7 MISTAKES TO AVOID IN YOUR BUSINESS PLAN

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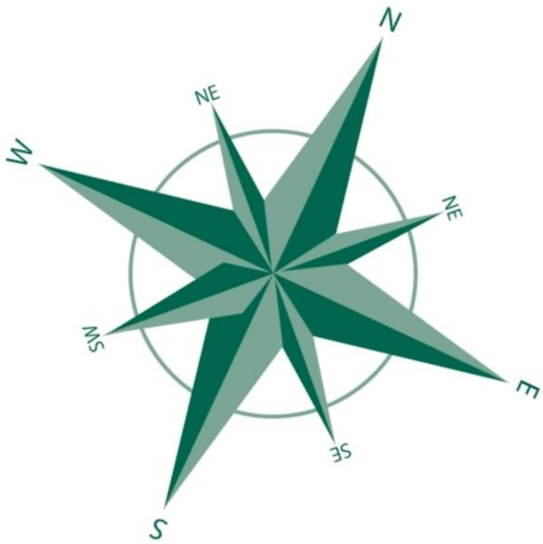

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CONCEPT

The process of writing a business plan means that you have to consider where you would like to be in 3 or 5 years, how you plan to get there, what level of funding you will need and how best to manage your cashflow.

Get all of this right and you are more likely to be successful.

Unfortunately, most businesses will either fail completely or at least fail to achieve the level of success the owner expected.

Many business owners are obliged to write a business plan only when they want external funding, which pushes them to consider their goals and evaluate the level of funding required to achieve them.

Regardless of whether you need external finance, you are investing your own money and your valuable time, so the good discipline of constructing your business plan is even more important for you.

This e-book is about mistakes that people make when compiling a business plan. For most, this relates to whether or not the business plan will help them get external funding, yet they are just important if you're self-funding.

If you don't need external funding, still write a business plan and imagine yourself as an external investor and judge it against these typical mistakes

If you avoid the mistakes identified in this e-book, you'll not only have a better chance of getting funding, you'll also improve your chances of succeeding with your business.

Each of the following sections discusses a typical mistake and how to avoid it.

1. CREDIBILITY

You and your team have to be credible in relation to the amount requested, both in terms of relevant expertise and your track record in business.

If someone applies for a job with a salary of £100,000 per year and they currently earn £75,000 that's credible, whereas if they currently earn £35,000, that's likely to stretch credibility a little too far and they won't even make the cut for interview.

It's the same with your business. Do you have a credible track record of running a similar sized business in a similar market as that presented in your business plan?

- A lender needs to have confidence in your ability to run the business profitably until the debt is fully repaid
- An investor needs to believe that you can deliver the return on investment within the proposed exit timeframe
- Partners will need to believe in you before committing

In particular, readers of your business plan will be assessing your credibility in terms of Aspiration, Comprehension and Inspiration.

Aspiration – The scope of your aspiration has to be appropriate for the level of investment:

If your aspiration is too ambitious or too modest, it will be deemed too risky

Comprehension – You will be expected to have in-depth knowledge of your market and the solutions of your likely competitors.

Your understanding of finance has to be credible, especially the relationship between the investment and return and how the return will be realised and in what timescale, i.e. the exit strategy.

Inspiration – Your ability to lead your team to success and exhibit the tenacity to overcome the inevitable obstacles you will encounter along the way.

In order for your business plan to succeed in gaining funding, you need to emphasise your relevant experience and that of your team. Also, identify any areas of weakness within your team, for example on marketing or finance and indicate how you intend to solve this; perhaps once the funding is received.

An investor or partner will also view your team objectively as an outsider, which may reveal people in positions beyond their competence. This may have resulted from their ability to bring initial funding to the enterprise.

It may not even have become apparent as yet, but the investor or partner will look ahead and consider whether the competence, personality or commitment may be exceeded as the business grows with consequent growth in management responsibilities.

