Startup Business Planning

When starting your own business, you should avoid the Christopher Columbus approach. When he set out on his journey he didn't know where he was going. He didn't know where he was when he arrived. And when he got back, he didn't know where he had been.

How do you avoid this?

The answer is to prepare a business plan. In fact, research has shown that over 50% of businesses that start without a business plan fail within the first two years.

This strongly indicates that success in modern business requires planning. And if you're looking to get financing from the bank or investors a properly prepared business plan is a must. So it makes good sense at an early stage to seek advice and assistance to ensure that your business is set up on a sound footing. That’s where we can help you.

Are you up to it?

Before you carry out any detailed work it's a good idea to analyse your business idea and what your basic commercial strategy will be. Ask yourself:

- What exactly is the product or service you are selling?
- Is it, or how will it be, ready for its market?
- How do you go from the developed product to the first sale?
- Where, exactly, are those first sales coming from?
- Who will achieve this?
- What do you expect your business to be doing in a few years' time?
- Who will be achieving that?

You, the entrepreneur, will be playing a developing role in this business. And your role in the business will change over time. Perhaps to start with you'll do almost everything in the business, but if you're planning to expand can that remain the case? It's unlikely. You role in the business will therefore have to change over time as you gradually bring in people.

To help think about what will be needed think about these questions. How are you going to drive the business forward? How will you get those vital sales at the right margins? How will production schedules be met and the business be administered so that you know where you are? How will you get the reliable and up to date management information you'll need? And how will you lead the development of the team managers that you'll need in order to achieve your expansion?

If you don't know, or you are just a brilliant inventor who does not really care, stop now!

Finally, do not underestimate the amount of time required to establish and finance a new business venture. It can take six months, and maybe longer in some cases, to get things in place.

First project appraisal

Before you get into the detailed business planning it's a good idea to work through a first appraisal of your business idea. This is so you don't get bogged down in detail, and instead get the important elements clearly in your mind. Taking independent advice may be necessary to do this.

Imagine yourself in the position of a potential investor in your business. Is the business idea strong enough that you'd be tempted to make the investment if this was someone else's idea?

When it's done well, your self-appraisal will match the appraisal that the bank or other investors would make of the major elements of your business. This makes it much more straight-forward for you to obtain the finance you need.

How do you do it?

Start with the three 'M's: Management, Marketing and Margin.

Without competent management, a properly understood market into which the product will sell, and more than adequate margins from trading, there will be little point in taking the business further.

You can't assume that all these elements will be there because of how good the product or service is. You need to be able to demonstrate, by independent evidence, that each of these elements is present in the business.

The product, the market, the management team and an appropriate commercial strategy all go together.

And if your aim is expansion, you'll also need to consider how your commercial strategy is going to cope with further products or services and how those will be developed for, and then be sold into, their respective markets.

Let's take the three 'M's one at a time.

Management

'Management' encompasses the production, marketing, financial, administration and leadership skills needed by the business. These skills are rarely all present in one person so a team is normally needed.

Of course, if you're starting a very small business your team might include external advisors that supplement and support you in the areas where you lack a particular skill.

When it comes to looking at the team each member needs to be experienced in the right areas, complementary to you and one another, and have a determination to make your business succeed.

If you're looking to hire someone then scrutinise their application and curriculum vitae carefully to ensure that the right elements are there. And make sure you take up all references.

So in considering the first 'M', management, write down a list of all the skills needed to manage the business effectively. Then next to each skill write the name of the person who will cover that area.

Markets and marketing strategy

'Markets' involves answering the question: who are or will be your customers?

The most frequent failing in startup situations is a lack of considering where sales will come from.

You need to be realistic. While it's tempting to assume that customers will appear and to prepare cashflows showing sales progressively increasing, banks and investors will want to know more. The only way to find this out is to research the market and get independent perspectives.

