Business plan preparation

Manual for Entrepreneurs
AGENDA

• Short introduction to the use of business plans

• Preparation guidelines for business plans
TYPES OF NEW BUSINESSES

Product/service

New

New product
- Palm
- Smart
- Sony Playstation
- Rollerblades

New industry
- Direct satellite TV
- Netscape
- Mobile telephony

Existing industries and businesses

Existing

New business system
- Dell
- Fotolabo
- Charles Schwab
- FedEx

Source: Planen, gründen, wachsen (McKinsey & Company)
USE OF BUSINESS PLANS

**Standard use**

- Start-up companies:
  - Application for venture capital
  - Search for management team members
  - Communication with partners, suppliers, …
- Established, developed businesses for investment decisions
  - In-house budget allocations
  - External financing

**Complications for New Venture projects**

- High insecurity concerning technology, timing, and cash need
- Difficult data situation due to newness of innovative products
- Necessity of external know-how transfer
- Lack of skills/motivation/time

Start-up business plans to be tailored to new venture needs

Source: McKinsey & Company
Business planning is an iterative and adaptive process that requires constant update and adjustment work.

Not the quantity of analyses, but the clarity and preciseness of the pack are important.

No hype, but factual statements. Enthusiasm will be generated by the investor realizing the opportunity on his own.

Those who allocate investment resources rarely are technical experts for the technology used in the proposal.

The storyline and all the facts presented must fit together and generate a well-rounded impression.

A clear, precise structure is a courtesy to those investing their time in reading the proposal.
DEVELOPMENT STEPS FOR BUSINESS PLANS

Level of maturity of business idea

Step 1: Idea description
- Product/service
- Market and competition

Step 2: Rough business plan
- Marketing and sales
- Business system
- Opportunities and risks

Step 3: VC-tailored business plan
- Management team
- Implementation plan
- Financing

Completion of financing
- External evaluation (due diligence)
- Deal structuring

Milestones

New decision on further proceeding when next milestone is reached

Time

Source: McKinsey & Company
REQUIRED BUSINESS PLAN ELEMENTS IN EACH PHASE FOR THIS COMPETITION

- Executive summary
- Product/service
- Management team
- Market and competition
- Marketing and sales
- Business system/organization
- Implementation schedule
- Opportunities and risks
- Appendix

Phase I

Phase II

Source: McKinsey & Company
AGENDA

• Short introduction to the use of business plans

• Preparation guidelines for business plans
CHAPTERS OF COMPLETE BUSINESS PLAN

- Executive summary
- Product/service
- Management team
- Market and competition
- Marketing and sales
- Business system
- Implementation plan
- Financing
- Opportunities and risks

Source: McKinsey & Company
CONTENT OF EXECUTIVE SUMMARY

• Gives a brief overview of the concept's most important aspects
• Describes idea as clearly, compellingly, and concisely as possible
• Raises interest of decision makers
• Is not more than 5 - 10 minutes to read

Quality of summary decides if rest of business plan is read

Source: McKinsey & Company
Idea description

- What is your business idea? In what way does it fulfill the criterion of uniqueness?
- Who are your target customers?
- What is the value for those customers?
- What market volume and growth rates do you forecast?
- What competitive environment do you face?
- What additional stages of development are needed?
- How much investment is necessary (estimated)?
- What long-term goals have you set?

Source: McKinsey & Company
EXECUTIVE SUMMARY – ADDITIONAL QUESTIONS

Rough business plan
• How high do you estimate your **financing needs**?
• What are the **sales, cost, and profit** situations?
• What are the most important **milestones** along the way to your goal?
• What **test customers** have you approached/ could you approach?
• What **distribution channels** will you use?
• What **partnerships** would you like to enter into?
• What **opportunities and risks** do you face?
• What is the picture on **patents**?