TYPICAL MISTAKE

Aiming for glory too soon, with a team that isn't yet credible with no reference in the plan to how you intend to augment the team to fill any gaps in expertise.

Investors especially dislike having their time wasted, so don't blow it too early; you may need them later, when you're properly ready.

REMEDY

Work out sensible steps, with appropriate funding and build on each previous achievement to secure the next level of funding. Many businesses have successfully grown through a chain of funding.

If the business can't yet justify a full time position for an area of expertise, include costs for a sub-contracted specialist.

2. MARKET ANALYSIS

Lenders and investors become irritated by business plans that quote a market for the product or service as enormous and then fail to quantify it. They want to see detailed knowledge and understanding of the market, its growth prospects and the competition.

If you say that there's virtually no competition, investors are less likely to think it's a great opportunity and more likely to think that there's no proven market.

An investor will be less interested if the market isn't sufficiently large for your business to scale up in the future, so you may be limited to other forms of finance, such as a bank loan.

If the market isn't growing, the only way you can grow your business is by taking customers from the competition, so your analysis has to include any significant competitors and their strengths and weaknesses.

Explain what advantages you have or will have over the competition through technology or process in order to grow your share of the market. Otherwise, lenders and investors know you'll be fighting on price, which means lower margins and more risk.

A well researched and structured market analysis must contain numbers that can be verified

You need to show that you've researched the number of potential customers in your region and the typical purchasing patterns.

Lenders and investors will want to satisfy themselves that the volumes shown in your projections are realistic for the size of the market and the prices you aim to charge compared to competitors?

TYPICAL MISTAKE

Sales projections are based on the size of the market i.e. taking an estimate of the size of the market and then basing your projections on a share of that market.

Lenders and investors dislike plans that say, 'if we get just 1% of this market, our turnover will be ...'

They will consider it to be lazy, flawed and unrealistic, all of which leads to a lack of credibility and a resounding NO.

REMEDY

Build your projections based on your competitive value proposition and a realistic and affordable marketing plan, see the next section.

Then use an estimate of the size of the market to show the share of the market your projections would represent for each year of the plan to check they are realistic and indicate future potential.

3. MARKETING PLAN

The Marketing Plan will detail your planned routes to market, for example direct to customers, via agents on commission or distributors. You will need to show the impact of distributor discounts and/or agents' commissions on your projections.

Explain whether marketing is conducted directly by the business or locally by distributors or a combination.

If you've ever watched Dragon's Den, you will have heard them decline some opportunities because when they asked what the business owner planned to spend on marketing their experienced opinion was that it would be nowhere near enough.

Sales projections have to be credible, which means you need to explain exactly how many customers you need to acquire to meet your sales projections and include a fully funded plan to attain them.

Good market research and/or experience are needed to assess the buying behaviour of customers. This enables a business to produce a detailed, credible and funded plan to achieve the customer numbers required to achieve the sales projections.

The absence of a credible marketing plan explains why many businesses fail to achieve even modest success

When projections are correctly estimated, many business owners are shocked by the resulting budget required, which is why the Dragons from the Den are often very dismissive when it hasn't been done.

TYPICAL MISTAKE

The plan has only limited details of the routes to market and the costs of each.

Sales projections are not linked to the buying behaviour of customers and hence the marketing plan has no targets for the growing number of new customers required each year and month to achieve the sales projections.

REMEDY

Include full details and costs of the various routes to market and how these may change as the business grows.

Profile the buying behaviour of different types of customers and where appropriate the likely reordering frequency.

Estimate the likely retention of customers and hence how many extra new customers would be required to replace these. Now you can work out the number of new customers required each month to achieve your growth targets.

Measure the conversion rate prospect-to-customer currently being experienced or expected to be achieved and estimate the number of prospects needed each month.

Then estimate the conversion rate suspect-to-prospect for the different promotional options so that you can estimate the total promotional activity and budget required to meet your sales projections.

4. CASHFLOW

Profitable businesses can still go bust if they run out of cash, so any business plan must show projections for cashflow.

