Business Plan Basics

This business tool will help you set goals and achieve them…and win friends at the bank

by Ed Dunnavant

Many builders are so busy orchestrating the elements of individual projects that they spend little time — or often no time at all – planning the course of the business itself.

In good times, the task of committing a business plan to paper can seem superfluous – even a little dangerous. We all tend to be just a little superstitious about "messing with success." In bad times, our attention can become so scattered that we are overcome by the "paralysis of analysis," and we lose the ability to clearly plan for the future.

But the reality is that in good times and bad, a carefully considered business plan can be the compass that keeps us on a steady course toward success. During an "up" cycle, a business plan helps us take advantage of every opportunity without overextending our resources. During the inevitable "down" cycle, it provides the direction we need to weather the storms.

Benefits of a Plan

Anyone who has ever attended a management seminar already knows that a business plan offers a wide range of valuable benefits. But since so few of us rush home and actually write a plan, the benefits bear repeating.

For starters, the very process of creating a plan sharpens your communications skills – both within and outside of your company. It forces you to objectively review where you've been, where you are, and where you want to be in 12 months, in three years, and in five years. It forces you to closely examine such issues as diversification, personnel strengths and weaknesses, changes in competition, local demographic changes, and even your personal goals.

It also helps you more clearly communicate your objectives to those who will help you achieve them – your employees, suppliers, subcontractors, family (often you most valuable brainstorming and support group), and lenders.

Employee morale is almost always higher when people understand the company's immediate and long-term goals. It helps employees see how their performance directly affects those goals. Your suppliers are much more likely to extend greater lines of credit when they know you have a well though out growth plan. Everyone likes to associates with winners. If you plan requires short-term sacrifices by your family, it is essential that you share your vision for the ultimate payoffs they will receive. And today, virtually every lender wants to see hard evidence that its customers are prepared to deal with whatever challenges the overall economy might present.

Finally, as most highly successful professionals will attest, a written plan not only helps you spot trouble earlier, manage cash more effectively, and increase operational efficiency, it also tends to become a positive, self-fulfilling prophesy.

Since many lenders require a business plan as part of the submissions for a project loan, it makes sense to write your plan so that it can be excerpted easily for inclusion in such packages.

Toward that end, these three key elements are good starting points:

Part I: Company overview. This is a summary of jobs you have completed and lessons you have learned from your successful and not-so-successful endeavors. The trained business people who review your plan, whether they are lenders or suppliers, understand that we often learn more from our failures than from our successes. They also are likely to know about your less-than-successful ventures and will appreciate your candor.

Include personal and professional references in this section and update them regularly. It's handy to have a current reference list. Remind yourself to keep in touch with these people regularly.

This section isn't just for business activity. Describe your personal business history and credentials in the community: your professional experience, your skills, and your involvement in civic, religious, and charitable activities.

Describe the company's management structure. If you own the company, what would happen of you were to die? If the company is a partnership, what are the responsibilities and liabilities of each partner? What is the chain of command in your company? Do you have a buy/sell agreement that is adequately funded? What happens if the partners disagree?

Part II: Goals. In most cases, a business plan should contain three subsections for goals: objectives for the next 12 months, three years, and five years.

Include as much detail as possible about what you wish to achieve, but also build in flexibility so that your plan will remain viable if conditions change.

In the case of each goal, include:

- The obstacles you may need to overcome.
- The necessary financial arrangements.
- The needed personnel.
- The new knowledge or skills that may be needed.
- The people or groups who can help.
- The benefits you expect to gain from achieving it.

You are likely to benefit as much from writing the plan as you will from following it. During the writing, you may discover that some of the goals you had been carrying around in your head are either not appropriate or even desirable when viewed in terms of the operational changes and/or investment necessary to achieve them. On the other hand, you may discover that certain opportunities for growth that you had not considered are actually "naturals" for your company.

When including specific new projects among your goals, make sure you avoid the common pitfalls of market analysis. These include:

- Relying on population and housing-need projections made by public or private agencies without knowing the agency's purpose in making the projections. For example, a local government planning department is likely to project population growth at the highest reasonable levels because its purpose is to ensure that adequate public facilities will be available if the population reaches projected levels.