Most important questions an investor asks!
RUSMAR – EXECUTIVE SUMMARY

Product/service
• Potential foam plus applicator to replace expensive and space consuming earth that must be spread over garbage dumps every day
• Space savings of ~30% for dump operators
• Costs of coverage reduced by ~50% for dump operators

Market and competition
• Customers: household garbage dump operator
• Market: 300 to 500 dumps in Eastern USA with capacity of 500 to 10,000 tons/day
• Major competitor: 3M/Sanifoam (application takes longer and is more complicated)

Marketing and sales
• 1997: Investments of USD 850,000 required
• 1998: Sales of USD 2 million (break-even)
• 2002: Sales of USD 15 million, profit of USD 1.5 million

Business system
• Sale of foam and applicators (product business)

Opportunities and risks
• Necessary approval from authorities
• Proof of system's operational efficiency

Source: Inc. Magazine
Additional questions for complete business plan

- Summarize the results of your detailed business planning and state your exact financing needs!
- How will you delegate management tasks?
- How much production capacity is necessary?
- How will the implementation of your business idea be organized?
- List your next, concrete steps!
CONTENT OF PRODUCT/SERVICE SECTION

- Describes the function the product/service fulfills and the benefits the customer will gain from it
  - Product/service description
  - Customer value
- Explains status and next steps of product/service development
- Addresses patents/IP protection issues

Product/service section has to prove that entrepreneur can integrate the customers' perspective
Idea description

• What end customers will you address?
• What are the customers’ needs?
• What customer value does your product/service provide?
• What is the nature of your innovation? Why is it unique?
• What partnerships are necessary to achieve full customer value?
• What competitor products already exist or are under development?
• What stage of development has your product or service reached?
• Do you have patents or licenses?
• What further development steps do you plan to take? What milestones must be reached?
Rough business plan

- Which **versions** of your products/services are designed for which customer groups and applications?
- What **patents/licenses** do the competitors have?
- What kind of **service/maintenance** will you offer?
- What product or service **guarantees** will you grant?
- Compare the **strengths and weaknesses** of comparable products/services with yours in an overview!
DESCRIPTION OF THE PRODUCT/SERVICE

Technical description of lasers:

A device that converts incident electromagnetic radiation of mixed frequencies to one or more discrete frequencies of highly amplified and coherent ultraviolet, visible, or infrared radiation

Better:

High-performance device for the creation of a narrowly bundled beam of light

Source: The American Heritage Dictionary, Duden
SUCCESSFUL PRODUCT POSITIONING

- Identify relevant customer needs and problems
- Define clear, sufficiently large customer segments
- Define uniqueness and position offering vis-à-vis competition
- Address subjective perception of customers
Additional questions for complete business plan

• What resources (time, personnel, materials) do you require for each subsequent development?

• What share of sales do you expect from your various products/services (if applicable)? Why?

• What income from royalties/sales do you estimate from possibly marketing the property rights? Who would be your licensees/buyers?
CONTENT OF MANAGEMENT TEAM SECTION

- Outlines educational background and professional experience of founders
- Describes how existing skill gaps can be closed in the future
- Convinces potential investors that both managerial and technological expertise is present to run the venture

Venture capitalist will invest only if the venture is managed by an excellent team

Source: McKinsey & Company
Complete business plan

• Who are the members of your management team and what distinguishes them: education, professional experience, success, standing in the business world?

• What experience or abilities does the team possess that will be useful for implementing your concept and setting up your company?

• What experience or abilities are lacking? How will the gaps be closed? By whom?

• What targets do the team members pursue by starting up the business? How high is the motivation of the individual team members?
REASONS FOR BUSINESS PLAN REJECTION – BIOTECHNOLOGY VENTURES*

<table>
<thead>
<tr>
<th>Reason</th>
<th>Percent</th>
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<td>Not market-driven</td>
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<td>Long time frame</td>
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<tr>
<td>Money commitment too large</td>
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<tr>
<td>Not patentable</td>
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<tr>
<td>Inadequate technical expertise</td>
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<td>Other</td>
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</table>

"If you find good people, they can always change the product. Nearly every mistake I have made has been picking the wrong people, not the wrong idea" – Arthur Rock

Arthur Rock & Co.

