

## CHAPTER 3

# Strategies for Evaluating Opportunities

### *The Assessment Process*

*Being an entrepreneur doesn't mean jump off a ledge and make a parachute on the way down.*

—Fred Smith, founder of FedEx

*Be wary of the man who urges an action in which he himself incurs no risk.*

—Joaquín Setanti, circa 1614, Catalán, Spain

#### Objectives:

1. Understand the role of opportunity evaluation in the entrepreneurship process
2. Learn methods of evaluation that can be used for the initial idea and subsequent opportunities in the life cycle of the new venture
3. Prepare the Opportunity Organizational Proposal (OOPs), which is based on a comprehensive analysis of the feasibility of the venture idea
4. Undertake the feasibility analysis by completing the five sections of the OOPs

## Strategy in Action

### Scott Cook, Founder of Intuit

Scott Cook is the founder of Intuit, the company that developed Quicken and Quickbooks, the personal and business financial tools. He has been Intuit's CEO for more than 22 years, building the company into a \$1.7 billion enterprise. While most people are familiar with Intuit's progress and are likely to have used one of its products to help manage their personal or business finances, Cook's entrepreneurial journey is not widely known.

In 1983, when he launched Intuit, Cook already had significant corporate experience. He held an MBA from Harvard and had worked at Procter & Gamble as a brand manager and at Bain as a consultant. Cook's founding principle was, "Listen to your customers." His strategy was in place before the publication of *In Search of Excellence*, by Tom Peters and Bob Waterman, the book that made paying attention to your customers a core business value of excellent companies. Consider this Cook program, which emerged during the early days of Intuit, called Follow Me Home.

Intuit employees were assigned to stay in the local computer store until someone bought Quicken off the shelf (this was back when people did that sort of thing). The employees would then ask the buyers to take them home so they could see how difficult the product was to install. By observing customers at home, Intuit employees could gain valuable insights from every action, from how easily the shrink-wrap came off to which lines of the directions caused frustration. Cook insists, "If there were problems, the fault was Intuit's, not the customer's. Every pause, every source of frustration, [was] evidence of something Intuit needed to fix." Cook believes in radical simplification. He always knew that Intuit had to do more than just make Quicken better and easier than every other software program; it needed to make Quicken better and easier than the pen and paper check-writing process that Quicken aimed to replace. Cook knew that if he and his company were alert and creative and open-minded enough, then accomplishing this was possible: Their customers would tell them how.

Cook's assumption proved to be true. During Intuit's second decade, "customers invented our mid-market business before we even saw the possibility." Entrepreneurs had begun using Quicken to run the finances of their companies, modifying the program to suit their needs. The launch of Quickbooks came in 1992, and it allowed small businesses to manage their money in ways that had not been possible. By the end of its first full month on the market, Quickbooks became the best-selling accounting software. Cook claims this happened because of the fundamental innovation in Quickbooks. "It didn't come out of any big fancy R&D lab. It came out of us being closer to understanding the customer and the prospect than anyone else."

One of the key pieces of advice Cook shared for budding entrepreneurs is especially appropriate during the phase of the life cycle when the opportunity is being assessed and the entrepreneur wants to find out whether or not the concept will work. What does Cook advise?

"Behave humbly. Be humble about your importance, about how many answers you know, and about how much you don't know (which is always more than you think), humble about the need to engage with and learn from people around you, humble about customers, humble about learning. Please understand that I'm saying behave humbly; I don't think you can actually will yourself to be humble, but you can behave humbly. Which means saying, often, 'I was wrong.'

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Which you'll discover is the moment when the real insights and breakthroughs occur. And when it's hard to behave humbly because you're afraid people won't value you, just remember: People already know, they can see through you. They know what you're good at and what you're not, so don't pretend. Instead, try being true. Be human and vulnerable, the way you really are. And you'll find that by admitting you're not good at stuff, you build a bridge to people. You give them room to contribute."

Cook says, "Realize that to a scary degree a company grows to reflect its founder. Unlike with your kids, there are no unalterable genetics to blame, it's all nurture. You get to start the code. So be customer-driven. My biggest surprise was discovering how customers will invent your business for you. And commit to the right values—be straight, tell the truth. Especially the bad news. You'll discover that people always get over it, and even admire the effort you make trying to fix things. Short-term losses become long-term gains."

SOURCE: M. Hopkins, "25 Entrepreneurs We Love," *INC*, April 1, 2004. Retrieved February 13, 2006, from <http://www.inc.com/magazine/20040401/25cook.html>; C. Tkaczyk, "The Best Ideas Come From the Front Line," *Fortune*, Nov. 15, 2004, p. 193.

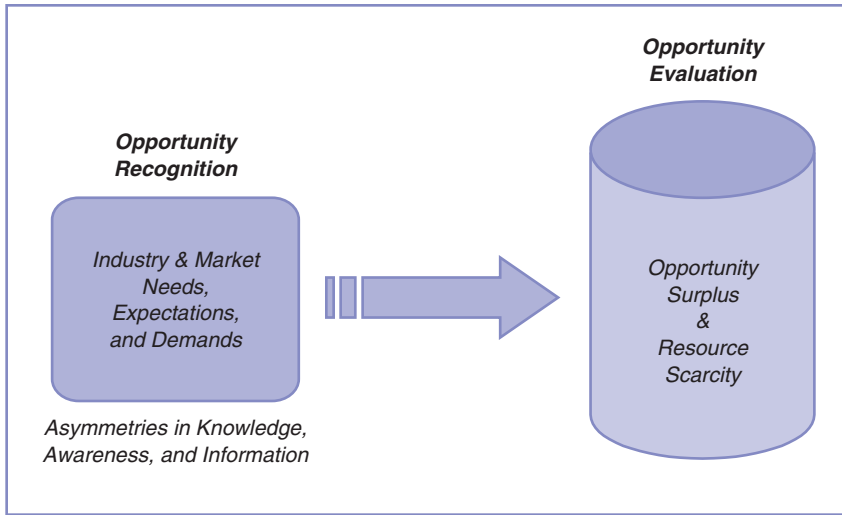
## Opportunity Evaluation: Will the Idea for the New Venture Work?

Once entrepreneurs have developed the idea(s) for the new ventures, they must begin the process of assessing whether or not the idea is in fact a viable business opportunity. Many new ventures have been launched around bad business ideas. An idea can seem sound in theory but in reality have poor marketplace potential. While failures can also be attributed to poor execution of the idea, it is important to assess feasibility as early as possible to avoid the much costlier effects of failed implementation. So how do entrepreneurs determine if an idea is an appropriate investment for their resources?

The U.S. Patent Office has granted some unusual patents in its history. Consider, for example, whether necessity really drove these inventions (Jones, 1991).

- A propeller-driven rocking chair
- An automatic spaghetti-spinning fork
- A power-operated pool cue stick
- A baby-patting machine
- An electronic snore depressor
- A parakeet diaper
- An alarm clock that squirts the sleeper's face

As you can see from these amusing examples, assessing an idea's potential to become a good business opportunity is absolutely necessary to avoid the allocation



**Figure 3.1** Opportunity Recognition to Opportunity Evaluation: The Assessment Process

of scarce resources, including the entrepreneur's time and effort. As we have seen in Chapter 2's discussion of opportunity identification, the process begins by determining the unique needs of the industry and marketplace, including what customers expect and demand that the new venture can provide. Many ideas and opportunities exist; however, resources are scarce, and this means that you must be very careful in your evaluation of business opportunities to be sure they can be supported by the knowledge and information you possess or can obtain fairly easily. Figure 3.1 illustrates the movement from opportunity identification to opportunity evaluation.

