Conducting a Feasibility Analysis and Crafting a Winning Business Plan

Feasibility Analysis

- Entrepreneurs do not lack creative ideas, but...
- Is a particular idea a viable foundation for creating a successful business?
- Feasibility study addresses the question: “Should we proceed with this business idea?”

Feasibility Study

- Not the same as a business plan
- Serves as a filter, screening out ideas that lack the potential for building a successful business before an entrepreneur commits the necessary resources to building a business plan
- An investigative tool
Chapter 6: Business Plan

Elements of a Feasibility Analysis

Two areas of focus:
1. Determining how attractive an industry is overall as a “home” for a new business
2. Identifying possible niches a small business can occupy profitably
Five Forces Model

Five forces interact with one another to determine the setting in which companies compete and, hence, the attractiveness of the industry:

1. Rivalry among companies in the industry
2. Bargaining power of suppliers
3. Bargaining power of buyers
4. Threat of new entrants
5. Threat of substitute products or services

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Five Forces Model Diagram

- Potential Entrants
- Threat of New Entrants
- Suppliers
  - Bargaining Power of Suppliers
- Industry Competitors
  - Rivalry among existing firms
  
  
- Buyers
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Rivalry Among Companies

- Strongest of the five forces
- Industry is more attractive when:
  - Number of competitors is large, or, at the other extreme, quite small
  - Competitors are not similar in size or capacity
  - Industry is growing fast
  - Opportunity to sell a differentiated product or service exists

Five Forces Model

- Bargaining Power of Suppliers
- Threat of New Entrants
- Industry Competitors
  - Rivalry among existing firms
- Bargaining Power of Buyers
- Threat of Substitutes
  - Products or Services
- Potential Entrants

Bargaining Power of Suppliers

- The greater the leverage of suppliers, the less attractive the industry
- Industry is more attractive when:
  - Many suppliers sell a commodity product
  - Substitutes are available
  - Switching costs are low
  - Items account for a small portion of the cost of finished products
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Bargaining Power of Buyers

- Buyers' influence is high when number of customers is small and cost of switching to a competitor's product is low
- Industry is more attractive when:
  - Customers' switching costs are high
  - Number of buyers is large
  - Customers want differentiated products
  - Customers find it difficult to collect information for comparing suppliers
  - Items account for a small portion of customers' finished products
**Threat of New Entrants**

- The larger the pool of potential new entrants, the less attractive an industry is.
- Industry is more attractive to new entrants when:
  - Advantages of economies of scale are absent
  - Capital requirements to enter are low
  - Cost advantages are not related to company size
  - Buyers are not loyal to existing brands
  - Government does not restrict the entrance of new companies

**Five Forces Model**

- Potential Entrants
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- Threat of Substitute Products or Services
- Substitutes
- Industry Competitors
- Rivalry among existing firms
- Buyers
- Bargaining Power of Buyers

**Threat of Substitutes**

- Substitute products or services can turn an industry on its head.
- Industry is more attractive to new entrants when:
  - Quality substitutes are not readily available
  - Prices of substitute products are not significantly lower than those of the industry’s products
  - Buyers’ switching costs are high
Five Forces Matrix

<table>
<thead>
<tr>
<th>Force</th>
<th>Importance (1 = Not Important, 5 = Very Important)</th>
<th>Threat to Industry (1 = Low, 5 = High)</th>
<th>Weighted Score (Col 2 x Col 3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rivalry among competitors competing in the industry</td>
<td>5</td>
<td>5</td>
<td>25</td>
</tr>
<tr>
<td>Targeting power of suppliers in the industry</td>
<td>2</td>
<td>4</td>
<td>8</td>
</tr>
<tr>
<td>Threat of new entrants to the industry</td>
<td>5</td>
<td>4</td>
<td>20</td>
</tr>
<tr>
<td>Threat of substitute products or services</td>
<td>4</td>
<td>3</td>
<td>12</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td></td>
<td>63</td>
</tr>
</tbody>
</table>

Business Prototyping

- Entrepreneurs test their business models on a small scale before committing serious resources to launch a business that might not work
  - Example: eBay
- Recognizes that a business idea is a hypothesis that needs to be tested before taking it full scale

Elements of a Feasibility Analysis
Product or Service Feasibility Analysis

- Determines the degree to which a product or service idea appeals to potential customers and identifies the resources necessary to produce it.
- Two questions:
  - Are customers willing to purchase our good or service?
  - Can we provide the product or service to customers at a profit?