* Reasons for rejecting business plans by firms experienced in biotechnology venture capital

** Multiple responses given

Source: Coopers and Lybrand, McKinsey & Company
TEAM RAMP-UP – EXAMPLES

- **Idea and team development**
- **Venture begins**
- **Technology & mkt. validation**
- **Proof of economic viability**
- **Explosive revenue growth**
- **Sustained earnings growth**

<table>
<thead>
<tr>
<th>Role</th>
<th>Venture begins</th>
<th>Technology &amp; mkt. validation</th>
<th>Proof of economic viability</th>
<th>Explosive revenue growth</th>
<th>Sustained earnings growth</th>
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<tr>
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<td>✓</td>
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<tr>
<td>Technology</td>
<td>✓ X</td>
<td>▲</td>
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<td>Marketing</td>
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<td>Sales</td>
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<td>✓</td>
<td>▲</td>
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<tr>
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<td>▲</td>
<td>✓</td>
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Source: McKinsey & Company analysis, external interviews
PERCENTAGE OF FOUNDERS OF FAST GROWING COMPANIES*

- Unemployed or recent graduate: 6
- Start-ups: 4
- Midsize to large companies (including Fortune 1000): 42
- Not from business: 13
- Running other businesses: 14
- Small established companies: 21

Examples include:
- Intel
- Microsoft
- Lotus
- Sun Microsystems
- Mattel
- CompuServe
- Advanced Micro Devices
- Raytheon
- Fairchild Semiconductor
- TRW
- CondeNast
- News Corp

* 4-year growth rate of 573% or higher, 1984 - 1990, 456 companies

Source: McKinsey & Company
NECESSARY EXPERIENCE FOR VENTURE MANAGEMENT

**Traditional corporate experience does not fit new venture needs** …

- Skills aligned to achieving near term earnings and sustained revenue growth
- Processes based on internal milestones
- Staff support allows extensive delegation (e.g., HR, finance, marketing)
- Decision making enabled by significant capital resources

**… but corporate experience is valuable when it includes**

- Business building roles, e.g.,
  - Led expansion into new geographic markets
  - Built new product line or division
  - Provided marketing leadership to develop a new brand
- Relevant industry sector experience

**Catherine Hapka, CEO**
**Rhythms NetConnections**
- Former EVP of US West
- Responsible for business and telecommunications units with USD 7.5 billion in revenues
- Started and built US West’s INTERPRISE Networking Services Unit to USD 400 million in revenue
- Established partnerships with 15 leading hardware and software providers

**Richard Thompson, CEO**
**Aradigm**
- Former President of Johnson & Johnson subsidiary, Lifescan
- Built Lifescan from the ground up
- Led within Johnson & Johnson expansion into Europe and Japan

Source: Executive search firm and VC interviews
SKILL SET OF TEAM MEMBERS

Team members

<table>
<thead>
<tr>
<th>Hard factors</th>
<th>J. Chapuis</th>
<th>S. Fischer</th>
<th>M. Tscharner</th>
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<tr>
<td>Finance</td>
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<tr>
<td>Project management</td>
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<tr>
<td>Contacts</td>
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<tr>
<td>Marketing/sales</td>
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<tr>
<td>Production</td>
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<tr>
<td>Human resources</td>
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</table>

<table>
<thead>
<tr>
<th>Soft factors</th>
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<tbody>
<tr>
<td>Social competence</td>
<td>•</td>
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<tr>
<td>Initiative</td>
<td>•</td>
</tr>
<tr>
<td>Communication</td>
<td>•</td>
</tr>
<tr>
<td>Sales/negotiation skills</td>
<td>O</td>
</tr>
</tbody>
</table>

High skill level
Medium skill level
Skill gaps

Obvious skill gaps to be filled with additional team members

Source: Planen, gründen, wachsen (McKinsey & Company)
CONTENT OF MARKET AND COMPETITION SECTION

