

NORTHWEST FARM CREDIT SERVICES

BUSINESS TOOLS

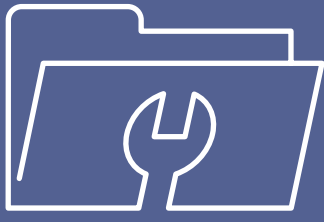
Strategic Business Planning

Tip: Those who prepare a business plan are 10 to 20 times more profitable.

Farm and ranch managers generally spend most of their time making day-to-day operational decisions, like when to seed or harvest, when to sell cows or whether to purchase equipment now or later. While short-term operational planning is important, it does not substitute for long-term planning, which charts where the owner wants the business to go, how it will get there, who will be involved, and what resources will be needed. Most business owners hope for a better future, but figuring out just how to make it happen can be challenging. Long-term strategic business planning can help.

Why do business planning?

The saying, "If you don't know where you're going, any route will take you there," reflects the importance of business planning. Developing a business plan is a process to help business owners grow their operations, increase profits, develop and market products, or plan for business transition. A good planning process allows business owners time to step back from the day-to-day operations to focus on the bigger picture. Thoughtful discussions with key players inside and outside of the business help to



Tip: Effective business plans incorporate input from everyone who has a stake in the business.

ensure a common vision and understanding of where the business is headed, how it's going to get there, and what objectives or milestones will be used to measure success. Business planning also helps avoid short-term emotional decisions and focuses decisions on pre-set objectives and goals.

How to formulate business plans

Business plans may be prepared for many different reasons, including new business start-ups, major changes in existing businesses, or to maintain the strategic direction of an ongoing business. Business plans can be used internally for management purposes and externally to communicate the vision and plan to attract investors, to obtain financing from creditors, or to recruit quality partners or employees. Business plans provide the business owner with a way to evaluate the feasibility of a proposed venture. The process may reveal previously unconsidered opportunities or limitations. Business plans should provide clear direction for the organization. They may be customized depending on the target audience — investors, creditors, board of directors, family members, employees, or others.

Do agricultural businesses need a business plan?

A written business plan can be invaluable for

both large and small businesses, especially those in an expansion or transition mode. Even small, stable businesses can benefit from a simple business plan that focuses on those areas that address perceived weaknesses in meeting business objectives. While most farmers and ranchers have a clear plan in mind for their operation, conditions can change rapidly. The value of a written business plan is to provide a well thought out and agreed upon guide for making daily decisions and to help evaluate business opportunities and threats. Many agricultural producers are turning to alternative crops, employing non-traditional practices, planning for transition, or implementing unproven technology. In these situations, a sound business plan is essential.

What is a business plan?

A business plan is a written document outlining the goals, strategies, and action plans for the key functional areas of a business including management, finance, production, and marketing operations. Simply put, a business plan is a road map for a business. The depth of detail that a business plan contains will vary depending on the scope of the business and the purpose for which the plan is being prepared. For example, a non-traditional business trying to obtain venture capital will have a much more detailed plan than a more conventional

business trying to obtain a small loan. Almost all business plans have parts in common, which will be discussed later.

Who should prepare the plan?

Tip: A business plan is an overview of your journey, not the destination.

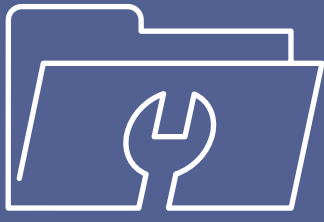
How are business plans best prepared? Should a plan be developed alone or should someone be hired to facilitate the process? Although professional consultants can help in developing business plans, the business owner should take the lead role and ultimate responsibility to develop and implement a plan. The most effective planning processes seek and incorporate input from every level of the organization. In a family business, both spouses should have input as well as other family and non-family members who have a stake in the business. In a large business, the president or manager should not have sole responsibility for creating the plan. Numerous templates are available for developing business plans. While these templates are useful for providing a basic framework, their flexibility may be limited. Combining these programs along with individual creativity will make for a better plan.

Where can you get information and help in developing a business plan?

