Finance	**Markets/Sales**	**Management**	**Offerings**	**Operations**
Underestimating start-up costs (for operations & capital expenditure).	Misjudging the size or growth of the overall market.	Lack of relevant sectoral experience.	Inability to supply profitably to required price.	Under-investment in equipment etc.
Insufficient funds or access to top-up finance.	Overoptimistic estimates of market penetration & shares.	Insufficient functional breadth.	Problems with maintaining quality standards.	Excessive overheads (relative to scale of operations).
Wrong mix of funds (e.g. too much debt and gearing too high).	Delays in securing or developing distribution channels.	Unresolved differences of opinion.	Restricted range of offerings.	High operational costs and/or low productivity.
Over reliance on trade credit (receivables).	Underestimating the strength of competitors.	Unreal expectations.	Lack of innovation (*me-too* offerings).	Poor capacity utilisation.
Mistaking profit for cash flow	Misreading customer requirements.	No formal or clear structures.	Problems sourcing supplies.	Inadequate physical distribution.
Overoptimistic projections or overtrading.	Lack of promotion & customer awareness.	Ineffective financial & managerial control systems.	Offerings out of line with customer needs.	Inappropriate business location.
Unable to withstand interest rate increases.	Inability to handle an economic slowdown.			

Clearly, there are very many other reasons as to why businesses fail. The key point is that causes are usually very apparent (especially with hindsight, but of course, hindsight is a very exact science) and the trick is to anticipate them by executing appropriate strategies at the outset.

3.9. Basic Approaches

So far we have described generic business strategies, the characteristics of successful businesses and some of the main causes for business failures in addition to the main elements of the strategic plan.

For an established business there are two main approaches to strategic development. These can be classified as either organic or quantum as illustrated below:

Organic	**Quantum**
Lower risk	Higher risk
Limited resources needed	Substantial resources needed
Absorbs less effort	May divert/deflect attention
Low immediate returns	Higher returns (?)
Incremental learning/progress	Excellent insights required
Strategic flexibility	Unforgiving of errors

In the case of a start-up venture, organic and quantum approaches translate into *soft* or *hard* start-up strategies. An example of a soft start would be a software company which evolves from a part-time business into full-time service provider and then progresses into software products (classic "back room" start). Another example, would be an engineering company, which starts in a shed and gradually moves into proper premises ("garage" start).

Soft start strategies can be very effective as they allow entrepreneurs to learn the trade (and make mistakes) without incurring major, irrevocable (and maybe premature) commitments. Hard starts are obligatory where substantial investments (in R&D, market or assets) or resources (technology, manpower etc.) are needed from the outset. It may be possible to *soften* a hard start by renting (rather than buying) premises; leasing equipment (instead of purchasing); acquiring a franchise (in lieu of developing a new brand, systems etc.); entering into a joint venture; or subcontracting manufacturing, distribution, accountancy services and so on.

3.10. Strategic Combinations

This Section presents several different combinations of strategies, which could be used to help develop a range of strategic options. These can be strung together to form explicit strategic statements of intent.

The purpose of this section is not to encourage a form of *planning by words* but to simply expose the range of possibilities that might be considered when formulating explicit strategies. These can be applied equally to start-ups and established businesses. Of course, the big distinction is that the start-up is building strategies from scratch without the benefits of any market position, momentum or pre-existing strategies.

Any selected suite of strategies must be integrated and internally consistent and in-line with the business's broader vision, mission and objectives. There is little point in a business claiming to be technologically advanced if its R&D spend is sub-critical, or aspiring to become a leading brand if it has neither products, nor funds nor distribution to ensure this could happen.

Basic thrusts of a business (to be continued, deepened or initiated):

Basic Supplier Thrusts		
Specialist	Vs.	Full-line
Market/price leader	Vs.	Market/price follower
Products	Vs.	Solutions
Goods	Vs.	Services
Low volumes	Vs.	Mass production
Commodity offerings	Vs.	High added-value
Differentiated offerings	Vs.	*Me-too* offerings
Niche markets	Vs.	Broad segments

Primary product and market combinations include:

	Existing Products	**New Products**
Existing Markets	Lowest risk	Moderate risk
New Markets	Moderate risk	Highest risk

Investment possibilities include the following:

Improve market share, enhance brand, extend distribution
Increase capacity or efficiency or reduce costs
Extend product ranges and/or served markets
Stabilise/strengthen financial position
Innovate and create new offerings
Increase skills or productivity
Scale back or close down

Possible future directions of main activities (Xs signify desired action):

Activities	**Direction**				
	Ignore	Initiate	Intensify	Reduce	Withdraw
Distribution	X	-	-	-	-
Retail	-	-	-	-	X
Services	-	X	-	-	-
Manufacturing	-	-	X	-	

Alternative technology acquisition routes include:

Own R & D
Own D & no R
License in
Joint venture
Co-finance/sponsor

Funding strategies could embrace the following sources and forms:

Sources	**Forms**
Internal	Retentions Forego dividends Existing shareholders Disposal of surplus assets Sale & lease back Better management of working capital
External	Debt (short- or long-term) Factoring & discounting Supplier/customer loans or advances Leasing (operating & capital) Grants & subsidies Equity (formal and informal venture capital)

The range of quantum leap possibilities could include:

License in/out
Franchise
Trade investment
Minority/majority stake
Joint venture
Consortium membership
Merge/demerge
Acquisition
Sponsor start-up

3.11. Strategic Statements

Strategic statements can be defined as broad indicators of the direction(s) in which a business should be driven in order to fulfil its vision/mission while taking realistic account of its resources, constraints and opportunities.

They also serve as the link between the business's objective and actions plans and should result in a series of integrated sub-strategies and action programs with goals, budgets, and timetables. These can be most effective when linked to specific functional areas. For example:

Industry	Operations
Marketplace	Finance/funding
Technology	Sales
Offerings	Management
Marketing	Organisation

3.12. Next Steps

Once a set of strategies has been developed, it will almost certainly need detailed planning and reality testing. This could embrace market research, acquisition scouting and all forms of planning ranging from investment appraisal through financial projections to business plans or corporate submissions.

For a start-up, additional planning activities could include (in no particular order) management team formation, R&D, market research and market entry planning, feasibility studies and preliminary fund raising.

Be realistic about the rate at which a management team can implement strategic change and allow for the fact that these may involve factors totally outside the business's control. It may be better to implement a few strategic initiatives successfully and on time rather than a multitude badly or only partially. The solution here is to prioritise.

3.13. Conclusion

Notwithstanding that "battles are often lost for want of nails", a company rarely succeeds or fails for minor or trivial reasons. The causes are usually substantial and are often self-evident, at least to an outsider. For example, the business was completely over-borrowed; management was weak; a major new product opportunity was identified; legislation changed; a major competitor went bust or expanded; the company never re-invested.

It should be possible in the course of a few pages to set down the main elements of a business's vision, mission, values, objectives, goals, strategies, SWOTs etc. The compilation of a short report along these lines is likely to prove much more difficult than a lengthy dissertation which mixes up details and principles, and confuses the broad picture.

Independent advisers or non-executive directors can play a valuable role in this process because they can readily adopt the role of devil's advocate and also bring external knowledge and expertise to bear.

3.14. The strategic planning worksheet

The worksheet presented below may also assist as it sets out the steps to be followed.

3.14.1 Using the Worksheet

Relate the planning exercise to a specific company or, if diversified, to individual strategic business units.
Ideally the worksheet should be compiled by a multi-discipline management group, or separately by 2/3 groups and then discussed in plenary session if a large business unit is involved.

If working on your own, complete the worksheet and then return to it a few times over the following few days and critically review what you wrote - why, why, why etc. and ask yourself whether you have seen the "wood for trees".
A completed worksheet should be edited down into a 1-2 page document and reviewed by the group(s). The final form of the document need not follow the worksheet's layout provided all the matters are covered.
If working on your own show the plan to somebody you can trust and who has some experience of business - a professional business advisor would be useful here.
All ideas, issues etc. should be internally consistent and realistic.
You need a very good understanding of the market, competitors etc. in order to make a clear assessment of your SWOTs. If you haven't got this insight, suspend work on your strategic plan until you have done this basic research.

Bear in mind that it is much more difficult to write a short plan than a long one!