• Provides thorough understanding of markets and competitors:
  – Market size and growth
  – Market segmentation
  – Competition
  – Positioning of product vis-à-vis the competition

The market and competition section has to outline the full economic potential of the venture

Source: McKinsey & Company
Idea description

• How is the industry developing?
• What role do innovation and technological advances play?
• How will you segment the market?
• What market volumes do the individual market segments have, now and in the future (rough estimates)?
• Who are your target customer groups?
• What major competitors offer similar products/services?
• How sustainable will your competitive edge be?
Rough business plan

- What market volume (value and amount) do you estimate for your individual market segments over the next five years?
- What will influence growth in the market segments?
- What is your estimate of current and future profitability of the individual market segments?
- What market shares do you hold in each market segment? What segments are you targeting?
- Who are your reference customers? How do you plan to get reference customers?
- What are the key buying factors for customers?
Most vertical specialty marketplaces expected to consolidate.

Attractive

Unattractive

Potential market size
USD millions

~ 100 - 200

1999

~ 1.000 - 2.000

2009

Source: McKinsey & Company

EXAMPLE

ROUGH ESTIMATES
• **Target customers: Operators**
  – Operators of one or more "larger" dumps for household garbage
  – Eastern USA (approx. 300 to 500), beginning 2002, whole USA
  – Throughput of 500 to 10,000 tons per day
  – Fee of USD 65 per ton

• "Target customers": Agencies
  – Environmental Protection Agency (federal regulatory body)
  – Department of Natural Resources (state regulatory body)
  – Local licensors
  ⇒ Consent required of three additional agencies
Additional questions for complete business plan

• How does the competition operate? What strategies are pursued?
• What are the barriers to market entry and how can they be overcome?
• What market share does your competition have in the various market segments?
• How profitable are your competitors?
• What are your competitors’ marketing strategies?
• What distribution channels do your competitors use?
• How will competitors react to your market launch? How will you respond to this reaction?
• Profile the strengths and weaknesses of your major competitors with your own in the form of an overview!
COMPETITIVE ADVANTAGE

- Revolutionary improvement in performance
- Steep drop in price
- Creation of unusually emotional bond with customer

Number of hypergrowth companies with unique competitive advantage:
- 27
- 19
- 3

Source: McKinsey & Company
## RUSMAR, INC. – ANALYSIS OF THE COMPETITION

<table>
<thead>
<tr>
<th>Customer requirements</th>
<th>Degree of fulfillment</th>
<th>Reason</th>
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<tr>
<td></td>
<td>Rusmar</td>
<td>3M/Sanifoam</td>
</tr>
<tr>
<td>• Covering layers with low volume</td>
<td>✔️</td>
<td>✔️</td>
</tr>
<tr>
<td>• Short application times (longer dumping time)</td>
<td>✔️</td>
<td>❌</td>
</tr>
<tr>
<td>• Simple application</td>
<td>✔️</td>
<td>❌</td>
</tr>
<tr>
<td>• Cost advantage per application</td>
<td>✔️</td>
<td>❌</td>
</tr>
<tr>
<td>• Equal performance as layer of earth regarding</td>
<td></td>
<td></td>
</tr>
<tr>
<td>– Odor absorption</td>
<td>✔️</td>
<td>❌</td>
</tr>
<tr>
<td>– Erosion from weather</td>
<td></td>
<td></td>
</tr>
<tr>
<td>– Protection from pests</td>
<td>❌</td>
<td>❌</td>
</tr>
<tr>
<td>• Constant availability of foam</td>
<td>❌</td>
<td>✔️</td>
</tr>
<tr>
<td>• Applicator licence available quickly, at low cost, and without concern (without reassessment of the dump by regulators)</td>
<td>❌</td>
<td>✔️</td>
</tr>
<tr>
<td>• Rapid and high-quality maintenance</td>
<td>❌</td>
<td>✔️</td>
</tr>
</tbody>
</table>

Source: Inc. Magazine
 CONTENT OF MARKETING AND SALES SECTION

• Outlines planned marketing and sales activities (four "Ps" framework):
  – Product
  – Price
  – Place
  – Promotion

Marketing and sales section has to explain how market is developed

Source: McKinsey & Company
Idea description

• What **final sales price** do you want to charge (estimated)?
  What criteria did you use to arrive at this final sale price?
  How high is the **profit margin** (estimated)?