Northwest Farm Credit Services' Business

Management Center helps business owners learn how to better manage their businesses and transition ownership. Through the BMC, producers gain access to information, industry knowledge, and business planning expertise through seminars and individual business consulting. Sources such as the Cooperative Extension Service, Small Business Administration, universities, and regional small business centers can also provide general information and guidance. These organizations may offer help in obtaining financing or finding investors.

Numerous sources of data are available for specific industries and markets. Primary data includes market surveys, questionnaires, focus groups, or other data collected firsthand by the business. While primary data is the most specific to a business' needs, it's the most difficult and costly to obtain. Secondary data is obtained from an external source, such as lenders, trade associations, census data, magazines, journals, other publications, or marketing research firms. Financial data for specific industries is available from sources such as the USDA's National Agricultural Statistic Service Resource at www.nass.usda.gov. The largest source of secondary data available is the Internet. One should use caution and evaluate the quality, source, and age of any secondary data, regardless of how it's obtained.



Tip: A good business plan can take anywhere from 50 to 100 hours to prepare. This sounds like a lot of time, but it's not when you are making a five or six figure investment.

What are the various components of a business plan?

The following components are generally found in most business plans. The order and emphasis placed on each component will vary depending on the business and purpose of the plan.

Executive summary

Depending on the needs and length of the plan, an executive summary, or concise overview of the key aspects of the plan is helpful. This summary, which should be written after the plan is complete, gives an interested party a quick overview of the plan to help create understanding and enthusiasm about the business and opportunities that exist.

History and general description

The history and general description of the company is a current inventory of what the business is about, its structure, and why this structure is important to current success. This section includes a list of farm partners and key employees by name and background qualifications, the reasons for starting the business or adding the new product, and general description of the industry. For an existing business, a discussion of products and their success (or failure) should be included.

Vision statement

A vision statement describes the grand goals the organization would like to achieve and how it will look when it operates effectively and efficiently to achieve the vision. Vision is the concrete statement of your ultimate dreams for the business. The vision statement answers the question "What will success look like?" Below is an example of a vision statement.

Smith Ranches will be the most successful Angus cattle producer in Washington, producing the best quality, high-demand cows in a state-of-the-art, paid for, breeding facility, which is efficiently run by committed Smith family members and loyal cowboys who all reside in and support the Valley community.

Core values

Core values are the most important, deeply held values of the business and are independent of the current external environment. Values reflect the character and culture of the business. They are the convictions on how business is to be conducted and how people are treated, inside and outside the organization. Some examples of core values include.

- **Integrity** – we do what's right for everyone through honesty, fairness, and conscientious accountability.

Tip: Define niches that the business plan can meet profitably.

- **Accountability** – we take personal responsibility for our actions; say what we'll do and do what we say with a sense of pride and commitment to the organization.
- **Action Driven** – we are determined and motivated to accomplish our goals without being afraid to make the first move or take the steps necessary to fulfill the mission.
- **Team Oriented** – we achieve a shared vision by recognizing individual talents and team synergies through effective communication.

Mission statement

A mission statement describes why the business exists. It should be brief and general enough to be flexible, but rigid enough to give the business a strategic direction. A mission statement may encompass both personal goals and business goals. Some of the key questions a mission statement should answer are: What do we produce? Who do we produce for? Why? Where? How?

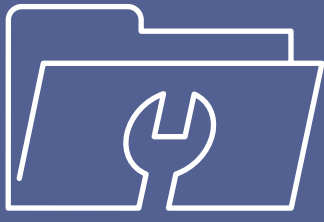
Like the entire business plan, development of the mission statement should include input from all levels of the organization, not just management. The mission statement should be visible; that is, every person involved in

the business, not just the owner or manager, should know and easily grasp the concepts contained in it. An example of a mission statement is:

To profitably provide high quality beef to health conscious consumers, sustaining a family business and balanced lifestyle.

Organization and management

The plan should explain how the business is organized; examples include sole proprietorship, partnership, corporation, or limited liability company. The duties and responsibilities of all involved should be outlined. For larger businesses, an organizational chart should also be included. Details on management compensation and allocation of profits and losses are essential, along with a backup management plan. If seeking outside financing, readers will want to know what experience each key person holds that make him or her compatible with the venture. In a family business, each member's role and responsibilities in the operation should be clearly defined. If expertise is weak in a certain area (marketing, sales, finance, etc.), the plan should express concern about this issue and offer ways to compensate for the problem. If professional consultants, such as lawyers or accountants, are to be used, this section should explain their roles.