3.15. Strategic Planning Worksheet

1. **Assess the business's EXISTING strengths, weaknesses, threats and opportunities:**

(SWs are internal to the business and OTs are external. All SWOTs should be 'one-handed' - something is either a S or a W but cannot be both. Enter up to six items under each heading and then rank them in order of importance. If you are planning a new business, consider the project's and its promoters' existing SWOTs):

Internal Strengths
Internal Weaknesses
External Threats
External Opportunities

3.16. 2.Vision of business in 3/4 years time:

(What will the business look like? If a visitor from Mars dropped in what would be seen and evident. Write in present tense. Maximum of 150 words)

3. Mission/purpose statement for business to cover next 3/4 years:

(What will the business really, really be doing? What activities will it perform, where, how etc. Every noun, adjective and verb in the statement is important and must be justified. Maximum of 150 words)

4. Statement of corporate values and beliefs:
(Covers employees, customers, environment etc. etc. Maximum of 150 words)

5. Set out key long-term objectives:
(These are the primary underlying reasons for being involved in the business, and are not specific targets - these come later)

5a Shareholders **5b Management (If different from shareholders)** **5c Business (Relative to competitors etc.)**

6. Identify key strategies for business and major functional areas:
(Build on strengths, resolve threats, exploit opportunities and avoid threats. Add any new dimensions revealed by Vision and Mission. List and prioritize up to ten or so major strategies.

2. **Assess possible FUTURE strengths, weaknesses, threats and opportunities:**
   (Do the foregoing strategies improve the initial SWOTs? If they don't, then they should have done so)

Internal Strengths **Internal Weaknesses** **External Threats** **External Opportunities**

8. Review your vision, mission, values and objectives:
(Refine and revise/restate key strategies to deal with the perceived FUTURE SWOTs)

9. Specify major goals achievable over the next 3/4 years:
(Quantify in terms of sales, market shares, finances, operations etc.)

10. Define strategic action programs:
(Indicate who, what, where, when, how etc. Set targets and prioritise)

If you have prepared a strategic plan along the lines suggested above, you have several possible pathways to proceed. These include the preparation of a full-blown business plan, compilation of financial projections, undertaking market research, product development, management team-building etc. etc.

4. Generating and Developing Business Ideas

When the entrepreneur has decided what type of business strategy to pursue a number of avenues are open, depending on the particular situation. If it is an established enterprise or with a new enterprise where a business opportunity has already been identified it may be possible to go straight into preparing a business plan. The more likely scenario is that the business idea may have to be still identified or further developed before detailed planning can start.

Many of the steps in this process have similarities to the strategic planning process outlined above. The type of enterprise you are likely to develop will depend on the type of business strategy you have decided to pursue. It must be consistent with the results of the SWOT analysis. In many ways it is a specific application of the generic strategic planning process.

4.1. General Comments

Finding and developing viable business ideas is a combination of art, a matter of luck and the use of systematic techniques. Certainly, you can use structured approaches, as described below, but the reality is that having the right background, being in the right place at the right time, and working hard to create lucky breaks are likely to be just as important in coming up with sound business ideas. Hard work is certainly very important. Henry Ford said that *genius is 95% perspiration and 5% inspiration.* Another relevant quotation is *the harder I work the luckier I get.*

The concepts presented below represent a series of checklists. They need not be followed systematically and, most certainly, they should not be perceived as a sure-fire recipe. Instead, view them as a series of menus from which you can pick and choose according as your thoughts develop. Probably, the only issue which everyone searching for new business ideas should review systematically is their own strengths and weaknesses and to use this as their key building block and jumping off point.

4.2. Identifying Strengths & Weaknesses

The starting point for developing new business ideas lies inside the prospective entrepreneur rather than in the marketplace, laboratory, business plan etc. The entrepreneur is the critical component - it is his/her strengths and weaknesses which should dictate the areas in which to seek ideas and the likely scale &

scope of the business. At the end of the day, support for a business by financiers, suppliers, customers etc. will also be a vote of confidence in the management's abilities to make it successful. In the case of new businesses the only tangible item that can be judged by prospective backers is the management.

The entrepreneur should build on **strengths** and surmount or work around **weaknesses.** If there are some serious limitations, these are likely to be a limiting factor and are likely to set the limit of what can be achieved. For example, there is little point in searching for capital-intensive or knowledge-based ideas if there is slim/no prospects of raising the necessary capital or if educational background is unsuitable. We have all heard stories of garage-starts by school or college drops-out which attracted venture capital and eventually became mega-businesses (Bill Gates is probably one of the best known college drop outs). But we don't hear so much about the huge numbers of failures.

4.3. What direction is the prospective entrepreneur coming from

Is s/he:

- An inventor who has a product/service idea?
- An innovator who has developed a new product/service?
- Out of work and want to create a job for yourself?
- An entrepreneur who wishes to create a business?
- A manager who wishes to develop a business?

Be especially aware that inventors and innovators do not necessarily make good business people. To establish and run a successful business requires more than good ideas. The Apple Computer operating system has always been regarded as a far more innovative and superior system to Microsoft, but bad strategic business decisions has consigned Apple to a very minor share of the market.

Areas where you should make honest assessments of your strengths and weaknesses include the following:

4.4. Educational background

- Any (special) business or technical qualifications?
- Do you have a knowledge of finance & marketing?
- Are you up-to-date with business-related issues?

4.5. Financial strengths

- Have you access to personal or family funds or finance from other sources?
- How much, how easily, what conditions and when?
- How long could you survive without any (regular) income while your business develops?

4.6. Commitment

- Why do you **really** want to start a business?
- Are you in reasonable health?
- Have you any/many family commitments?
- Does the family fully approve of your proposal to set up your own business?
- Are you willing to relocate/commute in order to pursue a business possibility?

4.7. Expertise & interests

- Do you have insights into any business sectors or trades?
- What are you good at or like doing?
- Do you have a hobby/interest/talent which could become the basis of a business?

4.8. Personal qualities

- Are you a resourceful, energetic and motivated person?
- Have you a capacity to take lots of knocks and bounce back? (most successful entrepreneurs do not make it on the first attempt)
- Are you realistic and practical? Are you a hard worker?
- What do you dislike doing?

4.9. Prior experience

- Where have you worked before?
- Have you done anything special, exceptional or unusual?
- What work-related skills or expertise do you have?

4.10. External contacts, resources etc.

- What contacts have you in finance, business etc.
- Have you or your family access to any under-utilised resources.
- Do you know people who might help give you a start?

Don't be afraid to ask other people to help assess your strengths and weaknesses. To help surmount weaknesses, consider the idea of forming an entrepreneurial team (or taking on a partner, part-time adviser, non-executive director etc.). Beware of trying to work with people you don't like or respect, and **do not** involve family unless you are really, really sure that it will work out for the long-term.

Write down your assessments and rank your main strengths and weaknesses. Make sure to avoid the trap of showing something as both a strength and weakness. Use the resulting list to help set the criteria and boundaries to your search for business ideas. For example, the scope of your ideas might embrace ideas centred on one of the following:
Specific local services;
about XX,000 cash;
use of an existing resource etc.
Previous work experience;
national markets;

Be specific but don't place unnecessary limits on the scope of your ideas or thinking. Some clear ideas may have already started to emerge which you could start evaluating straight away.

4.11. Looking for Ideas

When looking around for business ideas, bear in mind that these could be based on any of the following approaches:

- A **manufactured product** where
  - you buy materials or parts and make up the product(s) yourself.
  - Use local materials to manufacture goods (timber to make packing crates, fibre to make crafts)
- A **distributed product** where you buy product from a wholesaler, retailer, or manufacturer.
- A **service** which you provide.

Bear in mind that most good business ideas are not completely original and most "new" products are not new to the world. The following diagram shows the possible combinations of existing/new products/markets.

	Existing Products	**New Products**
Existing Markets	X	XXX
New Markets	XXX	X

The simplest business ideas are existing products in existing markets, and the trickiest are new products in new markets. If you concentrate on pursuing ideas involving existing products in existing markets, you run the risk of being exposed to severe competition. If you focus on new products in new markets, you might find yourself too far out on a limb. Look most closely at the combinations of either new products for existing markets or new markets for existing products.