• What **sales volumes** and **sales revenues** are you aiming for (estimated)?

Marketing and sales only briefly touched in executive summary (Phase I); more details are needed in detailed business plan (Phase II)
QUANTIFYING THE CUSTOMER VALUE

Dimensions of customer value

Evaluate and quantify customer value for all 3 dimensions
• Display value clearly
• Quantify wherever possible

Source: "Profitable pricing: guidelines for management", T.Nagle, R. Holden
MARKETING AND SALES – ADDITIONAL QUESTIONS

Complete business plan

• In which partial market segments will you make your market entry? How do you plan to turn this "toehold" into a high-volume business?

• What sales volumes are you targeting (detailed data by market segment)?

• Describe the typical process of selling your product/service. Who, among your buyers, ultimately makes the purchasing decision?

• How will you win reference customers?

• How much, in time and resources, will it cost to acquire a customer?

• Which advertising materials will you use to do so?

• What other planning steps are necessary in the run up to launching your product/service? Draw up a schedule with the most important milestones!
# DETERMINING TARGET SEGMENTS

<table>
<thead>
<tr>
<th>Select segmentation criteria</th>
<th>Determine segment volume</th>
<th>Analyse customer value per segment</th>
<th>Identify competition per segment</th>
<th>Determine target segment and evolution strategy</th>
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<tbody>
<tr>
<td>Segment 1</td>
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<tr>
<td>Segment 2</td>
<td>+</td>
<td>++</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Segment 3</td>
<td>0</td>
<td>++</td>
<td>0</td>
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</tr>
</tbody>
</table>

- Select clearly separate and segments with a strong proposition
- Arrive at market segments plausibly and validate it
- Understand customer value per segment
- Consider direct competitors and substitutions
- Make focus clear for market launch
- Anticipate evolution path

Source: McKinsey & Company
POSSIBLE CUSTOMER SEGMENTATION CRITERIA (EXAMPLES)

Consumer goods markets

- Location: country, urban/rural (population density)
- Demographics: age, sex, income, profession, company size
- Lifestyle: techies, counterculture, active seniors
- Behavior: frequency of product use, product application
- Buying habits: brand preferences, price consciousness

Industrial goods markets

- Demographics: company size, industry, location
- Operations: technology employed (e.g., digital, analog)
- Buying habits: centralized or decentralized purchasing, purchasing criteria, supplier agreements
- Situational factors: urgency of need, order size, etc.
Additional questions for complete business plan

• What demands (employee number, qualifications, and outfitting) must the operation meet in order to effectively implement its marketing strategy? What is your estimated expenditure for this area?

• How will sales volume and operating results be spread out among the various distribution channels (estimated)?

• What are your expenses? At launch – and later.

• What price will you charge for your product/service per target group and distribution channel?

• What payment policies will you lay down?
CONTENT OF BUSINESS SYSTEM SECTION

- Outlines what parts of the value chain are covered by the venture
- Discusses organizational issues
- Describes necessary partnerships
- Makes "make or buy" decisions

Business system section describes all necessary elements that enable the venture to physically deliver the customer value
BUSINESS SYSTEM – KEY QUESTIONS

Complete business plan

• What does the **business system** for your product/service look like?
• What **activities** do you want to handle yourself?
• Where will the **focus** of your own activities lie?
• What **business functions** make up your organization, and how is it structured?
• What **resources** do you need (quantitative and qualitative) to create your product/service?
• How high is your need for **technical input** (raw materials, materials to create your service)?
• What will you **make**, what will you **buy**?
• Which **partners** will you work with? What are the advantages of working together for you and your partners?