The extent to which a cashflow projection is different from a projection of profit and loss depends on the company. P & L and cashflow projections could be quite similar for a service business if it doesn't offer credit terms and operates below the threshold for VAT.

Profitable businesses still go bust if they run out of cash

Projections for P & L and cashflow could be very different for a business trading stock with credit terms and is above the VAT threshold. The payment to suppliers for stock usually occurs much earlier than revenues are received from customers.

A business trading stock may be tempted to buy stock in larger batches to take advantage of better prices from suppliers and improve profitability. The danger is that the business may not have sufficient funding to cover the working capital required.

OVER-TRADING

A business may be selling well and keeps taking orders and buying more stock and then become a victim of *'over-trading'*. This occurs when it no longer has the cash reserves to pay bills when they fall due, despite good and profitable trading.

The Profit & Loss projection won't show the danger of 'over-trading' whereas the cashflow projection will

CAPITAL EXPENDITURE

Purchasing large capital items, such as machinery or vehicles is another area where the profit and loss and cashflow projections may be very different. Capital expenditure usually impacts cashflow at a single point, whereas it is shown as depreciation in the profit and loss over time.

Buying a capital item may appear more attractive than leasing in terms of profit, but it will add to the pressure on cashflow and may restrict growth.

A business without sufficient cash reserves may have to limit spending on promotional activities, which means it has to grow more slowly. So, cashflow is fundamental to making appropriate business decisions.

If funding is obtained through a loan, the cashflow projections must also include loan repayments and interest, which means you have to calculate how much larger the loan needs to be in order to cover repayments and interest each month.

The cashflow projection will confirm how much funding a business needs, why it is needed and whether it can afford to pay it back.

Add a sensible contingency to cover areas of sensitivity, see the next section.

TYPICAL MISTAKE

The request for funding is not linked to robust cashflow projections, so the amount of funding requested, why it is required and whether the business can repay it, cannot be verified.

REMEDY

Include a robust cashflow statement with realistic projections for the inflow and outflow of cash and show why the funding is required to keep the business cash positive.

5. SENSITIVITY ANALYSIS

A business plan is looking into the future and because we can never accurately predict the future, there is only one thing we know with reasonable certainty about the business plan and that is that the projections will be wrong. The question is: *By how much?*

Check how wrong your estimates can be before there will be serious implications to the viability of your business

Lenders and investors will be looking at the assumptions made and to what extent they are sensitive to various factors. For example, if a business buys in Euros and sells in Sterling, how far can the exchange rate move before the profitability declines to critical levels?

A lender will check to what extent a parameter can move and the business will still be able to repay the loan. They will then consider how likely this could be within the timeframe of the loan.

There will also be a *'threat'* assessment, for example overseas competition with cheap labour, the emergence of a new technology or a new well-funded competitor.

This sensitivity analysis will form part of any lending or investing risk assessment.

TYPICAL MISTAKE

A typical mistake is not to include anything that may be seen as negative in case it prejudices the decision to lend or invest.

Yet failing to identify and recognise threats and the sensitivity of the projections to critical parameters may be deemed naive, which will reduce credibility.

REMEDY

Include a sensitivity analysis and show how you might mitigate for any impact, for example, if you have a critical component, which you prefer to source from a particular supplier, identify alternatives, perhaps priced in a different currency. These may currently have higher costs resulting in lower margins and not preferred, but at least you can define the likely extra cost and the extent of the risk if there is an interruption to your primary source.

Include an analysis of your Strengths, Weaknesses, Opportunities and Threats (S.W.O.T). Don't be concerned about identifying weaknesses and threats. Show how you will overcome weaknesses, perhaps when you have the finance and show how you can mitigate for potential threats.

Showing that you are fully aware of your weaknesses and potential threats and that you have contingency plans will increase your credibility and reduce the perceived risk of lending or investing.