The evaluation process begins with some fundamental questions to help entrepreneurs assess the potential for the new venture to succeed. Evaluation of business opportunities should be conducted not just by the entrepreneur but also by as many stakeholders in the new venture as possible: potential customers or clients, employees, advisers, investors, and suppliers.

## Four Primary Areas for Assessment

There are many questions to ask during opportunity evaluation, and they can be classified according to four primary areas for exploration:

1. *The people behind the idea:* the background, talents, and experience of the entrepreneur and the management team, employees, and advisers. Even a great idea with high market potential requires an entrepreneur or team behind it that can effectively (and passionately) support and grow the idea. It is then much more likely to be successful. An entrepreneur's skills and talents might have led to the discovery of the idea, but does the entrepreneur have the competence to turn the idea into a business?

**64** ENTREPRENEURSHIP STRATEGY

2. *The resources* available to the entrepreneur and the management team, including the equity and debt sources of capital that are available and accessible, additional assistance from people with expertise needed by the firm, and the technology required to support the idea. What relationships can the entrepreneur or team rely on to acquire the necessary resources?

3. *The knowledge and information* possessed by the entrepreneur, including knowledge of the new venture concept, the industry, and market research. Moreover, what is not known that needs to be known for the new venture to be successful? Information about competitors? About customers' preferences? How will this information be obtained?

4. *The idea's ability to generate revenue.* How great is the potential to sell something that will generate actual revenues? One of the mistakes would-be entrepreneurs make is to assume that everyone will love the idea and that people will be standing in line to buy it, once the business opens. To what degree can the entrepreneur manage and contain the costs while maximizing returns?

These questions form the basis for the opportunity evaluation, and their answers will help the entrepreneur move forward to create strategies that ultimately support the viable business model.

### Review Questions

1. How do the four questions for assessing a business opportunity help entrepreneurs evaluate whether their business idea is viable?
2. Do you think entrepreneurs should proceed with an idea that has inherent weaknesses in any of these areas?

### The Innovator's Toolkit: Business Evaluation Scoring Technique (BEST)

The Business Evaluation Scoring Technique (BEST) was developed to help entrepreneurs evaluate a group of ideas before deciding which ones to pursue. The tool considers the various "windows of opportunity" related to new ventures. Answer the following questions by scoring them on a 1–5 scale: 1 = low and 5 = high.

1. Is the business really differentiated from other similar businesses?
2. Does the business have growth potential?
3. Will the business require capital? (Note: A low dollar requirement receives a higher score, while a high dollar requirement should receive a low score)
4. Can financing be secured?
5. Does the business suit the individual's entrepreneurial profile (e.g., mind-set, experience)?

<i>Total Score</i>	<i>Description</i>	<i>Action</i>
20–25	Excellent prospects	Must try
15–19	Very good prospects	Should try
11–14	Reasonable prospects	Try if nothing else is available
10 and under	Poor prospects	Avoid this loser

SOURCE: Edward Williams, [http://www.entrepreneurialprocess.com/new\\_site/best\\_technique.htm](http://www.entrepreneurialprocess.com/new_site/best_technique.htm). Reprinted with permission.

## Assessing the Feasibility of the New Venture Idea

Evaluating a new venture idea involves testing its *feasibility*, the extent to which the idea is a viable and realistic business opportunity. One of the first steps required in assessing the feasibility of an idea is to become aware of forces and factors in the internal and external environment that directly influence the new venture opportunity.

Factors internal to the venture include:

- *The knowledge, skills, and abilities* of the entrepreneur, the management team members, employees, and advisers
- *The resources available* to the entrepreneur, including people, financial resources, and technologies that can be acquired for the launch and growth of the opportunity

Factors external to the new venture include:

- *The industry*: competitors, structure of the industry, barriers to entry, and trends that affect businesses in the sector in which the new venture intends to locate
- *The market*: knowledge of the preferences, values, and buying behavior of the target market, including demographic and psychographic information necessary to appropriately position, promote, and price the products and services
- *Social norms, values, and trends* surrounding the new venture idea. Is it a fad? Is there an increasing need for or awareness of the product or service? Are there ethical concerns about the product, service, or its effects? Realize that a product or service (and any of its components) may be legal but unethical. The social environment of a new venture often involves the perceptions—not necessarily the reality—of the opportunity in the minds of customers and citizens.
- *Legal and regulatory forces* that could affect the business operations, including laws, policies, procedures, and regulations pertinent to the industry or municipality in which the new venture is located

Conducting an environmental feasibility analysis will help the entrepreneur prepare a strategic plan—the topic of Chapter 4.

In the next section, we examine the major questions to ask that will help you determine the feasibility of your business opportunity. A model that can guide the entrepreneur through the opportunity evaluation process is presented.

## Fourteen Questions to Ask Every Time

To evaluate opportunities, Allis (2003) has developed a set of questions for entrepreneurs.<sup>1</sup> The answers are helpful as entrepreneurs prepare to conduct a comprehensive feasibility analysis and to develop subsequent strategies for the emerging venture.

1. What is the need you fill or problem you solve? (value proposition)
2. To whom are you selling? (target market)
3. How could you make money? (revenue model)
4. How will you differentiate your company from what is already out there? (unique selling proposition)
5. What are the barriers to entry?
6. How many competitors do you have and of what quality are they? (competitive analysis)
7. How big is your market in dollars? (market size)
8. How fast is the market growing or shrinking? (market growth)
9. What percent of the market do you believe you could gain? (market share)
10. What type of company would this be? (lifestyle or high growth potential, sole proprietorship or corporation)
11. How much would it cost to get started? (start-up costs)
12. Do you plan to use debt capital or raise investment? If so, how much and what type? (investment needs)
13. Do you plan to sell your company or go public (list the company on the stock markets) one day? (exit strategy)
14. If you take on investment, how much money do you think your investors will get back in return? (return on investment)

### Strategic Reflection Point

#### ALUO to Evaluate the New Venture Idea

ALUO (Advantages, Limitations, Uniqueness, and Opportunity) is a useful tool that enables the entrepreneur to examine the advantages and limitations of an idea. Most entrepreneurs do this, but ALUO is helpful because it also asks you to consider what is unique about the idea and what opportunity emerges from the advantages, limitations, and uniqueness of the idea (Gundry & LaMantia, 2001).

**A:** What are the advantages of the idea? How does it build on or extend what is already available in the market?

**L:** What are the limitations of the product or service? This may be hard for the entrepreneur to assess realistically (watch out for idea infatuation!). You may want to ask others for their opinions on this. What elements of your idea might not work as well as predicted? What flaws might exist?

**U:** What is unique about the idea? What can't be substituted by something already available in the marketplace? Is your idea easily imitated by others? How can the entrepreneur make it difficult for others to copy? If the product or service is not unique, are there ancillary products or services that could be packaged to maintain uniqueness?

**O:** What opportunities emerge from the unique features and advantages (or even the limitations, as you consider ways these could be minimized)?