You must narrow your search to specific market or product areas as quickly as possible. For example, the "food business" is too broad a search area. Do you mean producing, manufacturing, distribution or retailing, or do you mean fresh, frozen, pre-prepared etc. or do you mean beverages, sauces, confectionery etc.? It is better to pursue one or more specific ideas (hypotheses) rather than one diffuse concept which lacks specifics and proves impossible to research and evaluate.

Generally, you should always aim for quality rather than cheapness. Be very cautious about

- pursuing ideas which involve any prospect of price wars or are very price sensitive;
- of getting sucked into short-lived fads;
- of having to compete head-to-head with large, entrenched businesses.

Observe consumer behaviour:

- What do people/organisations buy?
- What do they want and cannot buy?
- What do they buy and don't like?
- Where do they buy, when and how?
- Why do they buy?
- What are they buying more of?
- What else might they need but cannot get ?

Look at changing existing products or services with a view to:

- Making them larger/smaller, lighter/heavier, faster/slower
- Changing their color, material or shape
- Altering their quality or quantity
- Increasing mobility, access, portability, disposability
- Simplifying repair, maintenance, replacement, cleaning
- Introducing automation, simplification, convenience

- Adding new features, accessories, extensions
- Changing the delivery method, packaging, unit size/shape
- Improving usability, performance or safety
- Broadening or narrowing the range
- Improving the quality or service.

Be on the look out for:

4.12. Emerging Trends

For example, the population within your area may be getting older and creating demand for new products and services.

- **Expanding Market Niches**

  For example, local industries may be outsourcing more of their services.

Try the following approaches to locating ideas and suggestions:

- Brainstorm with your friends, associates
- Ask people for their ideas
- Use one idea to spark a better one
- Read relevant trade magazines (local, national and foreign)
- Skim through trade directories (local, national and foreign)

Philippine government agencies such as

- The Department of Science and Technology
- The Department of Trade and Industry
- The Fibre Industry Development Authority
- The Philippine Coconut Authority

Research institutes and universities can also be a good source of ideas.

Above all, open your eyes wide and try to spot the obvious gaps.

Go into shops, supermarkets, hardware stores, markets or anywhere else where products are bought and sold. See what products are there that are imported, or are manufactured a long way away and could be made locally.

By all means be inventive, imaginative and original in your thinking but stay market- and consumer-orientated rather than product-obsessed. We all know stories about people inventing a better mousetrap and never getting a nibble from the market!!

4.13. Assessing Ideas

Having built up a moderate list of ideas, these must be evaluated so that a short-list of preferred options with the greatest potential and lowest risk can be assessed in greater depth.

One way of evaluating ideas would be to use a simple scoring system using gut-feel with a limited number of criteria as shown below.

Factor	**Score (1-10)**
Personal fit	??
Degree of risk	??
Funding needed	??
Ease of start-up	??
Short-term potential	??
Level; of preparation	??
Competitive threats	??
Etc. etc.	??
Total	**xx**

Before scoring individual ideas, run through the criteria and set what you feel should be minimum desirable scores for each. The resultant total could be used as your overall minimum threshold. If some ideas don't achieve satisfactory scores, drop them and look for better ones.

Once your short-list has been developed, you will need to start devoting substantial time to assessment, research, development and planning. For a start, you could pursue the following tasks:

4.14. Discuss products/services with prospective customers

Would they buy from you, at what price, with what frequency etc.? Why would they prefer your products to the competition?

Find out what they really think - there is a danger that people will tell you what they think you would like to hear. Listen carefully to what is being said; watch carefully for qualifications, hesitations etc.; and don't brow beat respondents with your ideas - you are looking for their views. At this point you are not trying to sell your product or service, you are doing market research and trying to guage the reaction of the market.

4.15. Assess the market using desk & field research

How does the market segment (by price, location, quality, channel etc.)?What segments will you be targeting?How large are these segments (in volume terms) and how are they changing?What are the price makeups/structures?

What market share might be available to you bearing in mind your likely prices, location, breath of distribution, levels of promotion etc.?

Analyse your competition

Who are they and how do they operate? Are they successful and why? How would they react to your arrival? What makes you think that you could beat the competition?

At whose expense will you gain sales? These are questions which are particularly important for service industries.

4.16. Consider possible start-up strategies

Will you be able to work from home or part-time? Will you seek a franchise or set up as an in-store concession? Will you start by buying in finished products for resale as a precursor to manufacturing? Will you contract out manufacturing? Will you buy an existing business or form an alliance? Could you lease or hire equipment, premises etc. rather than buy? How will you stimulate sales?

4.17. Set ball-park targets and prepare first-cut financial projections

Estimate possible sales and costs to get a feel for orders of magnitude and key components and to establish a rough break-even point (when your sales might start covering all your costs). Avoid over-estimating likely sales and under-estimating costs or lead times. Better to be relatively conservative. Don't confuse profits and cash and make sure that you make provision for working capital

4.18. Prepare a simple action plan

Cover the first year of operations to highlight the critical tasks and likely funding needed before the business starts generating a positive cashflow. This is critical especially if you have to undertake significant product or market development or need to give credit to customers.

4.19. Critically examine ideas from all angles

Can I raise enough money? Can I get a premises/staff etc. Will the product work? How will I promote and sell? Think through possible problems.

What would happen if:
sales took twice the expected time to develop
costs escalated? What would happen if ....

This is where a *what if* or *sensitivity analysis* should be conducted.

There are now computer programmes which will perform a certain amount of analysis on business plans and show up some weaknesses. In skilled hands these can be a very useful tool in assessing business proposals.

Bear in mind that the incubation period for a new business can easily last several months or even years. Don't rush into the first feasible idea without letting it incubate or develop in your mind for a reasonable period. There might be a tendency to get all fired up and enthusiastic such that your heart is starting to rule your head. Instead, stand back and think!!

Do not be afraid to seek external assistance from professional advisers or from enterprise support organisations.

4.20. Next Steps

Having firmed up on a specific idea and conducted preliminary research, you have several options including the following:

- Undertake more detailed/specific market research.
- Do further product research, development, testing etc.
- Review and refine your proposed start-up and developmental strategies.
- Draft a detailed or outline business plan.
- Prepare financial projections.
- Start looking around for the key resources - people, money. premises, partners etc.

Most probably, you will start addressing all these tasks in parallel rather than sequentially. Other issues which you may need to start thinking about include the following:

- Select a company or business name, logo etc.
- Decide how you will start trading - limited company, sole trader etc.
- Inquire into any licences which might be needed, or regulations to be complied with.
- Think about where the business will be located.
- Look for professional advisers (lawyer, accountant) and a bank.
- Consider likely telephone/communications needs.

Bear in mind that, to develop a successful business, you must:

- Define precisely the nature of the business

- Offer clearly identifiable products or services
- Tap a real need or generate a demand for your product/service
- Operate within your expertise and resources
- Have realistic targets and have reasonable expectations
- Keep everything as simple and straightforward as possible.

If, at all feasible, there are huge advantages to be gained by embarking on a "soft start" or pilot launch before plunging full tilt into the new business. This approach can be of enormous value in helping to firm up on the scope of the opportunity; gaining more insights into the market; debugging products and getting customer feedback; curtailing costs and personal or financial exposure; acquiring a track record etc. etc.

5. Business Planning

A business plan is, or should be a realistic view of the expectations and long-term objectives for an established business or new venture. It provides the framework within which the enterprise must operate and, ultimately, succeed or fail. While a comprehensive plan is no guarantee of success the absence of one is a pretty sure guarantee of failure.

The complexity of a business plan will vary depending on the scale of the enterprise. Large complex enterprises will require a high level and very detailed planning. Smaller enterprises will obviously require less detailed planning. But even micro enterprises such as an individual small farm will still require some level of planning. In the case of farm enterprises we call them *farm plans* but they still are business plans and will contain some or all of the same basic elements.

For example, if a farmer is planning to start a small fruit production venture he would not be expected to produce a twenty or thirty page business plan. He would however, need to have some information on markets, planting material, financing requirements, cash flows, yield and income projections and any specialised equipment needed etc. If he was looking for a loan to finance all or part of this he would need to outline what other capital sources he has, how he would propose to pay interest and pay for fertiliser and chemicals during the gestation period of the crop. ***Here you have all the elements of a business plan.*** In this case it will be fairly short but it will also be reasonably comprehensive. The section on marketing might only be a few lines. Perhaps produce might be for sale to a local trader or cooperative or processor. The bank manager, if he needs some more information or reassurance on the market, can then contact the trader or the coop or the processor.