- Not knowing when a "hole in the market" is a bottomless pit. While smart builders and developers are always looking for a market niche that everyone else has overlooked, the mere absence of a given product type or price of product does not necessarily indicate a lucrative niche. There's a good chance that nobody else is building that product simply because nobody wants to buy it.
- Not digging deeply enough into what others are planning. Plan approvals and land transfer notices tell what competitors are doing. By attending planning commission meetings and by listening to what lenders, brokers, and other builders and developers are saying, you'll know what your competitors plan to do. Your market research should include data on how much land is available (or could be made available through rezoning) for a development similar to the one you're considering.
- Assuming that numbers tell the whole story. Numbers show housing needs (for example, they might indicate a shortage of rental housing), but only exposure to the human elements of the market place gives a clear picture of consumer wants. For example, there might actually be a pent-up demand for affordable housing even when total activity appears to exceed market need. Buyer surveys, focus groups, and a hard look at all project and price-range comparables (check the ones that aren't selling well, too) will provide information on critical factors like amenity preferences that may be peculiar to your city or the section where you want to develop.

The goad-writing process also forces you to objectively review your personnel. Can your existing staff handles the new responsibilities needed to meet new goals? So employees need special training or more education? Are they psychologically prepared for change? If you must add staff, where will you find qualified candidates? When should you start looking? How will you pay for new positions? Do you need to trim your staff?

Finally, don't forget to factor in personal goals. You may not want to share this section of the plan with others, but it's important to put in writing the goals you have for your own professional, personal, and social development. If your plan isn't flexible enough to accommodate your need for time with your family, community, and religious organization, as well as time to simply relax, then it is usually doomed from the start.

Remember, realistic is better than overly optimistic.

Part III: Balance sheet and profit/loss statement. The financial sections of your plan should include forthright summaries of:

- Assets (cash collateral).
- Liabilities (including those from other companies in which you may have some ownership).
- Short-term funding sources. (Where are you getting your funds for operational expenses?)
- Long-term finding sources. (What is you long-term dept? Interest burden? Notes coming due?)
- Owner's contribution. (How much are you "putting up?" The day of leveraging is over.)
- Net worth. (A negative net worth doesn't mean you can't still do business. Everyone has had adversity; show how you plan to achieve a positive net worth.)
- Income. (Is it realistic? Remember to pay yourself first. Don't be greedy, but don't pay yourself less than someone else would pay you for the same work.)
- Expenses. (Which are fixed and necessary? Which are variable? Which can be eliminated?)
- Profit. (Remember, you can't spend depreciation and lenders generally don't accept it as a profit factor. If you so have profits, don't tie cash up in trades and notes that aren't liquid. You need an accessible reserve to bail yourself out when the down cycle hits. Goal: Cash to fund six months of operating expenses.)

Practice "what if" scenarios when writing your plan, so you will have workable pro-formas for best-case, worst-case, and most-likely situations. Play with the numbers to see what happens if you trim staff, for instance, or add employees.

When you have completed a first draft of the plan, ask a trusted associate to review it. This can be a lender you've worked with; he can often suggest changes that should be made before presenting the plan to a loan review board. The reviewer can be an experienced "old timer" – a retired builder or developer who may be willing to serve as a mentor, or a peer who is an important member of your professional network.

Remember, too, the number one rule about professional networks: If you don't have a network in place before you need it, you won't have it when you need it. Establish relationships with at least two subs and suppliers for each product so you'll never be left in the lurch. Similarly, establish continuing relationships with at least two lenders; lending officers change jobs just like everybody else, and you don't want to be talking to a stranger when you submit your loan request.

Perhaps the biggest benefit of a written business plan is that it helps you recognize your own strengths and respond accordingly. The smartest, most successful – and happiest – people clearly understand that they can't excel at everything. So, concentrate on doing what you do best, hire others to do the rest, and set goals that are not only satisfying, but also attainable. ■

Ed Dunnavant is a professional associate with the Greenman Group, Inc., a national new-home marketing and management consulting firm based in Hollywood, Fla. He is also president of Dunnavant & Associates, the home-building company he founded in Richmond, VA, in 1972, and he is a past president of the Richmond Home Builders Association.