Source: McKinsey & Company
BUSINESS SYSTEM – VALUE CHAIN

Generic value chain

- Research & Development
- Production
- Marketing & Sales
- Distribution
- Service

Case example City Scape

- Development of Internet technology
- City Scape system design
- Acquisition: General information, Businesses
- Internet production
- Marketing: Consumers, Businesses
- Business sales
- Updates, services
- Licensing

EXEMPLARY

Covered by City Scape

Source: Planen, gründen, wachsen
## BUSINESS MODEL – REVENUES SOURCES

<table>
<thead>
<tr>
<th>Revenue sources</th>
<th>Description</th>
<th>Revenue potential</th>
</tr>
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<tbody>
<tr>
<td><strong>Product business</strong></td>
<td>• E.g., sale of software tools</td>
<td></td>
</tr>
<tr>
<td><strong>Services</strong></td>
<td>• Revenues resulting from service provision or consulting</td>
<td></td>
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<tr>
<td><strong>Contract development</strong></td>
<td>• Development of customer-specific solutions</td>
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<tr>
<td><strong>Others</strong></td>
<td>• Customer training</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Support/Maintenance</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• IP sale/license fees</td>
<td></td>
</tr>
</tbody>
</table>

Source: McKinsey & Company
**Additional questions for complete business plan**

- Where will you **locate** your business?
- What **capacity** for product manufacture and service production do you plan (number of units)?
- How much will **production and delivery** of your product/service **cost**?
- How, and at what cost, can you **adjust** your **capacity** in the short term?
- What measures are planned for **quality assurance**?
- If you need a warehouse, how will you organize your **inventory**?
- How much of your product has to be put in **storage**?
- How are your **costs structured** (fixed, variable)?
CONTENT OF IMPLEMENTATION PLAN SECTION

- Describes the most important activities and milestones for the development of the business
- Lists the planned short- and long-term investments
- Links the investment needs with major milestones

The implementation plan section gives the investor a clear roadmap to control the business development.

Source: McKinsey & Company
**Complete business plan**

- What are the most important **milestones** for the development of your business, and **when** must they be reached?
- How do you plan to **structure the work** to reach these targets?
- For which tasks/milestones do you anticipate **bottlenecks**?
- How many **new employees** will you need in the individual business areas over the next five years? What will this cost?
- How much real **capital** is necessary to achieve initial sales?
- List your planned **short-term investments**!
- List your planned **longer-term (3 - 5 years) investments**!
- What **investments** will be required when which **milestones** are reached?
- How high is the **annual depreciation** for each investment?
## IMPLEMENTATION PLAN

<table>
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<th>Main activities</th>
<th>01/00</th>
<th>02/00</th>
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<th>12/04</th>
<th>Key success factors</th>
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<td>• Activity 2</td>
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<td>• KSF 2</td>
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<td>• Activity 3</td>
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<td>• KSF 3</td>
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**Gantt timeline to show the interdependence of the activities and the eventual bottlenecks**

**Main milestones that pushes the business to the next level; focus on external milestones (e.g., market entrance, product launch etc.)**

**Time frame year 1 - 5 with decreasing level of detail**

**Detailed explanation of investment needs:**

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<th>Expenses</th>
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<td>• Activities 1 - 3</td>
<td>Personnel USD xx</td>
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<td>• Material</td>
<td>USD xx</td>
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**Milestones**

- Milestone 1
- ...
- ...

**Investment need**

- USD xxx
- USD xxx
- USD xxx

**Source:** McKinsey & Company
## CityScape Example – Implementation Plan

<table>
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**Source:** “Planen, Gründen, Wachsen”
CONTENT OF FINANCING SECTION

- Provides rough cash-flow forecasts
- Outlines forecasts of profit and loss statements
- Gives overview of future balance sheet structure

The finance plan explains the timing and volume of necessary financing rounds
Complete business plan

• How will your revenues, expenses and income develop?
• How will your cash flow develop? When will you expect to break even (= sum of all revenues greater than the sum of all expenses)?
• How high is your need for financing based on your liquidity planning?
  How much cash is needed in the worst case scenario?
• What assumptions underlie your financial planning?
• Which sources of capital are available to you to cover your financing needs?
• What deal are you offering potential investors?
• What return can investors expect?
• How will they realize a profit (exit options)?