Most plans follow a well-tried and tested structure and general advice on preparing a plan is universally applicable. This paper therefore sets out to outline a generic business planning process which can be adapted for specific enterprises and situations.

The preparation of a written business plan of course is not and end in itself, but is an important intermediate step in the overall objective of achieving the targets set out in the plan.

A formal business plan is just as important for an established business, irrespective of its size, as it is for a start-up. For an established business it also demonstrates that careful consideration has been given to the business's development, and for a start-up it shows that the entrepreneur has done his or her homework.

An important element of the planning process is that in the course of preparing the plan there will be some questions that can not be answered at least with certainty. The planning process does however highlight these areas and will alert management to the need to pay particular attention to them in the future. General Dwight Eisenhower, the Supreme Commander of the Allies in Europe during World War II and later U.S. President, once said *"it is not the plan that is important but the planning"*.

The planning process forces managers or entrepreneurs to understand more clearly what they want to achieve, and how and when they can do it. Even if no external support is needed, a business plan can play a vital role in helping to avoid mistakes or recognise hidden opportunities.

For many entrepreneurs and planners, the process of planning (thinking, discussing, researching and analysing) is just as, or even more, useful than the final plan. So, even if you don't need a formal plan, think carefully about going through the planning process. It could be enormously beneficial to your business. During this planning phase opportunities may be identified for adding value or possible pitfalls spotted.

So even in very small enterprises the planning process should be followed.

The plan serves a number of functions:

- Helps management to clarify and to focus on issues which will affect their business' development and prospects.
- Provides a logical framework within which a business can develop and pursue business strategies over the next three to five years.
- Serves as a basis for discussion with third parties such as shareholders, agencies, banks, investors etc.
- Offers a benchmark against which actual performance can be measured and reviewed.

5.1. Preparing an Outline Plan

It can be useful to first prepare an outline plan. This has the advantage of enabling the plan's writer to concentrate on the essentials of planning the business rather than become too absorbed in the actual drafting of the plan. Sometimes an outline plan may suffice or, at least, provide the building block for the more detailed plan. An outline plan is useful for testing ideas before embarking on comprehensive planning. If a credible and acceptable outline plan cannot be compiled then it is highly improbable that a more comprehensive plan can be prepared.

5.2. Preparing a Detailed Plan

When writing a business plan two considerations we should keep in mind are:

- what is the purpose of the plan
- who is it for.

This will determine what information needs to be included, the level of detail and perhaps the layout.

Next all the main issues to be addressed should be identified. This will help to identify gaps which need to be researched before drafting commences. A business plan should be the end result of a careful research and development project to be completed before any serious writing of a plan should be started.

Finally the layout of the plan should be sketched out.

5.3. Structure & Content

A typical business plan comprises the following main elements:

Brief **Introduction** setting out the background and structure of the plan.
Summary of a few pages which highlights the main issues and proposals (to be written last).
Main **Body** containing chapters broken into numbered sections and subsections.
Appendices containing tables, detailed information, exhibits, etc. referred to in the text.

5.4. Length & Time-scale

Whilst the sheer length of a business plan may bear no relation to the underlying prospects of a business, it is likely that a well-developed plan would be at least twenty pages long plus appendices.

The elapsed time needed to produce a plan might be between twenty and one hundred days. This would be determined not only by the complexity and scale of the venture, but also by the scale and maturity of the business and relevant experience and skills of the management team. Whilst the task of writing the plan itself may only take a relatively short time, be sure to allocate enough time to the research, preparatory work and the underlying thinking and discussion.

Practical Hints

While external help and guidance in preparing a business plan can be extremely valuable a word of caution here is necessary. The resultant plan must remain the property of the entrepreneur or manager and not that of their advisers.

The following suggestions may be of assistance:

The most important and difficult sections to prepare relate to marketing and sales as these can make or break the business - without a market there can be no business and the market is often the area about which there is least certainty

The financial projections are likely to be straightforward but decide on a sensible level of detail as regards the time horizon etc. For more complex plans access to a computer and a financial modeling package for the projections would be extremely useful

When drafting the plan be positive but realistic about the business's prospects and explicitly recognise and respond honestly to shortcomings and risks.

The management section of the plan is crucial - experience, balance, ability and commitment. If a new venture is involved, then management is likely to be its only real asset. Consider formation of a management team or strengthening management as part of the plan. Remember the five ingredients of a successful business are management, management, management, market and product (in that order, and **not** in the reverse order as some inventors and entrepreneurs might like to think). No matter how good a market opportunity might be

5.5. When writing the plan:

- avoid unnecessary jargon and use simple unambiguous words whose meaning is clearly understood
- economise on words – if one line is sufficient do not use two.
- use short crisp sentences and bullet points
- check spellings
- concentrate on relevant and significant issues
- break the text into numbered paragraphs, sections etc.
- relegate detail to appendices
- provide a contents page and number pages
- write the summary **last**.

Get a qualified outsider to review your plan in draft form and be prepared to adjust the plan in the light of comments secured and experiences gained

Support market and sales projections by market research. Ensure that there is a direct relationship between market analysis, sales forecasts and financial projections. Assess competitors' positions and possible responses realistically.

Restrict the level of detail on product specifications and technical issues.

Be realistic about sales expectations, profit margins and funding requirements. Ensure that financial ratios are in line with industry norms. Do not underestimate the cost and time required for product development, market entry, securing external support or raising finance. Consider the possibility of the **halve-double rule** - halve the sales projections and double the cost and time required.

If looking for external equity, be realistic about the value of the business, risks involved and possible returns, and be sure to indicate possible exit mechanisms. Put yourself in the shoes of an investor and remember the **golden rule** - *he who has the gold makes all the rules*.

5.6. The Business Plan Worksheet

Only address matters of real substance and major significance. Feel free to change the suggested structure to suit the project and its state of development. If writing an outline plan, allow between a half and two pages per section.

The structure below could be readily expanded to become a 'full-blown' business plan by expanding the level of detail given. **Ideal** page lengths for a straightforward but comprehensive plan are given in parenthesis. Note the importance of marketing and sales in terms of the suggested number of pages. Relegate detail to accompanying appendices. Bear in mind that most investors, bankers etc. dislike having to read overlong business plans just as much as entrepreneurs and managers dislike writing the plans in the first instance. A banker is not really interested in knowing whether you have to spray your crop every six days, every seven days or every month. He probably does not want to even know to know what you are spraying for or what you use (unless maybe he likes farming himself). Obviously if you need financing for these operations you must calculate how much finance you need. The financing requirement should be in the main body, the details of how that requirement is calculated should be in an annex. The bank's agronomist can then check the detailed calculation if necessary.

1.Introduction (1)

Introduce the plan. Explain who wrote it, when and for what purpose. Give contact details.

2. Summary (1-3)

Write last.

3. Mission, Strategies etc. (1-2)

What are the central purposes and activities of the planned business? What are its SWOTs? What are its major objectives, key strategies and prime goals ?

4. Present Status of Project (1-3)

Summarise achievements and performance (financial, sales, technical etc.) to date. Introduce the stakeholders in the business.

5. Product/Service Description (1-2)

Keep descriptions short and confine them to broad groups. Explain briefly what makes them special.

6. Profile of Target Market(s) (2-3)
Size, segments, trends, competition and user/customer profiles.

7. Marketing Strategies & Sales Plans (2-3)
How will the business market its products/services and sell to customers? What sales will be achieved in its main markets? How will it deal with competitors? Indicate costs. It may only be necessary to demonstrate here that you can match prevailing prices.

8. R&D and Technology (0-2)
If relevant, explain progress, plans, resources and highlight any technological advances.

9. Manufacturing/Operational Plans (2-3)
Cover distribution & service activities and/or manufacturing. Highlight major elements only. Indicate organisation, resources, costings etc.

10. Management (1-2)
Introduce the proposed management team, structure etc. Indicate overhead costs.

11. Financial Position & Projections (2-3)
Use simple tables to present key financial projections e.g. summary P&L, cashflows, balance sheets and key ratios. Place the detailed analyses in appendices.