## The Feasibility Analysis: Beginning the Evaluation Process

### The KIC: Knowledge of Industry Checklist

While it may be tempting to take the leap into writing a business plan as soon as you develop and refine your business idea or opportunity, this can prove to be a serious mistake. Many would-be entrepreneurs underestimate their competitors (both in number and in capability) and therefore develop entrepreneurship strategies that have no likelihood of success. Don't fall into that trap—idea infatuation is one of the strongest predictors of business failure because infatuated entrepreneurs ignore or discount objective industry and market data that even slightly questions their idea. To increase the odds of success and help you identify potential flaws and areas for improvement a priori, start with the KIC: Knowledge of Industry Checklist. A complete industrial analysis usually includes a review of an industry's recent performance, its current status, and the outlook for the future. Many analyses include a combination of text and statistical data. Some of the points entrepreneurs consider in this analysis are given below.

### Current Industry Analysis

- Describe the industry as specifically as possible. Some business ideas fall into more than one industrial classification.
- What are the current trends in the industry?
- What is the current size of the industry? Is it dominated by large players? Are there a significant number of small to medium-size enterprises in the industry?
- Where is the industry located? Is it local, regional, national, or global?
- What is the average sales and profitability for this industry?



**The Innovator's Toolkit: Give Me Five**

When you have gathered preliminary information about your industry, try this challenge to push thinking forward with respect to this industry. Your responses to this exercise will help you formulate your competitive strategy for successful industry entry and growth (Gundry & LaMantia, 2001).

- *Give Me Five* things you have observed as a consumer or employee of this industry.
- *Give Me Five* things businesses in this industry should be thinking about right now.
- *Give Me Five* things customers of this industry would tell you if you asked them.
- *Give Me Five* actions or behaviors businesses in this industry should take within the next six months to two years to remain competitive.
- *Give Me Five* ideas that businesses in this industry haven't even thought about yet.

### Competitor Analysis

- Obtain basic information on the competitors you have identified. Who are the direct competitors of the new venture?
- Where are the competitors located? Be careful not to assume that a competitor located across the country—or the world—is not a direct competitor. Many firms conduct business on-line, and a remote competitor may prove to be a formidable one if it has a strong on-line presence.
- What are the advantages and disadvantages of the competitors?
- What features of their products or services are similar to yours?
- How are your products or services distinctive from those of your competitors? This is a key part of the competitive analysis.

The following worksheet will help you gather data about your competitors. Use additional worksheets to identify more competitors. You will use the information in this worksheet, Table 3.1, to help you develop your competitive strategy in Chapter 4.

### Sources of Information for the Industry and Competitor Analysis

There are many sources of industry analysis: investment firms, business and trade periodicals, trade associations, and government agencies. To conduct a thorough industry analysis, include a variety of sources. Appendix 3.1 contains some recommended sources for your research, including Internet and print sources. As you conduct your research, don't neglect to record your own personal observations: Visit competitors in a nondisruptive manner. What do you notice? What could be improved? How is the product or service used? Create the experience of being a customer of this business and industry.

**Table 3.1** Worksheet for Competitor Analysis

<i>Competitor Identification</i>	<i>Business Name</i> _____	<i>Business Name</i> _____	<i>Business Name</i> _____	<i>Business Name</i> _____
Key product or service				
Location(s)				
Local, regional, national or global?				
Primary features of product or service				
Advantages of product or service				
Disadvantages of product or service				
Target market				
Market share				
Pricing				

*(Continued)*

## 70 ENTREPRENEURSHIP STRATEGY

Table 3.1 (Continued)

<i>Competitor Identification</i>	<i>Business Name</i> _____	<i>Business Name</i> _____	<i>Business Name</i> _____	<i>Business Name</i> _____
Promotional activities				
Knowledge, skills, and abilities of key staff				
Resources				
Image				
Culture of the business (norms and values)				
Financial condition				
How is your venture distinctive from this competitor?				

## Failures and Foibles

### Knowing What's *Not* a Good Opportunity

In 2005, for the fourth year in a row, Stew Leonard's, a family-owned fresh food store with locations in Norwalk and Danbury, Connecticut, and Yonkers, New York, has been named to *Fortune* magazine's "100 Best Companies to Work For" list. The company placed 29 on the 2005 list, when for the first time, companies were also listed by their size—large, mid-size, and small.

Stew Leonard's, a small company with less than 2,000 employees, is ranked 15 when compared to other small companies that also made the list. Stew Leonard's was dubbed the "Disneyland of Dairy Stores" by the *New York Times* because of it had its own milk processing plant and costumed characters, scheduled entertainment, a petting zoo, and animatronics were in its stores. The company has received worldwide acclaim for excellence in customer service and quality and is featured in two of management expert Tom Peters's books: *A Passion for Excellence* and *Thriving on Chaos*. In 1992, Stew Leonard's earned an entry into *The Guinness Book of World Records* for having "the greatest sales per unit area of any single food store in the United States."

Tom Leonard, son of the founder, was walking around the store one day when he was approached by a man who asked if the store carried shaving cream. Tom replied that it did not. The man went on to explain that shaving cream was one of the hottest items in grocery stores, and Stew Leonard's ought to get some. Tom admitted that was an interesting fact and took out his day-timer to make a note of it. The customer interrupted and said, "Tom, today is your lucky day. I sell shaving cream." Tom got excited and placed the order right there. "And the first week," he notes, the shaving cream "sold very well."

However, sales slid, and within a few weeks, Tom learned that the shaving cream was not moving, and the stores were stuck with trailer loads of the product. Tom realized that shaving cream was unlike most of the products sold at Stew Leonard's Dairy: It was not perishable. Customers had purchased the shaving cream during the first week or two, but then they were set for a few months and didn't need any more.

But Tom was not discouraged: "When we have a situation such as this, we know what to do." So he had the advertising department draw up a sign that said, "Shaving Cream: 99 cents a can. Buy 1, get 2 free." Tom recalls that he then learned the biggest marketing lesson of his life:

"If the customers don't want one, they surely don't want THREE! It took us months to get rid of the stuff."

Tom's story is an important one because it reminds entrepreneurs that what might appear to be a great opportunity just might not be a good fit with your business.

SOURCE: <http://www.stewleonards.com>

## From KIC to OOPs: The Opportunity Organizational Proposal

In the first section of this chapter, we examined the key factors that are part of the opportunity assessment. A comprehensive feasibility study is conducted to help the entrepreneur determine whether the opportunity can lead to the emergence and growth of a successful organization. The Opportunity Organizational Proposal is composed of five major sections. You can use the detailed outline below as you analyze the potential of a business opportunity and decide whether or not to move ahead and create the new organization. The worksheets you will need for investigating financial feasibility are found in Appendix 3.1 at the end of this chapter.

## Outline for the Opportunity Organizational Proposal: Feasibility Analysis

### *Description of Your Business*

*What business are you really in?* Describe your product or service in the most concise way you can, and think beyond the characteristics of the product or service to the *experience* that you hope the customer receives from buying the product or service.

### *The Product or Service*

- *Describe what you are selling and how it will benefit your customers.* Explain how your product or service is different from the competition. Answer the question, “Why will people buy from me?” (your product/service concept, benefits, and customer profile). It is important that you can concisely and accurately describe your product or service in terms that are relevant to your customer and that the customer can understand. The ability to describe your product or service will be a critical factor in the success of your marketing and advertising. What are the things about your product or service that are important to your customer? What words immediately create an image of your business?

- *What are the unique characteristics of your product or service?* What are the unique features of the product or service? How do these features meet your customers’ needs or preferences? What are the benefits of this product or service compared to the competition? Describe your product or service very simply, and use photos or drawings to illustrate how it works.