Financial plan outlines
• Cash flow statement
• Income statement
• Balance sheet
### Application of Financial Planning Instruments

**Can I fulfill my financial obligations at any time?**

**Am I profitable?**

**Where has my capital been invested, and where has it come from?**

<table>
<thead>
<tr>
<th>Cash flow statement</th>
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<tbody>
<tr>
<td><strong>Deposits</strong></td>
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<td>...</td>
</tr>
<tr>
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<td><strong>Liquid funds</strong></td>
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<table>
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<tr>
<th>Income statement</th>
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<tbody>
<tr>
<td><strong>Proceeds</strong></td>
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<td><strong>Profit/loss</strong></td>
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<table>
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<th>Balance sheet</th>
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<td><strong>Assets</strong></td>
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<td>...</td>
</tr>
<tr>
<td>...</td>
</tr>
<tr>
<td>...</td>
</tr>
<tr>
<td><strong>Total assets</strong></td>
</tr>
<tr>
<td><strong>Capital invested</strong></td>
</tr>
</tbody>
</table>

- **Cause of bankruptcy:** illiquidity
  - (liquid funds < 0)

- **Cause of bankruptcy:** excessive debt
  - (equity < 0)

Source: McKinsey & Company
CASH FLOW AND INCOME STATEMENT

Cash flow statement

| Deposits | = |
| Payments | = |

Liquid funds

Proceeds generated and expenses (consumption of resources) are entered into the books for the period under review – irrespective of concrete payments

Income statement

| Income | = |
| Expenses | = |

Profit/loss

Deposits and payments refer to the amount of liquid cash and are not entered into the books until actual payment takes place

Constantly safeguarding liquidity takes top priority for start-up companies

Source: McKinsey & Company
## BALANCE SHEET STRUCTURE

DM thousands

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<thead>
<tr>
<th>Assets</th>
<th></th>
<th>Equity + liabilities</th>
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<td><strong>Fixed assets</strong></td>
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<td><strong>Equity</strong></td>
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<td>Intangible assets</td>
<td>20</td>
<td>Nominal capital</td>
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<td>Real estate and buildings</td>
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<td>Additional paid-in capital</td>
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<td>Technical equipment, plant, and machinery</td>
<td>1,936</td>
<td>Net earnings/losses brought forward</td>
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<td>Other equipment and fixed assets</td>
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<td>Net income</td>
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<td><strong>Current assets</strong></td>
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<td><strong>Liabilities</strong></td>
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<td>Raw materials and supplies</td>
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<td>Provisions</td>
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<td>Semi-finished and finished goods</td>
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<td><strong>Total assets</strong></td>
<td>8,321</td>
<td><strong>Total equity + liabilities</strong></td>
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Source: McKinsey & Company
### STRUCTURE OF INCOME STATEMENTS IN DIFFERENT INDUSTRIES

**Percent**

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<th>Revenues</th>
<th>Food</th>
<th>Research and development</th>
<th>Consulting</th>
<th>Leasing</th>
<th>Electronics</th>
<th>Automobiles &amp; machinery</th>
<th>Chemicals</th>
<th>Publishing/ printing</th>
<th>Textiles</th>
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<td>Sales</td>
<td>96.2</td>
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<td>92.1</td>
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<td>7.0</td>
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<td>3.5</td>
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<td>4.2</td>
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<th>98.5</th>
<th>96.9</th>
<th>92.6</th>
<th>100.8</th>
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<th>94.4</th>
<th>93.3</th>
<th>97.6</th>
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<td>41.3</td>
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<td>• Wages and salaries</td>
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<td>1.3</td>
<td>1.7</td>
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<td>3.6</td>
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<td>6.7</td>
<td>3.3</td>
<td>2.8</td>
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<td>0.9</td>
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<td>0.9</td>
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<td>50.1</td>
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<td>19.0</td>
<td>16.5</td>
<td>23.3</td>
<td>18.5</td>
<td>17.6</td>
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</tbody>
</table>