12. Funding Requirements & Proposals (2-3)
If applicable, summarise funding requirements, possible sources, likely terms, and, for investors, the projected return on their investment. Be realistic!

13. Implementation (1-3)
Explain the major decision points, time scale and actions required by management and others to progress the plan.

14. Conclusion (1)
Indicate why the business will succeed and why it should be supported.

6. Financial Planning

6.1. Introduction

Financial planning is a critical activity for every business irrespective of its age and size. For new enterprises, the preparation of financial projections is integral to the business planning process. For larger companies, financial planning forms part of annual budgeting and plays an important role in long-term planning, business appraisals, corporate development etc.

Central to the task of preparing a set of projections is the construction of a mathematical model to reflect the finances and activities of a business. Sales *minus* Costs *equals* Profits (S-C=P) is an example of a very simple model for deriving projected profits from assumptions for future sales and costs.

In practice, financial planning models are much more complex as they must accommodate multiple time periods (months, quarters and years) and handle hundreds of variables relating to sales, costs etc. The volume of data mounts up very quickly when each variable is multiplied by the time horizon, for example, by twelve months. Assumptions can also be varied which also can add considerably to the complexity of calculations.

Figure 1 below lists typical assumption variables used to generate a set of financial projections.

Figure 1 - Some assumption variables used by a financial model to produce projected P&Ls, cash flows and balance sheets for a manufacturing business.	
Sales volumes	Fixed asset values
Selling prices	Material costs
Selling & distribution costs	Accumulated depreciation
VAT rates for inputs	Prepayments/accruals
Research & development	Material/WIP stocks
Interest rates	Capital expenditure
VAT rates for sales	Share issues
Management/administration	Direct manpower levels
Changes in loans/debt	Capital & revenue grants
Bad debt provisions	Dividends
General overheads	Wage rates

Operating leases & HP Target finished stocks Depreciation rates Current year debtors/creditors Opening balance sheet	Fixed asset disposals Corporation tax Other direct costs Finance leases Phasing of opening balances Operational overheads

A comprehensive model can contain many thousands of formulae with functions ranging from simple addition to complex conditional statements (e.g. if projected cash flow is positive, reduce the overdraft before adding any residual balance to the cash account).

Financial models are used to compile forecasts and budgets; to assess possible funding requirements; and to explore the likely financial consequences of alternative funding, marketing or operational strategies. They can also be used for business planning, raising finance, investment or funding appraisals, financial analysis, corporate planning etc.

Used effectively, a financial model can help prevent major planning errors; identify or evaluate opportunities; attract external funding; provide strategic guidance; evaluate financial and development options; monitor progress etc.

6.2. Using a Computer

A personal computer with appropriate software can help prepare financial projections. A computer-based model reduces the tedium of carrying out numerous repetitive calculations; simplifies the alteration of assumptions; and improves the presentation of results.

When using a computer, a manager or planner can utilise a spreadsheet to build a model from first principles. While the development of a spreadsheet model of a company's profit & loss account should be well within the capabilities of many managers, the development of an integrated and comprehensive financial planner is an infinitely more challenging, time consuming and difficult task. A manager must know when to draw the line between using a spreadsheet to plan and becoming a spreadsheet programmer.

As an alternative to a DIY model, a manager or entrepreneur can purchase a ready-made model, which can be either (a) loaded as a template into a spreadsheet or (b) run as a stand-alone package.

The main advantage of building a bespoke model is that it can be fine- tuned to meet very specialised requirements. However, the drawback is that building a comprehensive, error-free and user-friendly financial model could require hundreds of hours of development and testing along with considerable programming and financial expertise. This work inevitably distracts from the real task of planning the business and begs the question as to why managers, entrepreneurs, advisers etc. should re-invent the wheel whenever a set of financial projections are required.

Additionally off-the-shelf packages are becoming more sophisticated and cheaper all the time and at the same time more user friendly. They can also be applied to more or less any situation.

6.3. How Models Work

A computer-based financial model is the electronic equivalent of a very large sheet of ruled paper which, depending on circumstances, could be 10 to 20 square feet in area. The computer's screen serves as a small window on this electronic sheet, which usually displays variables and values along rows and time periods in columns.

A model utilises assumptions for sales volumes, prices, operating costs, funding etc., to produce projected balance sheets, profit & loss accounts and cash flow statements. Typically, it makes monthly projections for the first year and less detailed projections for the following years. Some models will produce projections (P&Ls, cash flows, balance sheets) for the first year on a monthly basis and for the following two years on a quarterly basis. As all the components of a model are linked by formulae, a change to any assumption in any period results in appropriate adjustments to profits, cash flows etc. throughout the model for the remaining months, quarters and years.

Once initial assumptions have been entered, they can be readily altered to evaluate alternative scenarios. For example, a model could be used to explore the extent to which future sales can be increased while holding borrowings within predetermined limits; to assess the effects of varying selling prices and/or volumes on net profits; or to determine the optimum level and mix of future funding for a business.

As a practical example, Figure 2 below shows the results of using a model to undertake a "what-if" analysis where sales volumes and prices have been increased by a fixed percentage.

Figure 2 - Results of Sensitivity Analysis

Sales (P000)	553	664	608
Sales (% change)	n/a	+20	+10
Pre-tax Profits (P000)	28	65	85
Pre-tax Profits (% Change)	n/a	+132	+204
Net Cashflow (P000)	43	68	93
Net Cashflow (% Change	n/a	+58	+116
Peak Monthly Loans (P000)	72	65	57
Peak Monthly Loan (% Change)	n/a	-10	-21
Full-Year Return on Capital (%)	16	30	35

Given a choice between a 20% increase in sales volumes or a 10% increase in selling prices, the model shows that the latter would be a far more attractive option. The results also offer an insight into the underlying cashflows and funding requirements.

In the same way the effect of changes in production, costs etc can be demonstrated.

6.4. Planning to Plan

For managers of an existing business, or promoters planning a new venture, financial modelling can be an invaluable tool to assist the preparation of a business plan. However, **business planning should not be confused with the preparation of financial projections**.

- The business plan must provide the foundation for the financial projections which can be derived arithmetically by a model.
- The model and its forecasts should contribute to but never dictate the contents of a written business plan.

If financial projections are not coming out the way we want them under no circumstances should you start massaging the figures. The reason for doing the exercise is to test if the hypothesis is feasible.

Once basic issues relating to markets, sales and operations have been fully researched and considered, a model can be used to produce the financial projections. However, the veracity and usefulness of these projections will be completely determined by the quality and reliability of the underlying assumptions determined outside the model. For example, if sales or cost forecasts are unrealistic or inadequately researched, then the value of a model's output is greatly diminished. An impressive set of financial projections is of little benefit if unsupported by research or only based on speculation or wishful thinking.

Before using a financial model to help plan the future of a business, a manager or entrepreneur should:

Decide at the very outset on the central purpose of the planning exercise (raise funds etc.); the target audience (co-directors, financial institutions etc.); and the time horizon (one year etc.).
Identify and think through all the critical assumptions. Prepare outline projections to confirm their overall direction, examine the critical elements in detail and consider strategic issues relating to sales, profitability, funding etc.
Check that all key assumptions (e.g. sales forecasts) and data (e.g. opening balance sheet and any prior-year financial results) are to hand, and have been adequately researched.

Recognise the danger of presenting too much detail or too many reports. Most senior managers, investors and financiers seek simple financial statements, which have been based on detailed analysis and realistic assumptions.

6.5. Tips & Traps

When preparing financial projections, be conscious of the pitfalls and dangers listed in below. These can arise as the result of a lack of foresight or insight, or because of excessive optimism. As they can lead to under-estimation of the resources required to develop a business with potentially disastrous consequences, it can be counter-productive to overstate its potential.

Figure 3 - Financial Planning Traps
• Using financial forecasting as a substitute for business planning. • Ignoring historic trends or performances at company, sectoral and national levels. • Overstating market shares and growth, sales forecasts, and profit levels. • Giving insufficient consideration to working capital requirements. • Under-estimating costs and delays likely to be encountered. • Disregarding industry performance norms and competitors' responses. • Breaching generally accepted financial guidelines and ratios. • Making unduly optimistic assumptions about the availability of loans, trade credit, grants, equity etc. • Seeking spurious accuracy while failing to recognise matters of strategic importance.

