

## What Makes a Good Business Plan?

Whether in start-up, expansion or turnaround-situations – every business needs to write a business plan sooner or later. The business plan as a tool got a lot of publicity during the boom times of the New Economy. It is one of the most important documents for start-ups looking for venture capital. Unfortunately, the New Economy-hype brought up some wrong or at least simplistic assumptions about business plans. The term ‘elevator pitch’ for instance, indicates that it might be possible to explain a business plan within a few minutes.

Therefore, I will start with the result:

- A business plan is more than the description of a company’s business model, products and services
- A business plan serves more purposes than only acquiring capital.

The author’s practical experience has given evidence, that not all business plans take into consideration these statements – as obvious as they might seem to us.

Thus, this article will discuss functions and content of a good business plan.

## Functions and Target Groups of Business Plans

The business plan is, without doubt, one of the most important documents that has to be submitted to **potential suppliers of capital**, like banks, venture capitalists, business angels, cooperation partners with the intent to acquire a capital stake or public authorities that decide about state subsidies. For all these target groups the business plan has an information function. Investors need to find all the information that is relevant for their investment decision in the business plan. This comprises information on the past and current state of the business as well on about expected future developments, furthermore on business models, strategic partnerships, and the management team and on all other factors that might be of importance for the businesses future development. The most important question for any investor or supplier of capital, however, in the question for the expected return of his funds to be invested. The priorities of different types of investors may differ in relation to their particular objectives; nevertheless, all of them need to know about their chances for a successful exit:

Sources of Capital	Their Expectations
Investors like Venture Capital Funds, Business Angels etc.	Return of the funds invested with an adequate interest yield (here for instance IPO profits, dividends) within a reasonable period. The focus is normally on return on capital.
Banks	Payment of interests and repayment rates according to the agreements in the contract. This is their primary interest; nevertheless, banks are often interested in establishing a lasting business relationship as a basis for further business and cross-selling opportunities.
Strategic Partners, Cooperation Partners	Often they are interested in a long-term investment without loss of value, partly with regular payments of interests, dividends, license fees etc. Besides their expectations for return on capital, they normally wish to establish stable relationships for mutual benefits (e.g. synergies, access to raw materials or sales channels, access to know how)
Public Authorities (state subsidies)	Depending on the type of subsidy, they may expect returns and repayments as well. The primary objective normally is to stabilize and support the business.

Depending on their priorities and objectives, all types of investors expect information on the businesses future development, especially expected profits and liquidity for reasonable planning period in the business plan.

The business plan is not only a major source of information for investors and other suppliers of capital. Moreover, it is an important tool for **owners and managers** of the business. These persons should have a good look at past developments of the business, its objectives, stakeholders' expectations and the external environment when developing the business plan. In the result, management gets an idea of the business's strengths and weaknesses and on chances and risks in the external environment. Since the business plan is of long-term strategic nature, it can support operative decisions and reactions on changes in the external environment. Examples are:

- Evaluation of new market opportunities in relation to the organization's long-term objectives (Does this market segment fit into our overall strategy? Will this partnership provide additional opportunities for realizing our overall objectives? etc)
- Investment decisions (What effects will a particular investment and a particular way of financing it have on the balance sheet, the profit and loss account and the gearing ratio? Shall we lease or buy a new piece of equipment? etc)

Thus, the business plan can serve as the guiding line in an organizations day-to-day business. Dynamic markets require fast decisions without complete analysis. The long-term objectives formulated in the business plan can help to take decisions that fit the businesses overall strategic direction.

**Other target groups** of business plans may be potential partners in cooperations, partners

in mergers and acquisitions and several interest groups. They too are interested in comprehensive information.

### **Content of the Business Plan**

The functions of the business plan discussed in the previous section determine its content. In general, a business plan should provide information on the following topics:

- Business idea, corporate objectives and vision
- Legal questions (legal form, important contracts)
- Description of products and services
- Previous and present developments and financial situation (for start-ups: previous activities like search for partners, R&D activities)
- Management team
- Market analysis and marketing
- Planned future development (milestones, phases of growth, scenarios)
- Financial projections

If the business wants to acquire external funding, the information on expected returns for investors is of special importance. It has to be realistic and well founded on facts.

Business plans we develop for our clients in our consulting practice normally have the following structure. I need to stress here, that there is no one right standard-structure for a business plan. Depending on the particular situation of the business (purpose of the plan, target groups, existing documents, industry etc) the focus may shift or sections may be added or neglected.