- *What are the specific shortcomings of the product or service?* Can it become obsolete soon? Is it perishable, is it difficult to use or install, or are there legal restrictions? An honest assessment of your product or service is extremely important during this analysis. Entrepreneurs do themselves no favor by being in denial or failing to see the disadvantages *before* going into business. Noting them now will help you prepare solutions or ways to minimize these issues.

- *What is your product’s stage of development?* Is the product still in the idea stage, or is there a model or working prototype available? Have any samples been manufactured? If it is still in the idea or prototype stage, what is the time frame for getting it ready for production.

- *Research any legal restrictions and rights.* List any patents, copyrights, trademarks, or licenses that apply to your product or service. If you are entering into a franchise agreement, partnerships, distributorships, and so on, these should be discussed in this section. Seek the assistance of patent attorneys or intellectual copyright specialists for assistance. Also, list the government regulations with which you must comply, including any government approvals required, and research zoning restrictions carefully. If you will be home based and your clients will be coming to your house, will your neighborhood’s zoning restrictions be an issue?

- *What are the insurance requirements?* Research the liability of your product or service, and consult an insurance specialist to be sure you are protected adequately. This will depend on the nature of your business. A landscape design firm is in a different liability situation than a children's gymnastics and fitness center, for example. If you have employees, you will need insurance to protect them from harm also, along with any insurance benefits you want to provide your staff.
- *Estimate production or service delivery costs.* Will you be producing or subcontracting out the manufacturing or delivery of your product or service? List all the costs, including labor, supplies, shipping, repairs, and so on.

### *The Industry and Market*

- *Describe the current industry.* Determine the trends present in the industry, the size of the industry, the location, and the average sales and profitability of the industry. Use the KIC (Knowledge of Industry Checklist) presented earlier in the chapter for this section of the feasibility analysis.
- *What is the market potential for your idea?* Describe the market for your product or service as specifically as possible. Is the industry in a period of growth, stability, or decline? Can you predict the demand for your product or service over the next six months to two years? Would-be entrepreneurs should interview business owners, managers, or other insiders in the industry to learn about trends and market potential for the industry.
- *What is the impact of technology on the industry and market?* What is the level of technology in use in the industry today? How available or accessible is that technology to the entrepreneur? How can you remain up-to-date with technological changes in this industry? What resources will be required to access the technology at start-up? During the growth stage several months ahead?
- *What economic and legal/regulatory factors affect this industry?* Are there global businesses in this industry and market? How will these impact your operations or customers? What laws and regulations govern the industry, and what information do you need to be sure you operate within legal guidelines?
- *What ethical values are associated with this industry?* Are there any ethical guidelines for the industry? How can you be proactive and develop a set of ethical norms and behaviors in this business? Are there concerns perceived by customers or others in the industry about ethical behavior?
- *Who are the primary competitors?* Where are they located, and what are the unique features of their products or services? What are the advantages and disadvantages of these competitors, and how can your business be distinctive? Use the information from your competitor analysis worksheet presented earlier in this chapter.
- *Who are your customers or clients?* You will need demographic information, including statistics on where they live, income, educational level, number of children, and so on—whatever factors are relevant to your business opportunity. Searching by zip code through library databases (see the earlier section on sources in this chapter) will be helpful.

## 74 ENTREPRENEURSHIP STRATEGY

You will also need psychographic information, including your customers' preferences, values, attitudes, buying behavior, and so on. You can also use primary research, such as conducting surveys and interviews with potential customers to find out what they think about your ideas and whether or not they would buy the product or service.

Use creative approaches to learn all you can about your potential customers. Don't just listen to their words (or written responses on a survey). Try to observe their behavior—it often tells you much more about what they really think about your product or service. For example, if you are developing a new food, observe how much people eat (or drink) of the samples—not just what they say about them. If you are going to be offering a new consulting service, ask a small sample of potential clients to use the service (or a component of the service) and find out what problems the service solved (or didn't solve) for them. Remember Scott Cook's employees at Intuit who observed how the customers used Quicken as they were developing the product.

- *How will you accomplish market penetration?* How will you reach your target customers? What forms of distribution, advertising, and promotion will you use? How will your potential customers become aware of your business?

### *The Management*

- *What is your management and technical experience?* Briefly describe your management/technical skills related to this product or service. Who will you also have on your management team? Will you develop a board of advisers, including industry experts, accountants, or lawyers?

- *Consider the three crucial areas of experience and expertise:*

1. **Marketing strategies:** This means knowing what kind of product or service to sell, how to target and reach your customers, and how to sell your product or service at a price that maximizes your profits.
2. **Technical ability:** You must be able to get the work done and done right, so you will have satisfied customers.
3. **Financial knowledge:** While you do not necessarily have to be a financial wizard, you do need to know how to plan and control your business's cash flow, how to raise or borrow the money you will need to start your business, and how to get through tight periods without being caught short of cash. A certain amount of financial sophistication is becoming more and more important in today's increasingly complex financial world, even for the small business owner. Being able to focus on the bottom line and pay attention to the numbers is as essential as the ability to price your products and services, manage your cash flow, and make sure you collect payment for the work you do.

### *The Financing: Estimating the Necessary Funds to Launch the New Venture*

- *How much seed money do you need?* Entrepreneurs must estimate the costs of the new venture for at least the first several months. Every business is different and

has its own specific cash needs at different stages of development, so there is no universal method for estimating your start-up costs. Some businesses can be started on a shoestring budget whereas others may require considerable investment in inventory or equipment. It is vitally important to know that you will have enough money to launch your business venture.

- *What expenses will you have during the start-up phase?* Some of these expenses will be one-time costs such as the fee for incorporating your business or the price of a sign for your building. Some will be ongoing, such as the cost of utilities, inventory, insurance, and so on. While identifying these costs, decide whether they are essential or optional. A realistic start-up budget should include only those things that are necessary to start the business. These essential expenses can then be divided into two separate categories: fixed and variable. Fixed expenses include rent, utilities, administrative costs, and insurance costs. Variable expenses include inventory, shipping and packaging costs, sales commissions, and other costs associated with the direct sale of a product or service.

- *Allow for surprise expenses.* Even with the best of research, opening a new business has a way of costing more than you anticipate. There are two ways to make allowances for such expenses. The first is to add a little padding to each item in the budget. The problem with that approach, however, is that it destroys the accuracy of your carefully wrought plan. The second approach is to add a separate line item, which we call contingencies, to account for the unforeseeable.

Talk to others who have started similar businesses to get a good idea of how much to allow for contingencies. If you cannot get good information, we recommend that contingencies should equal at least 20 percent of the total of all other start-up expenses.

- *Use a worksheet that lists all the various categories of costs.* Appendix 3.2 at the end of this chapter contains a worksheet you can use to estimate your initial expenses (both one-time and ongoing). When listing your start-up costs, be sure to explain your research and how you arrived at your forecasts of expenses. Give sources, amounts, and terms of proposed loans. Also explain in detail how much will be contributed by each investor and what percent ownership each will have. All this information can then be included within your business plan and presentation to your investors and lenders.

## Review Question

1. Discuss the risks an entrepreneur faces if he or she does not complete a feasibility analysis.

## Next Steps: Strategic Planning for the Emerging Venture

When the entrepreneur has completed the feasibility analysis, the next steps into business involve strategic planning for the new venture. In Chapter 4, we will examine how to develop a strategic plan and strategies for the launch of the business.