Consider: who are your target customers? How many are there? How will you reach them? What will your goods or service do for them? Do they know they have a need for your product or service, or will some awareness marketing be required? Can they satisfy their need in another way, such as by alternative product? Why will they choose your product or service? Who are your competitors, direct and indirect?

Margins

'Margins' involves the difference between the price you can sell at and what it costs you to buy or supply your product or service.

There will be typical margins for your industry and on your range of products and services. You'll usually have a good idea of your costs, but it's important to make sure that you've thought about all possible costs. Including what might happen if prices of your supplies were to increase.

The more difficult area can be that of pricing.

You'll find that your potential customers will vary in how sensitive they are to pricing. At one extreme a customer may be willing to pay any price, and at the other extreme a customer may expect to pay very little. What then are the limits, top and bottom, for how you can price your product or service?

It isn't necessary for you to target every customer in your potential market, but will your pricing allow you access to enough potential customers for you to be able to turn an overall profit.

Unfortunately it's quite rare to be able to just set your own price. Competitors in your target market may already have led to expectations in the customer base when it comes to pricing. In addition, established competitors may respond to your entry into the market with aggressive pricing strategies that make it difficult for you to get established. How much of a threat would this be to you? And how would you deal with it?

Whether you can set your own price or whether the price is dictated to you by the market, it's important to understand the effect a high or low margin will have on your business.

Higher margins, although very desirable, are more vulnerable to competition.

On the other hand, low margins require a controlled type of business. The business needs to be highly flexible and have a strict control over its working capital.

Business plan

Now that you've got the critical elements of your business in mind you're in a position to start working on the detailed business plan.

To be worth its salt your business plan should convey your drive, character and determination.

What exactly should it contain?

It needs to start with a summary of the business, people, proposal and the finance sought.

And then it should give details of:

- The business.
- The market.
- The management/employees.
- The product or service.
- How sales will be achieved.
- The costs.
- The margins.
- Projected profits, cash flows and balance sheets.
- How much finance is required and how you propose to use it.
- The main risks and the potential impact on the business of those risks. Also showing how you would manage or cope with those risks.
- How the business will be developed and administered.
- The longer term view and the commercial strategy of the business.

You should use appendices to cover the trading terms and assumptions on which you've based your projections. All the detailed forecasting should be included in the appendices.

If you have details about customers, suppliers and the CVs of key personnel then these can also be included in the appendices.

Projections and models can easily get out of hand so take care not to get overwhelmed by the detail. At all times try to make sure that the business plan is focused on the critical elements we've discussed above.

Financing the business

Having determined that your business idea is workable and had potential then it's time to consider how you'll finance the business.

It's a good idea to plan and structure for this from the start. Businesses are more likely to fail because of inadequate finance than because of being unprofitable.

The objective for structuring the finance of your business is to obtain a proposition that appeals to bankers or investors, and that you get finance in a form that's matched to your needs.

Most businesses ultimately continue on the strength of the confidence of their bankers. So, if you insist on carrying on against the better judgment of the bank manager there's a very high risk that you'll launch a business which is likely to fail.

The funding of the business should enable it to survive any reasonable period of misfortune. Until that position is reached the business will be fragile and potential investors and bankers are likely to take a cautious view.

For this reason, and so that additional funds can be raised later for expansion, an adequate equity base is essential.

You will need to budget forward, usually for more than one year, and project cash flows and balance sheets. You'll need to consider and be able to demonstrate how sensitive those projections are to any trading assumptions you will make. For instance, if the assumption is that sales will increase at the rate of 5% a month, what happens if you only achieve 3% a month?

As you start the process of raising finance for your business, consider:

- Do I really appreciate how much I need?
- What equity do I have available?
- What types of other finance are normally available?
- How long will the finance be needed according to the cash flow?
- What will the finance be used for?
- To what purpose will the finance be put?
- What range of working capital requirement is likely?
- What reward will the investor get? In other words, why would this be attractive to them?

There are a variety of finance options available to businesses. Read on as we consider some of these.

