**Chapter Three**

**Business Planning**

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| **Chapter Objectives**  *After the discussion of this chapter, students must;*   * *Have the concept of how to prepare a business plan for different enterprise* * *List the advantage of preparing business plan* * *Recognize different components of a given business plan* |

**What is Business Plan?**

A business plan is a roadmap for starting and running a business. A well-crafted business plan identifies opportunities, scans the external and internal environment to assess the feasibility of business and allocates resources in the best possible way, which finally leads to the success of the plan. A business plan is a written proposal addressed to potential lenders or investors. Typically, it describes a new business and tells why it is deserving of financial support.

Doing a business plan involves a great deal of research. Because there is so much information to be drawn from so many different sources, you can easily feel overwhelmed.

**The objectives of Business plan**

* To give directions to the vision formulated by the entrepreneurs
* To objectively evaluate the prospects of business
* To monitor the progress after implementing the plan
* To persuade others to join the business
* To seek loans from financial institutions
* To visualize the concept in terms of market availability, organizational, operational and financial feasibility
* To clarify challenges in terms of opportunities and threats from the external market
* To clarify ideas and identify gaps in management information about their business, competitors and the market.
* To identify the resources required to implement the plan

**When business plans are produced?**

1. **At the start up of a new business**

After the initial stage of developing ideas and feasibility study are over, a new business may start up through a detailed planning stage of which the main output is the business plan.

2. **Business purchase**

Buying an existing business does not negate the need for an initial business plan. A detailed plan tests the sensitivity changes to key business variables. This helps to understand the level of risk that are accepted and the likelihood of rewards being available for the buyers.

3. **Ongoing process**

Ongoing review of progress, against the objectives of either a new business or a small business purchase is important in a dynamic environment. A periodic review with the business plan is required in the constantly changing environment. A business plan should be the live, strategic, and technical planning focusing on how a small business responds to the inevitable changes around it.

4. **Major decisions**

Even if planning is not carried out on a regular basis, it is usually instigated at a time of major change.

**II. Who makes the business plans?**

Three types of people are interested in a business plan:

1. the managers who run the business on a day to day basis
2. the owners, or prospective equity investors
3. the lenders, who are advancing loans for the enterprise

1. **Managers**

They are involved in small business planning both as producers and recipients of the plan. The management of a small enterprise is the only people likely to be sufficiently knowledgeable to produce a business plan. Business plans are also written to aid small business managers.

2. **Owners**

The managers of a small enterprise may also be the owners and take a keen interest in the planning process. A plan may be intended for prospective equity partners, either a sleeping partner looking for an investment, or an active partner looking to join an existing small business. Owners may also be lenders, who take an equity stake in return for providing loans.

3. **Lenders**

Banks are the main recipients of business plan. They encourage the production of business plans to justify overdrafts and loans offering literature and advice and putting together business plans. Other lenders of money, from private individuals to venture capital companies, will also expect to make their investment decision after the presentation of a formal business plan.

**Preparing a business Plan**

The various steps involved in preparing the business plan are:

* 1. **Preliminary Investigation:** Before preparing the plan entrepreneur should:
     + Review available business plan (if any)
     + Draw key business assumptions on which the plans will be based( e.g. inflation, exchange rate, market growth, competitive pressure, etc)
     + Scan the external and internal environment to assess the strengths, weakness, opportunities and threats
     + Seek professional advices from friends/relatives or a person who is already into similar business (if any)
  2. **Business Planning Process**: The business plan acts as a guiding tool to the entrepreneur and is dynamic in nature-it needs continuous review and updating so that the plan remain viable even in changing business situation.

1. **Idea Generation**: Idea generation is the first stage of business planning process. It involves generation of new concepts, ideas, products or services to satisfy the existing demands, latent demands and future demands of the market. The various sources of the new ideas are: Consumers/customers, Existing companies, research, employees, dealers and retailers.
2. **Environmental Scanning**: Once a promising idea emerges, the next step is environmental scanning, which is carried out to analyze the prospective strength, weakness, opportunities and threats of the business enterprise. The different variable to be scanned in terms of socio-cultural, economic, governmental, technological, demographic changes taking place in the external environment and availability of raw materials, machinery, finance, human resource etc. with the entrepreneur.