### Research in Practice: New Venture Capabilities

The results of a feasibility analysis can provide entrepreneurs with a much better understanding of the capabilities of the new venture. In the Panel Study of Entrepreneurial Dynamics,<sup>2</sup> 480 entrepreneurs reported how certain they were, on a scale of 1 (very low certainty) to 5 (very high certainty) that the new venture would be able to accomplish the following tasks and activities. The average response is given below:

Obtain raw materials:	1.4
Attract employees	2.3
Obtain start-up capital	2.6
Obtain working capital	2.8
Deal with distributors	2.9
Attract customers	4.0
Compete with other firms	3.5
Comply with regulators	4.0
Keep up with technological advances	3.3
Obtain a bank's help	2.2
Obtain venture capitalists' help	1.7

### Review Questions

1. Why do you think the entrepreneurs were fairly confident they would be able to attract customers (4.0) and comply with regulators (4.0)?
2. Why do you suppose they tended to be less certain they would be able to obtain a bank's help (2.2), venture capitalists' assistance (1.7), or raw materials (1.4)?
3. Does this suggest to you what entrepreneurs need to focus on as they prepare for the launch of the new venture?

### Summary of Chapter Objectives

1. Understand the role of opportunity evaluation in the entrepreneurship process
  - The evaluation process begins with some fundamental questions to help entrepreneurs assess the potential for the new venture to succeed.

- Four primary areas for assessment are: the *people* behind the idea (the entrepreneur and the management team); the *resources* available to carry out the idea; *knowledge and information* about the industry and market, including barriers to entry, location, competitors, social and economic trends, regulatory factors, target market, and market penetration; and the *ability to generate revenue*.
2. Learn methods for evaluation that can be used for the initial idea and subsequent opportunities in the life cycle of the new venture
    - Creative tools such as ALUO (Advantages, Limitations, Uniqueness, and Opportunity) can help entrepreneurs identify the key strategic points and differences surrounding their ideas for the business.
    - The KIC (Knowledge of Industry Checklist), including a comprehensive competitor analysis, is a useful guide for collecting and interpreting information about the industry.
    - “Give Me Five” is a creative tool that is helpful to understanding the experience that the product or service should provide to customers. It asks you to take the perspective of significant constituents to your business.
  3. Prepare the Opportunity Organizational Proposal (OOPs), which is based on a comprehensive analysis of the feasibility of the venture idea
    - The OOPs will help the entrepreneur evaluate the ability of the business idea to effectively solve the problem or fill the need for which it was intended, as well as the degree to which the idea can generate sufficient revenues to warrant the resources needed to bring the opportunity into action.
  4. Undertake the feasibility analysis by completing the five sections of the OOPs
    - Section I: Description of the Business, asks what business are you really in, and what experience does your product or service bring to the customer?
    - Section II: The Product or Service, asks you to delineate as specifically as possible the benefits of what you are selling to the customer. What are the unique features of the product or service? What are the shortcomings? What stage of development is the product or service in presently? Are there any legal restrictions, insurance requirements, or product delivery costs that are involved?
    - Section III: The Industry and Market, contains an analysis of current trends in the industry, and the complete KIC (with competitor analysis); the market potential for the opportunity, the impact of technology on the industry and market, economic and regulatory factors, ethical values associated with the industry, information on the customers, and market penetration.
    - Section IV: The Management, including the managerial and technical experience of the entrepreneur and any team members, including marketing, technical skills, and financial knowledge.
    - Section V: The Financing, in which you estimate your start-up costs, the expected annual sales forecast, cost of goods sold, operating expenses, gross profit, pricing and break-even points, and sources of start-up capital.

## CASE 3.1 Speaking of Strategy: Kate Spade

Kate and Andy Spade are the owners of a \$125 million business that designs fragrances, china, and other accessories. The business started in 1993 as a handbag company, when Kate—then an editor at *Mademoiselle* magazine, could not find the particular type of handbag she was looking for. Kate grew up in Kansas City, Missouri, and her fresh sense of style and singular personality reflect a keen sense of wit, propriety, and a no-nonsense approach to life. Kate has spent most of her professional career in the accessories business. In 1986, after she graduated college, she took a job at *Mademoiselle* magazine and was Senior Fashion Editor/Head of Accessories until she left in 1991. During her time at the magazine, Kate believed that the market lacked stylish, practical handbags. Not one to simply complain or settle for something less than what she desired, she began designing her own. Together with her partner and husband, Andy Spade, Kate identified a void in the market, combined their talents, took a risk, and designed six simple shapes that emphasized utility, color, and fabric. These six original designs continue to be the company's signature styles.

Kate did some sketches, investigated production costs, and created a line of classically shaped bags in satin-finished nylon, as well as interesting colors and fabrics. With their fingers crossed, Kate and Andy launched Kate Spade Handbags in January 1993.

In the early days of the company's growth, Kate and Andy realized they would need help to build the business. In late 1993, Pamela Bell joined Kate Spade to help locate sources of materials and produce the handbags. The following year, Elyce Arons, an old friend of Kate and Andy's from their college days at Arizona State University, came on board and was initially responsible for sales and public relations. Within a short period of time, a partnership was formed with Kate, Andy, Pamela,

and Elyce each contributing unique experience and strengths to the equation. Taking a modest, creative approach to design and marketing rather than risk being a flash in the fashion pan, the four partners, together with a collaborative team of people, continue to build a company based on vision, graciousness, and old-fashioned hard work.

In 1996, Kate was recognized by the Council of Fashion Designers of America (CFDA) for being America's new fashion talent in accessories, and in 1998, this organization once again honored her as best accessory designer of the year. In 1999, Kate was honored when her handbags were exhibited at the Cooper Hewitt Museum for the first national design triennial, celebrating American design excellence. That same year, she was recognized for her new home collection.

Kate Spade opened its first shop in 1996 in the Soho neighborhood of New York City. It quickly outgrew the space and moved around the corner in the fall of 1997. The store became a laboratory for different categories, from paper to travel. In 1998, Kate Spade opened in Boston; in 2000, in Chicago and San Francisco; and by 2004, in Atlanta, Houston, Charlotte, Dallas, and Boca Raton. Most recently, the company has expanded to locations in Las Vegas and Palo Alto, California, and outside the United States to Japan (four stores), Hong Kong (three stores), and the Philippines.

Appealing to a diverse group of women, the company's growth continues. "Kate Spade paper and social stationery" was introduced in 1998 and includes such items as personal organizers, address books, journals, illustrated note cards, and classic pencils and erasers. In November of 1999, Kate Spade introduced a much anticipated shoe collection incorporating her unique sense of style and sophisticated use of color. "Kate Spade glasses" was introduced in the spring of

2001, providing yet another natural extension of the refreshing and sophisticated Kate Spade aesthetic. The eye glasses collection features clean shapes, classic proportions and, naturally, an element of surprise. The line includes both sunglasses and ophthalmic frames exemplifying Kate's personal style. Kate Spade and Estée Lauder launched "Kate Spade beauty" with great success in the spring of 2002, with a signature fragrance based on the scent of a white floral bouquet. The most recent addition to the world of Kate Spade, "Kate Spade at home," was introduced in 2004. The home collection includes bedding, bath items, china, wallpaper, textiles, and other vibrant accessories for home.