Tip: If you can't communicate the essence of your plan on a napkin, it's probably too complex.

The business plan may also include a transition strategy, particularly when a business succession is planned. Plans regarding ownership, management, and asset transition should be discussed. Estate planning issues, particularly in smaller operations, may also be addressed.

SWOT analysis – strengths, weaknesses, opportunities, and threats

Once the foundation issues of vision, values, and mission have been determined, the internal and external factors affecting the business should be assessed. One of the most popular tools in this assessment is a SWOT analysis. A SWOT looks at all the positive and negative factors inside and outside the business that impacts the operation's success.

Strengths and weaknesses are internal to the operation, meaning they are areas that can be influenced or controlled. Strengths and weaknesses usually fall under four main categories: human competencies, products and services, process capabilities, and financial, physical, and/or natural resources. Strengths can be leveraged and built upon, while identified weaknesses should be minimized or eliminated.

Opportunities and threats, on the other hand, are external, market factors that can

impact the business either positively or negatively. These are areas that are not controllable, but need to be identified and taken into account during the planning process. Ultimately, the goal is to identify ways to align the operations strengths with external opportunities in the marketplace. And conversely, to minimize those weaknesses that compound the business' vulnerability in the face of market threats.

Market analysis

Analysis of the market is the backbone for most business plans. A business will not be successful, regardless of how well other business details are managed, if incorrect assumptions are made about markets or if products don't meet customer expectations. The market analysis outlines what customer needs are being met by the business, why the products or services are unique, and who will be attracted. It's also the time in planning to "think outside the box" to determine if there are market niches that the business can meet profitably. Many producers possess special talents and skills or can produce and distribute specialty products that could be profitable.

The market analysis considers the political and legal, economic and environmental, social and cultural, and technological environments. It also includes a definition

Tip: Failing to prepare is preparing to fail.

of the target market, or group of potential customers with similar characteristics, that will be the focus of marketing efforts. It's important to state the reasoning behind choosing a particular target market. The potential number of people in a market, emerging trends, and anticipated market share should be analyzed. Competitive analysis, looking at the strengths and weaknesses of the competition, indicates what competitive edge a business holds. Strategies for gaining market share from the competition may also be necessary.

Key planning assumptions

Much of business planning is based on logical assumptions rather than hard facts since it's impossible to have data to support every aspect of a plan. Therefore, assumptions of how issues outside the owner's direct control will evolve during the planning period should be established. It's critical to outline the key planning assumptions from the start to help avoid bias because of the emotion involved in planning a business venture. Key planning assumptions may include trends in supply and demand, the global economy, the marketplace, or consumer behavior patterns. They may also include changing government policy or the future of a particular technology.

Be sure to document sources of key data and assumptions. Using reliable sources of information in the business plan will help avoid using assumptions of what the owner hopes will happen, versus what an informed, unbiased third party believes is likely to happen.

Goals

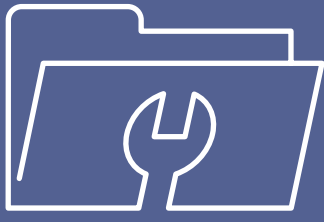
While the mission statement is broad and general, goals are quantifiable and specific.

Goals may be related to sales, profits, and efficiency, or may involve expansion or bringing another partner into the business. These should be SMART goals: specific, measurable, agreed to, realistic and measurable. Goals should be directed into two areas: long-term or strategic goals, for three to five years, and short-term or tactical goals, which are for one year or less.

Examples of goals are:

Long term

- Increase gross revenues by 5 percent over each of the next three years.
- Reduce leverage (debts/assets) to 30 percent or less within three years.
- Bring a son or daughter into a management position within two years.



Tip: Plans should recognize roadblocks and provide contingency plans to overcome them.

Short term

- Reduce death loss in the cattle herd to under 5 percent next year.
- Build working capital to account for at least 25 percent of business expenses by next year.