Banks

As indicated earlier, banks are a very common source of finance. Both overdrafts and term loans are useful forms of financing. Some banks will also offer or have connections with invoice discounting services.

In looking to obtain finance from a bank it's good to think about the bank's point of view. What are they looking to achieve? When you do this you can present your business to them in the most effective way.

The overriding priority for a bank is that they want their money back. So while they will use higher interest rates in cases where they see the risk as high, their primary consideration is the risk of not getting the money back.

When they offer term loans that are secured on your assets they're looking to see that even in a fire sale the loan amount is covered.

Overdrafts shouldn't be higher than the value of stock and debtors. If this isn't the case then the bank will likely look for more long-term finance to be in place.

In addition to security, bankers will look at the 'gearing' of the business. Gearing is the proportion of borrowed money against your own money in the business. This is commonly referred to as the debt/equity ratio.

Bankers will often say they prefer that proportion to be about 1:1. And they become very reluctant to lend when the gearing proportion moves higher than 2:1.

Owners' equity

This is the money that you, along with any other owners, put into the business.

Usually a bank or another investor will look to see that you're putting a stake into the business yourself. After all if you're not prepared to invest in your own business then why should they?

Even if you have very little capital in your own name there are various possibilities for raising funds in your own name. Some possibilities would include loan-backs, endowment policies and the tax reliefs available to relatives and friends for their investment.

Institutions

For many small businesses, the thought of allowing someone else to own shares in what is considered to be a family business prevents them from looking at outside or institutional equity investment.

However, there are a number of organisations that are prepared to take a minority holding in a small business.

Of course, you may need to accept that you will not be able to retain 100% ownership of your prospective business.

Government sources

Government can also be another source of finance.

These could include Government grants and schemes relating to the purchase of fixed assets and training programmes.

Currently there are a number of tax reliefs, deductions and exemptions available from Revenue to assist startup businesses.

Leasing and hire purchase

Rather than obtaining a cash loan from the bank, leasing and hire purchase can be a good option.

These will typically be related specifically to the particular asset you want to purchase and may give you more favourable terms or impose less strict lending requirements than a bank. It's good, however, to consider and compare interest rates.

Legal entity

You will need to consider the type of legal structure under which your business will operate. The most common in Ireland are:

Sole trader

A sole trader is a person in business on his own account. There are no statutory requirements governing the format of a sole trader's accounting records nor is it necessary to have them audited.

If sales are above a certain limit or made in certain territories a sole trader is required to register for VAT. And if anyone is employed by the business then registration for PAYE is required. Both areas would involve maintaining sufficient records and making returns to Revenue.

A sole trader is personally liable for all liabilities of the business.

Partnership

A partnership is where two or more (generally up to a maximum of 20) individuals enter into a business which is governed by the Partnership Act 1890 and/or a partnership agreement.

The requirements in relation to accounting records and audit are similar to those of a sole trader.

In general, each partner's liability is unlimited.

Limited company

Such companies are incorporated under the Companies Act 2014 which impose accounting, audit and public disclosure requirements.

An individual shareholder's liability is limited to the amount of his share capital (both called and uncalled) in the company.

If this entity is selected the choice of the shareholders, both at, and after, formation, requires consideration to avoid possible income tax and inheritance tax problems in the future.

You should seek the advice of your accountant in determining the legal entity most appropriate to your particular circumstances.

Conclusion

As we have shown, there are three critical elements to a successful business - Management, Markets and Margins.

It's necessary to assess your market and the product or service you are selling into that market.

You need to establish the profit margin which that market will provide to you and have contingencies in place to manage the variables of achieving this. Of course having the correct financing in place is key too.

And above all you have to ensure that management is responsible, disciplined and has the necessary skills to run a business. Most small business failures are the result of inexperienced management.

Call Now

To see how we can help you in planning your business startup why not call Seamus Parfrey today on **021 431 0266**.

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