## Example: Structure of a Business Plan

### Executive Summary

#### 1. The Organization

- 1.1. Visions, Objectives
- 1.2. Description of products and services
  - 1.2.1 Technological information, novelty, innovation
  - 1.2.2. Competitive advantages, value added for customers, unique selling proposition
- 1.3. Legal and organizational basis
- 1.4. For start-ups: founder team
- 1.5. Strategic partners, cooperations
- 1.6. If applicable: previous and present development and financial situation

#### 2. Market Analysis

- 2.1. Target markets (market volume, segmentation etc)
- 2.2. Competitors
- 2.3. Trends, drivers, future developments

#### 3. Phases of Corporate Development

- 3.1. Phases of growth
- 3.2. Potential risks, scenarios, alternatives

#### 4. Sales and Marketing

- 4.1. Objectives
- 4.2. Distribution channels
- 4.3. Marketing plan and budget

#### 5. Staff

- 5.1. Staff requirements, qualification requirements
- 5.2. Management team

#### 6. Planned Investments

- 6.1. Description and reasons for planned investments, expected effects
- 6.2. Planned financing of investments

#### 7. Financial Projections

- 7.1. Profit and Loss Account (Years 1-5)
- 7.2. Balance Sheets (Years 1-5)
- 7.3. Cash Flow Budgets (years 1-5), monthly cash flow plans for months 1-12, Working capital needs
- 7.4. Break Even Point
- 7.5. Exit options for investors, if applicable plans for interests and repayments

#### 8. Summary – Strengths, Weaknesses, Opportunities, Threats

© Recklies Management Project GmbH

## **Mistakes you Can Avoid**

Practice has shown that many business plans – even those written with great commitment – have weaknesses. Those weaknesses can lead to unnecessary problems when searching for investors. In our experience, the following points deserve special attention:

- **A Business Plan is No Advertising Material**

Of course, the business plan shall demonstrate the entrepreneurs' commitment and conviction. However, instead of selling the businesses products and services, it has to establish trust into the business as a whole. Especially start-up entrepreneurs are inclined to describe in great detail what they are most familiar with: the product or the technology. This kind of information is important; nevertheless, it should be presented in an objective matter-of-fact way. The business plan should avoid typical advertising terminology ("unforgettable experience", "the unique quality of our product"). An appendix with advertising flyers or with a draft of an advertising campaign will be fine, but the main body of the business plan should focus on facts.

Another point to remember is that the level of detail for the description of products and services needs to correspond with the scope and details in other sections of the business plan.

- **Market and Marketing**

Many start-up entrepreneurs have difficulties to figure out the ideal scope of their marketing activities. It is a mistake to limit the marketing budget in order to save money. But to plan for too ambitious marketing campaigns that do not fit the size of the business is a mistake too. The business plan does not necessarily need to contain a detailed marketing plan. It should, however, give an idea on the marketing activities the business plans. These activities have to be in balance with the business's size, the product, target groups

and the businesses financial muscle.

Another important point is a detailed market analysis. For instance, it should be the start-up team - not the evaluating investor - that has a look at all potential competitors. At this stage, the business plan needs to deliver a comprehensive analysis of all factors that could influence the sales of the products. This includes what customers might consider substitutes and complementary products.

(**Excursus:** A well-known example for the ignoring of substitutes was the World Exhibition Expo 2000 in Hanover. Planners considered the Expo to be a unique and outstanding event that people wanted to see despite of long travel distances and high prices. In reality, people compared the Expo with things like other cultural events, visits at traditional theme parks, even a last minute trip to Majorca or a shopping weekend at London. The Expo-planners had not expected this type of competition; hence, they planned for far too high numbers of visitors.<sup>1</sup>)

- **Financial Projections**

It is not enough to provide an appendix with a rough estimate of sales, profits and the most important costs for the first year, completed with expected growth rates for the years to follow. All financial projections (profit and loss statements, balance sheets, cash flow projections) have to fit together and should be presented as detailed as it gets. Moreover, it is important to provide explanations and reasons for all major developments. The more comprehensible the financial projections are, the more credible they are.

- **Contradictions and Lack of Plausibility**

Unfortunately, this is another weakness of many business plans. All information has to be conclusive in the context of the total

---

<sup>1</sup> For details see our article [A small number of visitors at EXPO 2000 in Hanover OR What do Expo and Euro-Disney have in common?](#).

business plan, and it has to fit to the state of the industry. If a company projects strong growth in a declining market or, for instance, does not see any need to hire (and pay → costs) an experienced financial manager despite obvious deficits in the managerial qualification of the start-up team, it should at least be able to give good reasons for this. There are many other examples like these. They cover the whole range from simple mistakes in calculations up to serious misjudgments of markets. Such mistakes are evidence for poor accuracy, lacking realism and skills of the management team in the eyes of an external reader.