| Profit | 1.5  | 3.1  | 7.4  | -0.8 | 2.8  | 4.6  | 6.7  | 2.4  | -0.3 |

Source: Planen, gründen, wachsen (McKinsey & Company)
**VALUATION METHODS**

**Valuation with DCF method**

**EUR thousands**

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<td>Free cash flows</td>
<td>-1,960</td>
<td>-660</td>
<td>-150</td>
<td>380</td>
<td>880</td>
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<td>Discount rate</td>
<td>65%</td>
<td>55%</td>
<td>45%</td>
<td>35%</td>
<td>25%</td>
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<td>0.416</td>
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<td>0.301</td>
<td>0.328</td>
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<td>Today's value</td>
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<td>Debt</td>
<td>0</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total value</td>
<td>2,500</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Continuing value**

**11,000**

**Valuation with multiples**

**EUR thousands**

<table>
<thead>
<tr>
<th>Year</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit for relevant period (year 5)</td>
<td>905</td>
<td>x 43</td>
<td>(multiple)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Discount factor (IRR = 65% for 5 years)</td>
<td>0.082</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>EUR value</td>
<td>38,900</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total value</td>
<td>3,190</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* Assumption: FCF in year 5 is 1,100, growth rate 6%, discount rate 16%

Source: McKinsey & Company
## POSSIBLE SOURCES OF FUNDING

<table>
<thead>
<tr>
<th>Financing stages</th>
<th>Seed</th>
<th>Start-up</th>
<th>Expansion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personal savings</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loan by family</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Government subsidies</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank loans</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Leasing</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Venture capital</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stock market</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Planen, gründen, wachsen (McKinsey & Company)
TYPICAL VC FINANCING PROCESS

1. Business plan
2. Preselection
3. First visit and discussion
4. Letter of intent
5. Further discussions, evaluations
6. Term sheet
7. Due diligence
8. Contract negotiation
9. Contract, financing
10. Support, coaching, and control
11. Exit

Source: Planen, gründen, wachsen (McKinsey & Company)
CONTENT OF OPPORTUNITIES AND RISK SECTION

- Describes the venture's specific opportunities
- Identifies the venture's main challenges
- Tries to assess and quantify risks (e.g., with sensitivity analysis)
- Develops countermeasures for "killer" risks

Consideration of risk involved will win the confidence of a potential investor

Source: McKinsey & Company
OPPORTUNITIES AND RISKS – KEY QUESTIONS

Complete business plan
• What **basic risks** (market, competition, technology) does your business venture face?
• What **measures** will you take to counter these risks?
• What extraordinary **opportunities/business possibilities** do you see for your company?
• How could an expansion of your **capital base** help?

Source: McKinsey & Company
TYPICAL RISKS – EXAMPLES

Inside the venture

- Management team of the venture cannot be completed
- Important team member (e.g., CTO) leaves venture
- Slow prototype development delays early market entry

Outside the venture

- Strategic partner cannot be found
- No agreement with sales channel partner
- Lead customer does not accept prototype

Source: McKinsey & Company
SENSITIVITY ANALYSIS

Cumulated cash flows

DM

Year

1 2 3 4 5

Payback period

Financing need

Determinants of different scenarios have to be well understood

Best-case scenario

Base-case scenario

Worst-case scenario

Source: McKinsey & Company
Additional questions for complete business plan

• What will your planning look like for the next five financial years under both a best and worst case scenario?
• What effect will this have on your need for capital and your return?
• In your view, how realistic are these scenarios?
• What consequence do they have on your business planning?