Realistic views should always be taken of a business's prospects, prospective profits, funding requirements etc. There is often merit in compiling "worst" case projections to complement "most likely" or "best" forecasts. In practice, the realisation of financial projections, especially for a new business without any trading history, might easily take twice as long and cost twice as much as expected. Remember that it is much less painful to deal with a flaw in a business at the planning stage, than later on when commitments have been made and the business has started trading.

6.6. Conclusion

Preparing a set of projections is only a means to an end. Once plans or projections have been approved or in the process of being implemented, they should be regularly updated and compared with the results being achieved.

A plan is only useful if it is being adhered to, if it serves as a benchmark for control purposes, and if the projected outcomes are being realised.

While a clear business plan with sound projections cannot guarantee success, the absence of a plan or poor projections could ensure the eventual failure of a business.

7. The Importance of Cash Flow to a Business

7.1. Importance of Cash

When planning the short- or long-term funding requirements of a business, it is more important to forecast the likely cash requirements than to project profitability etc. Whilst profit, the difference between sales and costs within a specified period, is a vital indicator of the performance of a business, the generation of a profit does not necessarily guarantee its development, or even the survival. **Bear in mind that more businesses fail for lack of cash than for want of profit.**

7.2. Cash vs Profit

Sales and costs and, therefore, profits do not necessarily coincide with their associated cash inflows and outflows. While, a sale may have been secured and goods delivered, the related payment may be deferred as a result of giving credit to the customer. At the same time, payments must be made to suppliers, staff etc., cash must be invested in rebuilding depleted stocks, new equipment may have to be purchased etc.

The net result is that cash receipts often lag cash payments and, whilst profits may be reported, the business may experience a short-term cash shortfall. For this reason it is essential to forecast cash flows as well as project likely profits.

Be realistic about when cash will be received and only record it as a cash flow when it is expected to actually occur.

The following simplified example illustrates the timing differences between profits and cash flows:

Income Statement:	**Month 1**
Sales (P000)	75
Costs (P000)	65
Profit (P000)	10

Cash flows relating to Month 1:	**Month 1**	**Month 2**	**Month 3**	**Total**
Receipts from sales (P000)	20	35	20	75
Payments to suppliers etc. (P000)	40	20	5	65
Net cash flow (P000)	(20)	15	15	10
Cumulative net cash flow (P000)	(20)	(5)	10	10

This shows that the cash associated with the reported profit for Month 1 will not fully materialise until Month 3 and that a serious cash short- fall will be experienced during Month 1 when receipts from sales will total only P20,000 as compared with cash payments to suppliers of P40,000.

In the case of long gestation enterprises like forestry or tree fruit production there may be negative cash flows for 10 or more years. This does not mean the venture is unprofitable. Everything may be proceeding as planned, but cash will have to be found for planting material, fertilisers, fungicides, insecticides and labour. If cash is not available for these items during this period the enterprise will fail although it may be potentially very profitable

7.3. Calculating Cash Flows

Normally, the main sources of cash inflows to a business are receipts from sales, increases in bank loans, proceeds of share issues and asset disposals, and other income such as interest earned. Cash outflows include payments to suppliers and staff, capital and interest repayments for loans, dividends, taxation and capital expenditure.

Net cash flow is the difference between the inflows and outflows within a given period. A projected cumulative positive net cash flow over several periods highlights the capacity of a business to generate surplus cash and, conversely, a cumulative negative cash flow indicates the amount of additional cash required to sustain the business.

Cash flow planning entails forecasting and tabulating all significant cash inflows relating to sales, new loans, interest received etc. and then analysing in detail the timing of expected payments relating to suppliers, wages, other expenses, capital expenditure, loan repayments, dividends, tax, interest payments etc. The difference between the cash in- and out-flows within a given period indicates the net cash flow. When this net cash flow is added to or subtracted from opening bank balances, any likely short-term bank funding requirements can be ascertained.

7.4. Using a Computer

With the aid of a computer and suitable software, a mathematical model can be used to prepare cash flow projections and project short-term banking requirements for a business. The use of a computer-based model reduces the tedium of carrying out numerous repetitive calculations and simplifies the alteration of assumptions and the presentation of results. A computer-based model can be constructed using a spreadsheet or acquired as a stand-alone package. If constructing a spreadsheet model, be aware that it is not as easy as it might seem to build a friendly, robust and error-free planner.

A cash flow model can be used to compile forecasts, assess possible funding requirements and explore the likely financial consequences of alternative strategies. Used effectively, a model can help prevent major planning errors, anticipate problems, identify opportunities to improve cash flow or provide a basis for negotiating short-term funding from a bank.

Generally, when seeking external funding, the time horizon covered by a set of projections should be equal to or greater than the period for which the funding is needed. The greater the amount of funding required and the longer the period of exposure for the provider of these funds, the more comprehensive must be the supporting projections and plan.

Typically, a computer model for short-term bank planning uses assumptions on sales, costs, credit, funding etc. to produce monthly cash flow projections for up to a year ahead. The initial assumptions can be readily altered to evaluate alternative scenarios. For example, a model could be used to explore the extent to which future sales could be increased whilst holding bank borrowings within predetermined limits; to assess the effects on cash flow of varying sales, costs or credit terms; or to determine the likely short-term funding requirements for a business.

There are also computer models for longer term cash flow projections. The further into the future we go the less certain will be the assumptions, but the exercise should still be done. The periods might be quarterly instead of monthly.

Once assumptions on sales, expense payments etc. have been established, a model can be used to produce the cash flow projections which, in turn, indicate the likely future cash balances or banking requirements.

However, the quality of these projections will be completely determined by the standard and reliability of the underlying assumptions. For example, if forecasts for sales, working capital or costs are unrealistic or inadequately researched, then the value of the model's output is greatly diminished. An impressive set of projections is of little benefit if it is unsupported by experience or research or based on mere speculation. In fact, they could be very damaging, or even destroy the business.

7.5. Planning to Plan

Before using a model for short-term cash flow forecasting, a manager or entrepreneur should:

- Decide the central purpose of the exercise (internal planning and control, negotiate a loan etc.)
- Identify the target audience (directors, bank manager etc.)
- Set the time intervals and horizon (e.g. monthly for twelve months)
- Sort out the level of detail required.
- Check that all the necessary key assumptions and data are to hand and have been adequately researched.
- Compile opening balances for all items which will involve cash flows within the forecasting period.
- Think through the likely impact of the critical assumptions on the cash flow projections. If necessary, prepare preliminary forecasts manually to confirm their overall direction and consider the underlying strategic issues relating to sales, funding, costs, stocks etc. As a guide, sales forecasts and debtor & creditor terms are likely to have the most profound impacts on short-term cash flows.

7.6. Planning Pitfalls

When preparing cash flow projections, be aware of the dangers of:

- Overstating sales forecasts
- Underestimating costs and delays likely to be encountered
- Ignoring historic trends or performances by debtors etc.
- Making unduly-optimistic assumptions about the availability of bank loans, credit, grants, equity etc.
- Seeking spurious accuracy whilst failing to recognise matters of strategic importance

These problems can arise as the result of a lack of foresight or knowledge, or because of excessive optimism. They can lead to under-estimation of the cash and other resources required to sustain or develop a business with potentially disastrous consequences.

When forecasting bank requirements and preparing cash flow projections, realistic views should always be taken about future prospects. There is often merit in compiling "worst" case projections to complement "most likely" or "best" forecasts and to accept that the "worst" case might occur and to plan accordingly. There are computer programmes available which offer extensive facilities for doing sensitivity analyses.

7.7. Critically Examine Results

Once the cash flow projections have been prepared, they should be critically examined and used as a management tool to control and improve the business's expected cash position. Issues which might be examined include the following:

- Increasing sales (particularly those involving cash payments) and/or reducing direct and indirect costs;
- Reducing the amount of credit given to customers and/or increasing the credit taken from suppliers;
- Reducing stock levels and improving control over work-in-progress;
- Utilising factoring or discounting facilities to accelerate receipts from sales;
- Deferring major capital expenditure or using alternative financing methods, such as leasing, to gain access to the use, but not ownership, of the assets;
- Re-negotiating bank facilities to reduce charges and/or extend repayment periods;
- Selling off surplus assets or entering into sale and lease-back arrangements;
- Deferring dividends or raising additional equity.
- Once a set of cash flow projections have been prepared, a computer model can be used to explore the impact of alternative measures, such as those described above, on the net cash flow and on bank requirements.