**External Environment:**

***Socio-Cultural Appraisal****:* It assesses the social and cultural norms of a society in a given period of time. The variables are: Values, beliefs, norms, fashions and fads of a particular society.

***Technological Appraisal****:* It assesses the various technological know-how available to convert the idea into a product.

***Economical Appraisal***: The status of the economy in a given society in terms of inflation, per capital income and consumption pattern, balance of payment etc.

***Demographic Appraisal****:* it refers the over all population pattern of a given geographical region. It includes variables like: Age profile, distribution, sex, education profile, income distribution etc. It helps in identifying the size of the target customer.

***Governmental Appraisal***: it assesses the various legislation, policies, incentives, subsides, grants, procedures etc formulated by government for a particular industry. The softer the government norms for the industry, the easier it is for the entrepreneur to establish and run the business.

**Internal Environment**

***Raw Materials****:* The availability of raw materials now and near in the future.

***Production/operation****:* the availability of machineries, equipment, tools and techniques that would be required for production/operation.

***Finance***: total requirement of finance in terms of start-up expenses, fixed expenses and running expenses. It also indicates the sources of finance that can be approached for funding.

***Human Resources***: Kind of human resources required and its demand and supply in the market. This further helps in estimating the cost and level of competition in hiring and retaining the human resources.

**III. Feasibility Analysis:** feasibility analysis is done to find whether the proposed project would be feasible or not. The various variables or dimensions are:

**A. Market Analysis**: The market analysis is an important first step in determining if you have a viable business idea, and how best to proceed. The market analysis will explore the practical aspects of producing your product or service:

* Is there a need current, emerging, unmet – for this product or service?
* What raw materials or resources would be needed?
* Where and how would you obtain them? At what cost?
* Will you need special equipment or manpower to produce this product, or special training or credentials to provide this service?
* Who and how many others are doing something similar to what you’re planning?
* Who would be likely to buy, benefit and/or invest in such a product or service offering?
* Whose likely to buy how much of what you’re selling, how often?
* Would this product or service appeal to a wide audience, or would it meet the specific needs of a select few?
* Conversely, is this product or service controversial, closely regulated, or subject to public approval?
* Is location a critical factor?
* Are there cultural or community factors influencing the market?
* How are you uniquely equipped to fill the gap between supply and demand
* How would you reach your target customer?

**B. Operational Analysis:** This is done to evaluate the operational ability of the proposed business enterprise. Key questions to be answered are:

* + What equipment does the proposed business need?
  + From where to be obtained?

Technical/operational analysis collects data on the following parameters

* + - **Material Availability:** the availability of raw material required for production. The availability of quality and quantity material, the factors on which the availability of raw material is dependent, price sensitivity of raw material and perish ability of raw material.
    - **Plant location**: While choosing the business location, the following elements should be taken into consideration:

I. **Vicinity to raw material**: the closer the plant to the place where raw material is the better it is. It helps in reducing the transportation cost and in case of perishable goods it also helps in reaching its destination with safe time.

II. **Availability of power:** constant availability of power is power must for the success of any business enterprise.

III. **Availability of labor**: the availability of skilled human resources

IV. **Proximity to the market:** proximity to the market enables the business to be in closer contact to the needs of the business market.

v. **Machinery and equipment**: is dependent on production technology, plant capacity, investment cost of buying, maintenance and running cost.

**C. BUSINESS STRUCTURE**

Choosing a structure for the business or organization sets the tone for how your business will operate, tax and insurance considerations, and disbursements of any profits. Consult an attorney for legal guidance on business structure, leases, contracts and other elements designed to protect your business relationships and help your business prosper. The most common business structures include:

* Sole Proprietorship – An individual operates the business, and there are no outside investors.

This is the simplest way of doing business and the most common form of business structure.

However, the individual can be exposed to personal liability for every act and debt of the business, and there is no room for expanding through new owners or their capital. Also some of the tax deductions available to other forms of business are not available to the sole proprietor.