As Kate Spade grows and evolves, a great deal of product development continues to occur within the company. Based on Kate's love of textiles, pattern, and strong geometric shapes, the company developed a signature, iconic design element inspired by the op art movement of the 1960s; this element has proved multifaceted and naturally developed into a new company mark and graphic art pattern. Various interpretations of the design were incorporated into the handbag, luggage, shoe, glasses, and paper collections and introduced as the "noel weave" collection in the fall of 2001. The company plans to incorporate this signature mark into its identity system and product collections going forward as a complement to the enduring "Kate Spade New York" logo.

In 2004, Kate was presented with three prestigious design awards: *House Beautiful's* Giants of Design award for tastemaker, *Bon Appetit's* American food and entertaining award for designer of the year, and *elle decor's* elle decor international design award for bedding. The first

Kate Spade music CD was issues recently: "the eight songs," written and recorded exclusively for Kate Spade by Beaumont, a modern pop band from the United Kingdom. It is a tribute to 1960s cocktail music with a jolt of modern glamour. Beaumont captures the sparkle and kick of Kate Spade in an unexpected and vibrant style.

The history and success of Kate Spade rests on the ability of Kate and Andy to identify and evaluate the right opportunities for their business. Their advice for entrepreneurs evaluating new opportunities is to ask if they really understand the opportunity and if it fits in with what they do extraordinarily well in the business. Even if the idea seems glamorous or is interesting, it may not be a feasible business opportunity. Andy explains, "If we do something interesting that doesn't sell, we don't perceive that as a success. We don't go back and tell people that the customers 'just didn't get it.'"

SOURCES: J. Creswell, "You Can't Say the Customer Doesn't Get It," *Fortune*, November 15, 2004, p. 196; R. Lieber, *Upstart Start-ups* (New York: Broadway Books, 1998); [www.KateSpade.com](http://www.KateSpade.com).

## Discussion Questions

1. How did Kate Spade determine if her idea was in fact a good business opportunity?
2. What criteria do you think Kate and Andy Spade use to decide whether or not to expand their accessories into other product lines and markets?
3. Why do you think Kate Spade has been so successful and distinctive in the extremely competitive fashion industry?



## CASE 3.2 Andy Szatko: A Grassroots Approach to Entrepreneurship

### Grassroots Landscaping, Inc.

During his freshman year at the University of Nebraska-Lincoln in the spring of 2000, Andy Szatko, who was majoring in horticulture, founded *Grassroots Landscaping* (now *Premier Landscape Construction*). When he told people that he wanted to start a landscaping business, the reaction was that starting a business at 19 years old is a bad idea, and at the very least, he should wait until he finished college. Andy Szatko did not listen to that advice. He started the business with a 1989 Ford truck and a few hand tools. His first jobs came from family and friends, and while he worked on these jobs, neighbors would stop by to see the kind of work he was doing. He told them about himself and his ambitions to create a successful landscaping company. Through word of mouth, his business grew quickly, and two years later, he purchased a new truck, which enables him to haul and carry more material. He also hired one full-time employee to help him stay organized. Andy contracted with his father, a carpenter, to do woodwork and build arbors for clients.

*Grassroots Landscaping* incorporated in late 2003. Andy notes, “We are now legally *Grassroots Landscaping, Inc.* That was pretty exciting stuff . . . moving more into a formal company. I did that because, in the past year, the company has been just me, I’ve been doing the work. A lot of the stuff comes from my head. In order to make it its own separate identity, I went ahead and incorporated it. That was a great first step.”

“I hire two full-time people during the season. I’ve been doing general landscape contracting, planting plants, and retaining walls. In the past couple of years, I’ve put a lot of effort into lawn maintenance such as mowing, fertilizing, and clean-up during the spring and fall. Just this past year—I didn’t really advertise it this year, but it’s going to be a big push for me during this

next year—we started to offer custom carpentry work. The reason I’m doing that . . . my dad is retiring from the Corps of Engineers and throughout his life, he’s always built custom carpentry.

In my parent’s home, growing up, [my dad] always built every single piece of furniture in our house. He has built everything, so I asked him if he wanted to join ranks with me and start offering custom carpentry. We’re going to be building bridges, arbors, Adirondack chairs, benches, . . . pretty much anything that a client wants made of wood, we would incorporate into the landscaping. It’s really exciting. I’m finding right now that there’s quite a bit of demand for that out there. So we’re really excited about pushing that service this upcoming year. [My dad] knows everything about it. He does quality work.”

In the world of landscaping, much of what Andy sells is the ability to create a design or image a client tells him about: “For one of the jobs we did this past year, a client of mine came to me and said: ‘I have this picture of an arbor from a Web site. I really like it, but I don’t have any dimensions or anything. Could you build it for me, or something like it?’ I gave the picture to my dad, and from just a picture from the Internet, he was able to come up with the measurements and the style of wood, exactly as the picture showed it. The clients were ecstatic about it. It turned out to be a really good project. So we can take anything from pictures, to just a rough sketch, and be able to transform it into what the people want for their landscape.”

Andy reports that he hadn’t actually thought about starting his own company. When he was 16 years old, he worked at a local nursery, actually part of a regional nursery and landscape center. He worked in the nursery selling plants, unloading trucks, and doing general labor at the store. He was there for about two-and-a-half years and left to attend college.

He began to enjoy working outside, working with plants, and seeing different plants. Andy explains, “I got a kick out of it, but I never thought of doing anything with it. My whole life, ever since I was seven years old, I wanted to go into meteorology. I love thunderstorms. I love going outside during thunderstorms and watching lightning. I’ve even gone to chase a few tornadoes, but I never was too successful in actually seeing one.

“When I got to college, I started off studying meteorology. During my freshman year, I started looking at the program and some of the requirements. The classes that were required really weren’t interesting to me. Without having an actual degree, you can still be a storm spotter, meaning if a storm’s coming, you get activated and you report in as far as storm spotting, or chasing, and that’s more or less what I like to do—to be outside working. So I came to the conclusion shortly after school started that I didn’t want to be behind a radar screen in an office.

Working at the nursery, I really liked landscaping and plants in general. So I switched over to the horticulture and landscaping degree, figuring I could do the weather thing kind of as a hobby and concentrate on landscaping. And having worked for a landscaping company before, I kind of saw how things should be run and how they could be better.

During the spring semester of my freshman year, I started thinking maybe I can start talking to family and friends—just small-scale side projects. So I went and got some hand tools, and I got a new truck so I could haul around materials, and that spring, I went out and started doing it more or less as a side project while still working at the nursery. But I found out that I could invest a lot more time into the company and make more money and do more things I like to do. So it kind of just evolved slowly and then my freshman year, it just kind of kicked into gear and went from there.”

How did Andy evaluate whether his idea to start the landscaping company was in fact a good business opportunity?

Andy recalls, “Omaha is the largest city in Nebraska. When I would drive around and look at all the new housing developments that were starting, in the back of my mind, I was thinking about the possibilities. I also saw a lot of older landscapes that were overrun. Also, having worked at the nursery, I saw all the people that would come in and buy these plants and have questions about what plants they should choose. So I didn’t do any formal research, but I still would think in the back of my head that the industry was very large and growing. I thought there’s got to be a way I could make it work. So, without formal research, I just jumped into it. But I was just thinking along the way, it’s a big industry, and there’s always work: Grass always needs to be cut, trees need to be trimmed, plants need to be replaced . . . it’s an ongoing industry. There’s never really an end to it.”