8. Managing Working Capital

8.1. Working Capital Cycle

Cash flows in a cycle into, around and out of a business. It is the business's lifeblood and every manager's primary task is to help keep it flowing and to use the cash flow to generate profits. If a business is operating profitably, then it should, in theory, generate cash surpluses. If it doesn't generate surpluses, the business will eventually run out of cash and expire. But beware, **a business can be operating profitably but still run into severe cash flow difficulties.**

The faster a business expands, the more cash it will need for working capital and investment. The cheapest and best sources of cash exist as working capital right within a business. Good management of working capital will generate cash which will help improve profits and reduce risks. Bear in mind that the cost of providing credit to customers and holding stocks can represent a substantial proportion of a firm's total profits.

There are two elements in the business cycle that absorb cash - **Inventory** (stocks and work-in-progress) and **Receivables** (debtors owing you money). The main sources of cash are **Payables** (your creditors) and **Equity and Loans**.

Each component of working capital (namely inventory, receivables and payables) has two dimensions:

- TIME
- MONEY

When it comes to managing working capital - **TIME IS MONEY**. If you can get money to move faster around the cycle (e.g. collect monies due from debtors more quickly) or reduce the amount of money tied up (e.g. reduce inventory levels relative to sales), the business will generate more cash or it will need to borrow less money to fund working capital. As a consequence, you could reduce the cost of bank interest or you'll have additional *free* money available to support additional sales growth or investment. Similarly, if you can negotiate improved terms with suppliers e.g. get longer credit or an increased credit limit, you effectively create *free* finance to help fund future sales. Extended credit from suppliers means in effect that the supplier is funding your working capital, at least in part. If you are giving your customers credit, then you are funding their working capital.

Many management experts regard inventory as a crime. Many large corporations now practice Just In Time (JIT) inventory control. That means having raw materials or components delivered just as they are needed. Compaq computers are said to operate with less than 20 minutes stock of component parts. It also means not building up inventory of finished product unless there is a very good reason, such as preparing for seasonal demand (Christmas toys)

If You	***Then you***
• Collect receivables (debtors) faster	You release cash from the cycle
• Collect receivables (debtors) slower	Your receivables soak up cash
• Get better credit (in terms of duration or amount) from suppliers	You increase your cash resources
• Shift inventory (stocks) faster	You free up cash
• Move inventory (stocks) slower	You consume more cash

It can be tempting to pay cash, if available, for fixed assets e.g. computers, plant, vehicles etc. If you do pay cash, remember that this is no longer available for working capital. Therefore, if cash is tight, consider other ways of financing capital investment - loans, equity, leasing etc. Similarly, if you pay dividends or increase drawings, these are cash outflows and, like water flowing down a plug hole, they remove liquidity from the business.

Many micro businesses run into severe cash flow problems because cash is withdrawn from the business for consumption.

8.2. Sources of Cash

Sources of additional working capital include the following:

- Existing cash reserves
- Profits (when you secure it as cash !)
- Payables (credit from suppliers)
- New equity or loans from shareholders
- Bank overdrafts or lines of credit
- Long-term loans

8.3. Overtrading

If you have insufficient working capital and try to increase sales, you can easily over-stretch the financial resources of the business. This is called ***overtrading***. Early warning signs include:

- Pressure on existing cash
- Exceptional cash generating activities e.g. offering high discounts for early cash payment
- Bank overdraft exceeds authorised limit
- Seeking greater overdrafts or lines of credit
- Part-paying suppliers or other creditors
- Paying bills in cash to secure additional supplies
- Management pre-occupation with *surviving* rather than managing
- Frequent short-term emergency requests to the bank (to help pay wages, pending receipt of a cheque).

8.4. Handling Receivables (Debtors)

Cash flow can be significantly enhanced if the amounts owing to a business are collected faster. Every business needs to know

- who owes them money
- how much is owed
- how long it is owing
- for what it is owed.

Late payments erode profits and can lead to bad debts.

Slow payment has a crippling effect on business, particularly on small businesses who can least afford it. **If you don't manage debtors, they will begin to manage your business** as you will gradually lose control due to reduced cash flow and, of course, you could experience an increased incidence of bad debt. The following measures will help manage your debtors:

Have the right mental attitude to the control of credit and make sure that it gets the priority it deserves.
Establish clear credit practices as a matter of company policy.
Make sure that these practices are clearly understood by staff, suppliers and customers.
Be professional when accepting new accounts, and especially larger ones.
Check out each customer thoroughly before you offer credit. Use credit agencies, bank references, industry sources etc.

Establish credit limits for each customer... and stick to them.
Continuously review these limits when you suspect tough times are coming or if operating in a volatile sector.
Keep very close to your larger customers.
Invoice promptly and clearly.
Consider charging penalties on overdue accounts.
Consider accepting credit /debit cards as a payment option.
Monitor your debtor balances and ageing schedules, and don't let any debts get too large or too old.

Recognise that the longer someone owes you, the greater the chance you will never get paid. If the average age of your debtors is getting longer, or is already very long, you may need to look for the following possible defects:

- weak credit judgement
- poor collection procedures
- lax enforcement of credit terms
- slow issue of invoices or statements
- errors in invoices or statements
- customer dissatisfaction.

Many debtors are delighted to get invoices with mistakes in them. It is their excuse not to pay for another month or so.

Debtors due over 90 days (unless within agreed credit terms) should generally demand immediate attention. Look for the warning signs of a future bad debt. For example:

- longer credit terms taken with approval, particularly for smaller orders
- use of post-dated checks by debtors who normally settle within agreed terms
- evidence of customers switching to additional suppliers for the same goods
- new customers who are reluctant to give credit references
- receiving part payments from debtors.

Profits only come from paid sales.

The act of collecting money is one which most people dislike for many reasons and therefore put on the long finger because they convince themselves there is something more urgent or important that demand their attention now. **There is**

nothing more important than getting paid for your product or service. A customer who does not pay is not a customer. Here are a few ideas that may help you in collecting money from debtors:

- Develop appropriate procedures for handling late payments.
- Track and pursue late payers.
- Get external help if your own efforts fail.
- Don't feel guilty asking for money.... its yours and you are entitled to it.
- Make that call now. And keep asking until you get some satisfaction.
- In difficult circumstances, take what you can now and agree terms for the remainder. It lessens the problem.
- When asking for your money, *be hard on the issue - but soft on the person*. Don't give the debtor any excuses for not paying.
- Make it your objective to get the money - not to score points or get even.

8.5. Managing Payables (Creditors)

Creditors are a vital part of effective cash management and should be managed carefully to enhance the cash position.

Purchasing initiates cash outflows and an over-zealous purchasing function can create liquidity problems. Consider the following:

- Who authorises purchasing in your company - is it tightly managed or spread among a number of (junior) people?
- Are purchase quantities geared to demand forecasts?
- Do you order quantities which take account of stock-holding and purchasing costs?
- Do you know the cost to the company of carrying stock?
- Do you have alternative sources of supply? If not, get quotes from major suppliers and shop around for the best discounts, credit terms, and reduce dependence on a single supplier.
- How many of your suppliers have a returns policy?
- Are you in a position to pass on cost increases quickly through price increases to your customers?
- If a supplier of goods or services lets you down can you charge back the cost of the delay?
- Can you arrange (with confidence) to have delivery of supplies staggered or on a just-in-time basis?

There is an old adage in business that *if you can buy well then you can sell well*.

Management of your creditors and suppliers is just as important as the management of your debtors. It is important to look after your creditors - slow payment by you may create ill-feeling and can signal that your company is inefficient (or in trouble!).

Remember, a good supplier is someone who will work with you to enhance the future viability and profitability of your company.

8.6. Inventory Management

Managing inventory is a juggling act. Excessive stocks can place a heavy burden on the cash resources of a business. Insufficient stocks can result in lost sales, delays for customers etc. while it is tempting to believe that we should always carry enough inventory to guard against the remotest possibility of a stock out, this is not always the correct thing to do. There are statistical models which can be used to help calculate ideal inventory levels and which balance the cost of stock outs and excessive inventory. Increasingly companies are using stockless purchase orders. This requires suppliers to carry a certain level of dedicated stocks which are then delivered as required.