* **General Partnership** – When two or more people create a business, a general partnership is formed. Their partnership is based upon an agreement to operate the business together, and the partners are jointly and severally liable for all obligations of the partnership. The partnership files an “informational” tax return, and the partners must report their portion of the partnership’s earnings or loss on their individual income tax returns.
* **Limited Partnership** – This is a special form of partnership where some of the partners are in charge of managing the day-to-day activities of the business (general partners), and the others (limited partners) are silent investors and do not participate in the day-to-day activities. The general partners are jointly and severally liable for the partnership, and the limited partners are only liable for partnership debts to the extent of their investment.
* **LLC** – Cooperatives are employee owned companies. All profits earned by the company are passed to the owners. A Limited Liability Company (LLC) is established by an operating agreement, similar to the bylaws of a corporation. The LLC is taxed like a partnership, but liability is limited like a corporation.
* **Corporation** – The Corporation is a separate legal entity, wholly apart from the individual shareholders who own it. A “C” corporation may have more than one form of stock (such as common and preferred), it may have a limited number of shareholders, and taxes on its profits are paid by the corporation as a separate taxpaying entity (this can result in “double taxation” where the company’s profits are taxed and any income the company’s owners receive.
  + **VISION AND MISSION**

The vision and mission statements for your business are usually broad statements that describe the guiding principles for your business or organization, and objectives spell out the primary reasoning about what the company hopes to accomplish. These guiding principles can be used as a tool to evaluate new prospects and to help keep the business on track.

* **ORGANIZATIONAL STRUCTURE**

The organizational structure details the key job positions and titles, both present and future, responsibilities, skills and qualifications, as well as the reporting structure. Any personnel already on board, particularly those with industry experience or specialized training should be included. The total number of employees, training and development plan, salaries and benefits are important information.

**D. Financial Feasibility**

I. **Cost of land and building**: the requirement and the availability of funds that land and building can be taken on lease or purchased

II. **Cost of plant and machinery:** includes estimates of cost of plant and machineries, their running and maintenance cost.

III. **Preliminary cost estimation**: is made to assess how much cost would be required in conducting market survey, preparing feasibility report, expenses in registering and incorporating machine, establishment costs and etc.

III. **Provision of contingency**: unexpected expenses which can emerged due to change in the external environment, like increase in price of raw material, or transport costs going up.

V. **Working capital estimation**

Vi. **Cost of production**: include raw material cost, labor cost, overhead expenses, utilities like power, water, fuel, etc.

Vii. **Sales estimation**

Viii. **Profitability projection**

**Format of a business plan report**

1. Cover Sheet(Name of the company, address, promoters)
2. Table of content
3. Executive summary
4. The business
   1. Objective of setting up business
   2. Brief history of past performance (if any)
   3. Form of ownership
   4. Name, qualification of the owner
   5. Proposed/head quarters
5. The funding requirement
   1. Debt
   2. Equity
6. The product/service
   1. Description of product/service
   2. Patents, trademarks, copyrights

VII. The plan

* 1. Marketing plan
* Market demography
* Strength and weakness of competition
* SWOT analysis of the market
* Marketing strategy mix
  1. Operational plan

1. Plant location
2. Plant layout
3. Material requirement
4. Inventory management
5. Quality control
   1. Organizational Plan
   * Organizational chart
   * Detail about the board of directors
   * Manpower planning
   1. Financial plan for 2-5 years

* For existing companies, a summary of previous financial data
* Projected sales
* Projected income and expenditure statement
* Projected breakeven point
* Projected profit and loss statement
* Projected balance sheet
* Projected cash flow

VIII. Critical Risks

IX. Exit strategy

X. Appendix

a. CV of the owner

b. Ownership agreement

c. Articles of association

**The Importance of a Business Plan**

1. It forces you to analyze all facets of your business – good and bad.

2. It sets financial goals and guidelines.

3. It establishes operating goals, sets priorities, and helps you develop strategies (i.e., how will I find a steady stream of customers? How can I be sure the business will be profitable?

4. It is absolutely necessary if you are going to persuade investors and lenders.

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| **Activities**   1. *Sketch the business plan format*   2. *What the sensitivity analysis tells you in business plan* |