### **Building the Business: From the Idea to Formal System Development**

“I knew I would need something to start billing customers with and a way to track what was going on. I came up with a really rough Excel spreadsheet where I laid out materials, labor, a description of what the job was, and an estimate of the price. So, I started off getting the forms all ready to go. Having never taken a business course in my life, I was winging it—thinking about what should go in there. Those were pretty good for the first year since we did mostly small-scale landscaping jobs.

“I also had to go out and purchase tools and equipment. I didn’t need a whole lot of tools to start out with because they were smaller jobs. So I just went out and got a several hand tools, and purchased a 1989 Ford F150—found a good deal and talked my parents into purchasing it for me. My car at the time was a Honda Accord. I convinced them that the Accord wouldn’t last a lot longer . . . I finally convinced them to help me out to get the truck, and that was the biggest feat right there—to be able to get the truck.



## 82 ENTREPRENEURSHIP STRATEGY

Because my dad builds all kinds of things, he had a lot of tools and equipment that I would borrow . . . So those are the initial things I did to set up the company. As far as finding jobs, they really came pretty evenly because family members would give me the chance to do a little something to their house. Then, often people in the neighborhood would ask me who I was.”

Word of mouth helped Andy create awareness of Grassroots Landscaping. He admits he never did any advertising for the first three years of the company. It was all word of mouth. And as he read stories about entrepreneurs in magazines, he learned how important referrals from satisfied clients can be.

Did his age affect customers’ perceptions? Andy replies, “Being young and trying to run your own company is pretty hard. A lot of people get the idea that young kids aren’t reliable and try to do things the easy way. So when I was first starting out, I had people who would literally sit down and talk to me about how impressed they were that I was so young and was actually taking the effort and the time to put together a company and do the sales and estimating and all the work that went with it. By virtue of my age, I landed a couple of jobs in the first couple years . . . just because I was young and ambitious.”

### On Being an Entrepreneur and a Student

“Starting a business when you’re a student is really hard. For me, I think I made it harder on myself. Having to pay the bills, I ended up staying away from home. Actually, the school (Nebraska) is in Lincoln, which is about an hour away from Omaha where I based the company. So I’m doing work in Omaha, my family’s up in Omaha, my tools are up in Omaha, and my fiancée’s up in Omaha, and I’m in Lincoln trying to sell and put things together and trying to go to school at the same time.

“When I first started, after that freshman year, since things went pretty good that summer,

I decided to go to school in Omaha at night at [the University of Nebraska, Omaha]. So I took a year and went to school here in Omaha so I could work on the business and develop it up here. The horticulture program has a two-year program at Omaha and then you have to go down to Lincoln to finish up the degree. So I took that second year in Omaha and worked on the company and was able to be closer to everything I was doing. That really helped to give me an even better start to the company. I was able to spend more time because I wasn’t driving back and forth from Omaha to Lincoln.

“But, starting a company is really hard. You have to separate your time from your work. You can’t expect not to put time into a company if you really want to build it up. The nice thing is that this was during my busy season, so this was time when I wasn’t in school. In the winter, people are always asking, are you doing snow removal? What are you doing? And I would just say: ‘No, I’m focusing on school.’

“When I was at Omaha, my horticulture professor helped me tremendously just because he was a great guy to talk with and get some ideas from. [My professor] also hired me and one other guy who was in my class—he also runs his own landscaping company and was starting it at the same time as I was. So we were talking to him about retaining walls, and it turns out he needed a large series of retaining walls at his home. So he gave us the opportunity to build all those walls—estimate it and do the work. It was an amazing opportunity to develop a relationship with someone well-known in the field and to do such a large project.”

Andy advises would-be student entrepreneurs to be sure to take advantage of any resources available to students in their colleges and universities, especially if there is an entrepreneurship department or center. Andy notes that these academic resources offer a tremendous opportunity to learn and teach yourself—and they have people to help you to build the company you want to build.

“After I went to the Entrepreneurship Center, they were offering to look over my business plan and give me tips and suggestions about what to do. Just being able to talk to someone about payroll is helpful,” Andy says.

## Greatest Challenge of Entrepreneurship

Andy reports that the biggest challenge for him was in saying no. “That was my biggest thing—I wanted to please everyone who called me, that I was working for, and so I would bend over backward for a client and try to do everything I could for them. When I did that, eventually in the second or third year I was working, I found that doing that overextended what I was capable of doing. Then I started to see flaws, or to think of things I could have done better if I hadn’t been so stretched for time. So, I’ve learned a really valuable lesson in the fact that you’re not going to please everybody. You’re not going to be able to take on all the work that comes your way. You have to be able to control the growth so that your quality doesn’t dip, but you’re still able to grow the company at a good rate.

“I’ve made quite a few little mistakes involving clients. Just this past year, I didn’t have a contract that really spelled everything out for a client. I had talked to them about the design and showed them all the different types of plants. . . . Everything was listed on there. We got the go-ahead, went in, and started doing the work. We had planted a few of the trees that were in the design. [The client] came home that day and said, ‘What are these trees doing here? We talked about not having them there.’ I said, ‘I don’t have anywhere in my notes about this.’ He was sure that we had talked about it and that we weren’t going to put those trees in. Because of that, I had to go back and dig up the trees I had just planted, take them, and eat the cost for those because I get most of my materials from a wholesale dealer, and I couldn’t just take them back after they’d been planted.

“So, I’ve learned that you need to have everything spelled out, you need to have that final check . . . Communication is key. That was a big mistake, but it was really a small one in the overall business. Because of it, I’m drafting new contracts and learned to do new things.

“Probably my biggest mistake—when I was growing, I didn’t say no, and I took on a lot of work, which, like I said, overextended me. I was doing too much just by myself, and it stressed the quality of my work at the time.”

## Grassroots Landscaping: Future Plans and Innovative Strategies

Andy plans to expand to include carpentry work. Despite the fact that a lot of his clients ask about snow removal services, he does not really care to do that. He would rather spend his time during the winter concentrating on sales, doing design work, talking with other companies, and giving contracts out. His ideas for expansion of the business include Christmas lighting design and installation. He has observed a demand for these types of services. How does Andy innovate in his business?

“As for innovation . . . right now I’m starting my own plant/landscaping database where, after I do a design for someone, I will print off pictures or descriptions of each plant that I installed on their landscape. I’m putting this all together by myself, so I’m going to have my own plant encyclopedia, I guess you could say. I give each client a binder so that they always have it, and they know what to do with the plants as they go along. I’ve never heard of anyone doing that. I think it’s a really neat idea because it shows that I’m putting that extra step, extra effort into my work—my designs—that people will appreciate.” It is clear that Andy provides his clients with much more than landscaping—he shares information with them and teaches them about the products in which they have invested.

This strategy is paying off for the business because Andy gets referrals from satisfied clients



## 84 ENTREPRENEURSHIP STRATEGY

who call him up and say, “Here’s an opportunity for you, what do you think?” It’s a position other entrepreneurs may envy, having opportunities given to you by your clients.

“It’s fun to take my wife or friends past jobs that I’ve done and get their reaction or their input. They say, you should think about doing this, or they’ll give me new ideas that I had never thought of. It’s really fun to take people by and talk about, hey—I just did that. It’s a real sense of pride that I get.”

What advice does Andy Szatko have for college students considering entrepreneurship?