The key is to know how quickly your overall stock is moving or, put another way, how long each item of stock sit on shelves before being sold. Obviously, average stock-holding periods will be influenced by the nature of the business. For example, a fresh vegetable shop might turn over its entire stock every few days while a motor factor would be much slower as it may carry a wide range of rarely-used spare parts in case somebody needs them.

Nowadays, many large manufacturers operate on a *just-in-time* (JIT) basis whereby all the components to be assembled on a particular today, arrive at the factory early that morning, no earlier - no later. This helps to minimise manufacturing costs as JIT stocks take up little space, minimise stock-holding and virtually eliminate the risks of obsolete or damaged stock. Because JIT manufacturers hold stock for a very short time, they are able to conserve substantial cash. JIT is a good model to strive for as it embraces all the principles of prudent stock management.

The key issue for a business is to identify the fast and slow stock movers with the objectives of establishing optimum stock levels for each category and, thereby, minimise the cash tied up in stocks. Factors to be considered when determining optimum stock levels include:

- What are the projected sales of each product?

- How widely available are raw materials, components etc.?
- How long does it take for delivery by suppliers?
- Can you remove slow movers from your product range without compromising best sellers?

Remember that stock sitting on shelves for long periods of time ties up money which is not working for you. For better stock control, try the following:

- Review the effectiveness of existing purchasing and inventory systems.
- Know the stock turn for all major items of inventory.
- Apply tight controls to the *significant few* items and simplify controls for the *trivial many*.
- Sell off outdated or slow moving merchandise - it gets more difficult to sell the longer you keep it.
- Consider having part of your product out sourced to another manufacturer rather than make it yourself.
- Review your security procedures to ensure that no stock "is going out the back door !"

Higher than necessary stock levels tie up cash and cost more in insurance, accommodation costs and interest charges. Stocks also require storage space and this can also be expensive.

8.7. Key Working Capital Ratios

The following, easily calculated, ratios are important measures of working capital utilisation.

Ratio	Formulae	Result	Interpretation
Stock Turnover (in days)	Average Stock * 365/ Cost of Goods Sold	= x days	On average, you turn over the value of your entire stock every x days. You may need to break this down into product groups for effective stock management. Obsolete stock, slow moving lines will extend overall stock turnover days. Faster production, fewer product lines, just in time ordering will reduce average days.
Receivables Ratio	Debtors * 365/ Sales	= x days	It take you on average x days to collect monies due to you. If your official

(in days)			credit terms are 45 day and it takes you 65 days... why ? One or more large or slow debts can drag out the average days. Effective debtor management will minimize the days.
Payables Ratio (in days)	Creditors * 365/ Cost of Sales (or Purchases)	= x days	On average, you pay your suppliers every x days. If you negotiate better credit terms this will increase. If you pay earlier, say, to get a discount this will decline. If you simply defer paying your suppliers (without agreement) this will also increase - but your reputation, the quality of service and any flexibility provided by your suppliers may suffer.
Current Ratio	Total Current Assets/ Total Current Liabilities	= x times	Current Assets are assets that you can readily turn in to cash or will do so within 12 months in the course of business. Current Liabilities are amount you are due to pay within the coming 12 months. For example, 1.5 times means that you should be able to lay your hands on $1.50 for every $1.00 you owe. Less than 1 times e.g. 0.75 means that you could have liquidity problems and be under pressure to generate sufficient cash to meet oncoming demands.
Quick Ratio	(Total Current Assets - Inventory)/ Total Current Liabilities	= x times	Similar to the Current Ratio but takes account of the fact that it may take time to convert inventory into cash.
Working Capital Ratio	(Inventory + Receivables - Payables)/ Sales	As % Sales	A high percentage means that working capital needs are high relative to your sales

Other working capital measures include the following:

- Bad debts expressed as a percentage of sales.
- Cost of bank loans, lines of credit, invoice discounting etc.

- Debtor concentration - degree of dependency on a limited number of customers.

Once ratios have been established for your business, it is important to track them over time and to compare them with ratios for other comparable businesses or industry sectors.

When planning the development of a business, it is critical that the impact of working capital be fully assessed when making cash flow forecasts.

9. The market plan

The market plan should begin with an outline of the marketing strategy. This would include:

- the target market
- pricing decisions
- distribution
- promotional activities
- personal selling decisions

9.1. marketing plan

Section	Content
i. Executive summary	Presents a short overview of the issues, objectives, strategy, and actions recorded in the plan and their expected outcomes for quick management review
ii. Current situation	Summarises relevant background information on the market, competition, past performance, and various elements of the marketing programme.
Iii. Key issues	Identifies the main opportunities and threats that the plan must deal with and the relative strengths and weaknesses of the product and business unit that must be taken into account when facing these issues
iv. Objectives	Specifies the goals that must be accomplished in terms of sales volume, market share and profit
v. Marketing strategy	Summarises the overall strategic approach that will be used to achieve the plan's objectives
vi Action plans	This is the most critical section of the plan. It specifies • **what** specific actions are to be taken • **who** is responsible for each action • **when** the action will be engaged in • **how much** will be budgeted for each action
vii.Projected P&L statement	Presents the expected financial payoffs from the plan
viii. Controls	Discusses how the plans progress will be monitored. May present contingency plans if performance falls below expectations or if the situation changes

10.Budgeting

10.1. The budget

Budgets are the basis on which a business, through estimating its income and expenditure, plans its financial requirements and against which the business or outside agencies monitor performance. The budget is a framework against which performance can be measured and variances from budget are signals to management that all is not as forecast and plans may need to be modified or other corrective action taken. Performance under each budget heading should be monitored separately. A favourable variance under one budget item might mask an unfavourable one under a different budget item and this would not become apparent if only the overall performance is looked at and a serious problem might not come to light until it is too late.

Budgeting is usually done for a number of different time periods e.g. monthly, quarterly, annually and sometimes for a period of several years. Obviously the shorter the budget period the more detailed the budget should be and with much more control over and certainty about short term events the more accurate the budget should be.

The fact that little may be known about events in 5 or 10 years time should not prevent the exercise being done. For some enterprises such as fruit growing when most of the capital expenditure is undertaken in year 1 and income may not start until year 3 or even year 5 or later. Forest tree production will have an even longer gestating period.

Projections for yield and price can only be made on the basis of the best information that is available at the time of preparing the budget. In preparing a budget, therefore, assumptions must be made using this information. In the business plan these assumptions should be stipulated and the more riskier ones highlighted

Budgets should be tight but realistic. It is important to remember that ***there is nothing to be gained and a lot to lose from preparing budgets that are unrealistically tight. This usually leads to cash flow problems at a most critical time. Most small businesses that fail during their first 1 to 3 years do so because of unrealistic cash flow projections which stems mainly from under estimating recurrent costs during that period.***

It is on the ability to plan well and to implement the plan while achieving the targets set out that performance will be judged. This is always an important criterion for financial institutions to base their decisions on a business' credit rating for future loans.

For example, if 100,000 is budgeted under a particular budget heading in the plan and the actual expenditure is 120,000 the business will be judged to have missed the performance target by 20%. There will be an unfavourable variance of 20%.

Suppose now on the other hand that same plan was submitted but with 125,000 budgeted under this budget heading. Suppose also that the actual expenditure is now124,000. Even though the business will have actually spent more money than under budget 1 there will be a positive budget variance. The business will have achieved its target and will be regarded as operating successfully in terms of both budgeting and control.

More importantly it will be likely to have made adequate provision for its cash requirements for the budget period and will be less likely to run into problems with its financiers, suppliers or workers.

11. Contingency Planning

Because all strategies and the action plans to implement them are based on assumptions about the future, they are subject to considerable risk. **Assumptions are not facts.** If any or all of the assumptions turn out to be wrong action should be taken to modify the plan.

A contingency planning process that includes the elements shown in Fig x should be followed.

Identify critical assumptions about the future

Estimate probability of each critical assumption being right

Rank order critical assumptions

Monitor action plan

Set triggers to activate contingency plan

Specify alternative response options