Primary research – collect data firsthand and analyze it
- Customer surveys and questionnaires
- Focus groups

Secondary research – gather data that already has been compiled and analyze it
- Prototypes
- In-home trials

Elements of a Feasibility Analysis
Financial Feasibility Analysis

- Capital requirements – must have an estimate of how much start-up capital is required to launch the business
- Estimated earnings – forecasted income statements
- Return on investment – combining the previous two estimates to determine how much investors can expect their investments to return

A Business Plan Is...

- a systematic evaluation of a venture's chances for success
- a way to determine the risks facing a venture
- a game plan for managing a business successfully
- a tool for comparing actual and target results
- an important tool for attracting capital

A Business Plan: Two Essential Functions

1. Guiding the company by charting its future course and defining its strategy for following it
2. Attracting lenders and investors who will provide needed capital
A Business Plan

- A plan is a reflection of its creator
- Sometimes the primary benefit of preparing a plan is the realization that a business idea just won't work!
- The real value in preparing a plan is not as much in the plan itself as it is in the process of creating it

Why Take the Time to Build a Business Plan?

- Although building a plan does not guarantee success, it does increase your chances of succeeding in business
- A plan is like a road map that serves as a guide on a journey through unfamiliar, harsh, and dangerous territory. Don't attempt the trip without a map!

Writing a Business Plan

- Typical plan is 25 to 50 pages long
- Like every business venture, every business plan is unique
- Use it to tell your company's story
Key Elements of a Business Plan

- Title page and table of contents
- Executive summary
- Mission statement
- Company history
- Business and industry profile
- Business strategy
- Description of products/services

Features vs. Benefits

- Feature – a descriptive fact about a product or service ("an ergonomically designed, more comfortable handle")
- Benefit – what a customer gains from the product or service feature ("fewer problems with carpal tunnel syndrome and increased productivity")

Key Elements of a Business Plan (Continued)

- Marketing strategy
Marketing Strategy

- Prove that a market exists
  - Show customer interest
  - Document market claims with research
- Describe target customers
- Advertising and promotion
- Market size and trends
- Location analysis
- Pricing
- Distribution

Key Elements of a Business Plan

- Marketing strategy
- Competitor analysis
- Owners’ and managers’ résumés
- Plan of operation
- Financial forecasts

Financial Forecasts

- Projected financial statements
  - Monthly for one year
  - Quarterly for next two
- Income statement
- Balance sheet
- Cash Flow
- Capital expenditures
Financial Forecasts

- Three forecasts
  - Pessimistic
  - Most Likely
  - Optimistic
- Realistic!
- Include assumptions on which forecasts are based

Key Elements of a Business Plan

- Marketing strategy
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- Loan/investment proposal

Tips on Preparing a Business Plan

- Make sure your plan has an attractive cover. (First impressions are crucial.)
- Rid your plan of all spelling and grammatical errors
- Make your plan visually appealing
- Include a table of contents to allow readers to navigate your plan easily
Tips on Preparing a Business Plan

- Make it interesting!
- Use spreadsheets to generate financial forecasts
- Always include cash flow projections
- Keep your plan “crisp” - between 25 and 50 pages long
- Tell the truth - always

Your Plan Must Pass Three Tests

- The Reality Test - proving that:
  - A market really does exist for your product or service
  - You can actually build or provide it for the cost estimates in the plan
- The Competitive Test - evaluates:
  - A company’s position relative to its customers
  - Management’s ability to create a company that will gain an edge over its rivals
- The Value Test - proving that:
  - A venture offers investors or lenders an attractive rate of return or a high probability of repayment

The "5 Cs" of Credit

- Capital
- Capacity
- Collateral
- Character
- Conditions
Presenting the Plan

- Prepare!
- Demonstrate enthusiasm, but don't be overemotional
- Start by communicating the dynamic opportunity your business idea offers
- “Hook” investors quickly with an up-front explanation of the venture, its opportunities, and its benefits to them

Presenting the Plan (Continued)

- Use visual aids
- Hit the highlights; focus on the details later
- Keep your presentation “crisp” – 2 or 3 major points
- Avoid overloading your audience with technical jargon

Presenting the Plan (Continued)

- Answer every lender or investor's question: “What's in it for me?”
- Close by reinforcing the nature of the opportunity
- Be prepared (with details) for questions investors are likely to ask
Presenting the Plan

- Learn to read the pattern of investors' questions and address the issues that concern them
- Follow up with every investor to whom you make your presentation