6. AUDIENCE

Communication is most effective when you know your audience and if your business plan is aiming to get funding, it must appeal to the motivations and concerns of the decision maker(s).

Funding is about:

Risk and Reward

This means that a business plan written for a lender won't be the same as one written for an investor or a partner.

For lenders: The reward is fixed by the interest rate, so it's all about the risk. A lender will prefer to see cash projections with worse-case sensitivity levels proving the loan can still be serviced until fully repaid.

For investors: The reward depends on how rapidly you can grow and they can exit with a return on their investment that compares favourably with other opportunities at a lower risk.

An investor will prefer to see scalable projections with defined exit options enabling a projected return on investment to be compared with other opportunities.

For partners: The reward may be financial or strategic and the opportunity to work with you will be compared with alternative proposals.

TYPICAL MISTAKE

Writing a business plan from a template without due regard for the needs of the specific audience.

REMEDY

Understand the motivations of your audience and write the business plan specifically for them. The projections are likely to be different.

A lender would prefer to see conservative projections, so the business isn't at risk of failing before the loan has been repaid.

An investor would like to see projections that ‘stretch’ the opportunity to see the full extent of the potential reward.

If you need to approach both lenders and investors or different types of investors, you may need to compile several plans for the different audiences.

7. STRUCTURE

A common criticism made by recipients of business plans is that it takes too long to discover the key points, which are either omitted or buried within too much background information.

Areader will first flick through it quickly to get a feel for how easily they'll be able to grasp the essential facts

If the reader perceives that it would be too much effort to check whether a business plan is of interest, they won't even bother to begin

A good structure with a clear contents page will help them quickly judge how much they will need to read before deciding whether to read more of the detail.

For this reason, the presence of an Executive Summary of only 2 pages at the beginning will show the reader at a glance that they only need to scan 2 pages to decide whether the opportunity could be of interest.

A well-crafted Executive Summary will inform the right audience of the merits of the rest of the plan and allow anyone else to disregard it without feeling they have wasted much time.

The Executive Summary is the last section you write, yet the first section your audience reads

Much of the text of your plan and particularly the Executive Summary cannot be written until you have your market and financial projections, because the text will relate to the numbers.

Any background information can be provided either as appendices or as supporting documents.

TYPICAL MISTAKE

Assuming your reader is willing to wade through an unstructured plan to tease out the information they require – *they won't*.

REMEDY

Write a structured plan enabling readers to quickly find relevant information and make a decision as to whether to progress further with the opportunity.

Include an Executive Summary at the beginning clearly presenting the critical information required by your target audience to decide whether to read further.

SUCCESS

Your business plan has a job of work to do: – To plan your route to success and/or to raise finance.

You will probably put a lot of effort into creating your business plan, so it is worth making sure it is fit for purpose

Lenders and investors regularly complain about the standard of business plans they receive and many plans will receive no more than a cursory glance.

This e-book has discussed the more significant issues and suggested how you should make changes to create the best chance of success.

There are other mistakes that are also quoted by lenders and investors, such as inconsistencies, poor attention to detail, the inclusion of less relevant information yet missing essential details and of course these mistakes should also be eliminated.

How can Sightpath help?

We will create a model of your business in our Business Development System and help you balance your ambition with your ability to fund it. We then generate a Business Plan, which you can implement and use to raise finance if required.

This can be done remotely, so you don't have to meet with us in person.

We have a good track record with banks and work with a network of investors to help you get funding. There are other options we can explore, which may be appropriate depending on your circumstances.

Please visit **www.sightpath.co.uk** or call **0845 468 2020** for more information or to engage one of our Business Catalysts to drive our Business Development system to model your business and generate your plan for success.

You can read more in the book by Sightpath founder Robert Copping: **The Heart of Business Success – How to overcome the Catch-22's of growing your business.** You can obtain a copy from most online retailers or by order from any book retailer ISBN 978-1-905823-52-9.

Finally, let me take this opportunity to wish you every success.

Robert Copping