Marketing strategy

The marketing strategy describes how sales goals will be accomplished in light of the conditions uncovered in the market analysis. A marketing strategy includes decisions regarding product selection and design, pricing, distribution, and promotion. Knowing break-even prices is critical to developing a sound marketing plan. A good marketer may resolve the emotional dilemma of foregoing “opportunity income” by selling inventory at a level below the top of the market. A good marketing strategy may include selling inventory above break even on a timely basis. If a product is branded or is a proprietary variety, the marketing strategy should discuss how the product will be protected to maintain its uniqueness.

A marketing strategy should be developed before the product has to be marketed to meet financial obligations or other deadlines. A well-developed and logical marketing strategy can avoid the mistake of holding inventory as an euphoric rise

in the market suddenly drops below the break-even point. It’s also important to have a backup marketing strategy in case the original plan fails.

Financial strategy

Every business owner should understand his or her operation’s strengths and the financial risks that may adversely impact success if the worst case events occur. The financial plan also determines whether the marketing and operational goals of the business plan are feasible. The financial plan should include initial financial requirements, historical and projected financial statements, and break-even analysis.

Lenders and/or investors will generally look for answers to these basic questions:

- How much money is needed?
- How long will the money be needed?
- What rate of return can be expected for investors?
- How will borrowed funds be repaid?
- What are the risks?

Current and projected balance sheets should show the initial financial position of

Tip: Projected income (profit and loss) statements and projected cash flows should be prepared.

the business with the relative investment levels of the owners, investors, and creditors. The impact of initial cost overruns on the amount of capital needed should be addressed. Projected income (profit and loss) statements and projected cash flows should be prepared. Sensitivity analysis of the best, worst, and most likely cases should show the impact of deviations in revenue and expense projections on income and cash flow. Properly prepared cash flow projections will uncover the need for and timing of short-term financing. This is essential to an effective operational plan.

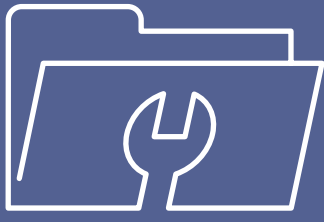
It's also critical that business owners understand key financial ratios and what they mean to the business. These five key ratios include: liquidity, solvency, profitability, repayment capacity, and financial efficiency.

- Liquidity is the financial ability, without disrupting normal business operations, to cover short-term cash obligations with available cash or near-cash assets.
- Solvency is the relationship between assets and liabilities. Solvency addresses the issue of how much of the business is owned and controlled by the owners versus how much of the business is under creditors' ownership and control.

- Profitability compares business revenues against all economic costs. It evaluates how productively a business utilizes its available resources.
- Repayment capacity measures the ability of a business to meet all financial obligations. Sound repayment requires a margin above all economic costs to set aside for reserves, future growth, and personal retirement purposes.
- Financial efficiency measures how efficiently a business uses its productive capabilities.

Operations and production

Another key aspect of a business plan is operational, which addresses issues related to location, facilities, equipment and material needs, supplier and distribution factors, personnel management, processes, inventory, and quality controls. This portion of the plan should tie together the product, marketing, and financial sections of the business plan into a unified approach toward running the business. The capacity of facilities to meet expansion needs, the availability of competent employees, and how quality will be measured and maintained should be addressed. A systematic flow diagram showing labor needs, timing, inventories, and scheduling may be needed.



Tip: Implementing appropriate evaluations and controls let business owners and others know that the plan is successfully being executed and that milestones are being met.

Action plans

Even the most well developed objectives and strategies can become meaningless without appropriate actions. One of the most effective ways to define tactical responsibilities and to hold individuals accountable is by developing specific action plans for each goal. Action plans should clearly define the action step, responsibility, and time frames to effectively accomplish each goal. Managers should periodically review the status of action plans to assess how well the business plan is being implemented.

Evaluation and controls

How will results of the plan be measured? Implementing appropriate evaluations and controls let business owners and others know that the plan is successfully being executed and that milestones are being met. These controls also ensure accountability and discipline in following the plan. Progress reports in completing action plans and operating data from normal business activity can be used as guide posts to measure progress. Accounting, production, sales, inventory, and other records can be key sources of information. As conditions change, these pre-determined control measurements can help business owners identify areas for improvement and goals

for getting performance back on track. A control or evaluation system should be easy to operate and maintain. The system should be so practical that it becomes a natural part of the management process.

A business does not benefit from a plan sitting on a shelf collecting dust. Oftentimes, business owners view the business plan as a one-time-only document to be used for a specific purpose and then forgotten. Business owners who are most successful in following through on the planning process view the business plan as a living document. The plan should be updated annually. It may need to be updated more frequently if the business is having trouble or if the marketplace is changing rapidly.

Appendices

Any relevant and supporting information that does not fit appropriately into the body of the business plan may be placed in appendices. Examples include management charts, resumes, brochures, letters of recommendation, or details on markets, finances, or operations. Placing irrelevant or excessive amounts of material in the appendices should be avoided.

Format

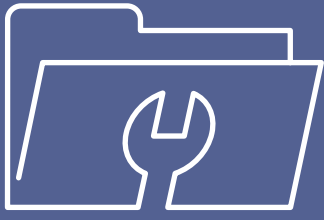
The length of the plan will vary, but most

plans are between 10 and 50 pages, excluding appendices. Often, a table of contents and cover pages are included for easy reference. Depending on the situation, plans should be dated and marked confidential. If appropriate, copies should be numbered before distribution.

Tip: The business plan should be a team effort and involve not only management but also key family and non-family members or stakeholders.

Common pitfalls in business planning

- **Too much detail** – There is a fine line between too little and too much detail in a business plan. Minute or trivial items that dilute or mask the critical aspects of the plan should be avoided.
 - **Graphics without substance** – With the sophisticated computer software available to the average user today, it's easy to overemphasize aesthetics while compromising substance. Graphics can be a complement to, but not a substitute for, logic and reasoning.
 - **No executive summary** – Many readers of business plans will not read past the executive summary; if it does not exist, they may not read the plan at all.
 - **Inability to communicate the plan** – The business plan should clearly outline the proposal in understandable terms.
- Monumental ideas are worthless if they can't be communicated.
- **No sensitivity analysis** – All quantitative aspects of a business plan should be tested for sensitivity. The most common areas tested are revenues and expenses. However, sensitivity analysis can be conducted on interest rates, yields, production variables, or any other quantitative measure that is relevant to business success.
 - **Failing to anticipate problems** – A good business plan will recognize potential roadblocks that could arise in implementing the plan and provide contingency plans to overcome them.
 - **Lack of involvement** – The business plan should be a team effort and involve not only management but also key family and non-family members or stakeholders. Careful consideration should be given before making the decision to shift responsibility of preparing the plan to someone outside the business. It's okay to have an outside consultant facilitate the development of a plan, but ultimately, the business owner is responsible. The strategic process of developing the plan is a key component of its success.



FOR ADDITIONAL INFORMATION:

farm-credit.com

1.800.743.2125

Tip: Farmers and ranchers can often become so focused on producing the product they forget about what the customer expects and wants to buy.

- **Infatuation with product or service** – Although a business plan should clearly explain the attributes and production of the business' key product or service, it should focus on the marketing plan. Farmers and ranchers can often become so focused on producing the product they forget about what the customer expects and wants to buy.
- **Focusing on production estimates** – When making projections, the focus needs to be on sales estimates, in addition to production estimates. Production is irrelevant if there are no buyers.
- **Unrealistic financial projections** – Potential investors are certainly interested in profitability so that they may earn a return on investment. However, unrealistic financial projections can quickly cause a plan to lose credibility in the eyes of investors.
- **Speak to your audience** – Technical language, acronyms and jargon that would be unfamiliar to a person without experience in a particular industry should be avoided. The reader will be more impressed if he or she understands the plan.
- **Lack of commitment** – The entrepreneur must show commitment to his or

her business if he or she expects a commitment from others. Commitment is exhibited by timeliness and following up on all professional appointments. Investment of personal money is looked upon favorably because it shows that the owner is willing to make a financial commitment.