“The first thing I would say to them is that they need to test themselves and see if it’s for them. Entrepreneurship isn’t for everybody. I questioned myself at first—trying to build a business and everything depends on you. It can be really stressful. Being able to test yourself to see if you’re willing to put in the hours, to be able to take the stress. It’s a lot of hard work, especially if you want to go that extra mile to create the really successful company that most entrepreneurs want to develop.

“Also, when you’re starting out and building your business, go to trade shows, go to conferences, get involved in organizations related to your industry—even not associated with your industry. Just having that visibility is priceless. I ended up getting involved with the local chamber of commerce, and I recently joined the Nebraska Nursery and Landscaping Association. Meeting these new people has just been great. They give you tips on what you should do. People give each other business. If you’re starting out and trying to build your business, go to trade shows, conferences, and any other organization with which you can get involved. Talk to other companies—see what they’re doing. Get

out there and talk to those people who are willing to help you. There are all kinds of sources I know of through [the University of Nebraska, Lincoln’s] Alumni Association, such as talking to people who have agreed to be mentors for me. It’s a great way to be able to talk to people and get advice, and develop your business from there. You want to get a broad range of advice and opinions.

“Finally, don’t get discouraged. It’s really easy to get discouraged—especially if things don’t take off right away. I’ve been discouraged a couple times—because you don’t have a good day or you don’t land a contract that you really wanted. But, that’s the name of the game—you just have to keep going and be confident in your abilities to build a successful company.”

## Discussion Questions

1. How did Andy Szatko evaluate the idea for Grassroots Landscaping?
2. Despite unfavorable reactions to his idea, Andy persisted in creating the business. How can entrepreneurs ascertain whether to go ahead in the face of negative feedback?
3. Andy describes one of his mistakes as the inability to say no. How can entrepreneurs guard against the temptation to expand too early or to take on business that may not be in the best interests of the company’s growth?

SOURCE: Case prepared with the assistance of Laurel Ofstein, who conducted the interview with Andy Szatko, winner of the Global Student Entrepreneur of the Year Award, Northern Plains Region, 2003. Printed with permission.

## Notes

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1. From Allis, R., *Zero to One Million*. Virante, Inc., www.zeromillion.com, copyright © 2003. Reprinted with permission.
2. Adapted from C. H. Matthews and S. E. Human, “The Economic and Community Context for Entrepreneurship,” in *Handbook of Entrepreneurial Dynamics: The Process of Business Creation*, edited by W. B. Gartner, K. G. Shaver, N. M. Carter, and P. D. Reynolds (Thousand Oaks, CA: Sage, 2004), Table 36.14, p. 424.

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## Appendix 3.1

# Sources for Industry and Market Research

### Industry and Market Resources

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Standard Industry Classification (SIC) and North American Industry Classification System (NAICS) manuals for your industry's classification. You need your SIC code to use certain references, such as the industry norms and business ratios reference books. Where to find a SIC/NAICS Code:

<http://www.census.gov/epcd/www/naicstab.htm>

Missouri Small Business Development Center: <http://www.missouribusiness.net/iag/tattooing.asp>

#### Databases\*

**ABI Inform Global:** ABI/INFORM Global is a business and management article database. ABI/INFORM provides in-depth coverage of business and economic conditions and a wide variety of other topics from more than 1,800 business and management publications. The *Wall Street Journal* is available full text within this database.

**Business & Industry Database:** Contains facts, figures, and key events for international public and private companies, industries, products, and markets for manufacturing and service industries. It covers all the primary business information sources from leading trade magazines, newsletters, and the general business press to international business dailies.

**Business Source Premier:** Business Source Premier is a business periodical database that includes both scholarly journals and business periodicals. Topics covered in this database include the following: management, economics, finance, international business, and much more.

**General Business File:** Use General Business File to find company profiles and Investext analyst reports. Use this database to analyze company performance, company activity, industry events, and industry trends. General Business File contains broker research reports, trade publications, journals, and company directory listings.

\*The database descriptions were provided by Kathleen Berger and Linda Wolf, Simmons School of Management Assistant Librarians.

**Industry Surveys from Standard & Poor's NetAdvantage:** Use this database to find industry ratios. This database provides comprehensive coverage of 51 major U.S. industries. Each survey contains an industry profile, key ratios and statistics, and a comparative company analysis.

**LexisNexis Academic:** LexisNexis Academic provides access to full-text information from national and regional newspapers, international news sources, business news journals, industry and market news sources, Securities and Exchange Commission filings, legal news sources, and much more.

**MarketLine:** MarketLine provides profiles of 10,000 companies and contains information on 2,000 industry profiles. MarketLine also contains 50 country profiles that give quick access to country data points, trends, and analysis.

**PROMT (Predicasts Overview of Markets and Technology):** Use this database to research companies, the products and technologies they produce, and the markets in which they compete. Includes summaries and full text from nearly 1,000 business and trade journals, industry newsletters, newspapers, market research studies, news releases, and investment and brokerage firm reports.

**TableBase:** Use TableBase to obtain statistical information. TableBase is the database that specializes exclusively in tabular data on companies, industries, products, and demographics. International in scope, it covers more than 90 industries.

Additional Databases: Reuters Business Insights, Plunketts Industry Almanacs, available in Business Source Premier.

## Print Sources

*Encyclopedia of American Industries*

*Encyclopedia of Emerging Industries*

## Internet Resources

Small Business Administration, [www.sbaonline.sba.gov](http://www.sbaonline.sba.gov)

<http://www.lib.duke.edu/reference/subjects/business/isi>: For emerging market reports, see also ISI Emerging Markets

Hoover's, an online resource for up-to-date, comprehensive company, industry, and market information: <http://www.hoovers.com/free/ind/dir.xhtml>

Internet Intelligence Index, <http://www.fuld.com/Tindex/I3.html>: Created by the Fuld & Company Library, this site provides "links to nearly 600 intelligence-related Internet sites, covering everything from macro-economic data to individual patent and stock quote information." Notice the sections on "Industry-Specific Internet Resources" and "International Internet Resources" further down the page. Fuld & Company offers management consulting in competitive intelligence.

Business.com: Covers more than 28 industries, from accounting to utilities. Business.com provides a directory of industry Web sites.

## Other References

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### Value Line Reports by Industry

Dun & Bradstreet's Industry Norms and Key Business Ratios: 10Ks, annual reports, prospectuses and other public company reports filed with the Securities and Exchange Commission. 10Ks are annual reports that include description of the industry in which the business is located, company performance, financial condition, product or service focus, strategy, and information about the company's management.

Thomas' Register of American Manufacturers

American Wholesalers and Distributors Directory

Wholesale & Retail Trade USA

Trade Associations and Research:

Encyclopedia of Associations—Print Source—HS17.E56 2003

Associations (Yahoo)—[http://dir.yahoo.com/Business\\_and\\_Economy/](http://dir.yahoo.com/Business_and_Economy/Organizations/Trade_Associations/)

[Organizations/Trade\\_Associations/](http://dir.yahoo.com/Business_and_Economy/Organizations/Trade_Associations/)

The Internet Public Library—Retail Trade—<http://www.ipl.org/div/aon/browse/bus41.72.00/>

Trade Shows: [www.expoguide.com](http://www.expoguide.com), [www.tsnn.com](http://www.tsnn.com), and [www.tscentral.com](http://www.tscentral.com).

Associations Online and Associations Database: Links to associations with Web sites. Two sites that are useful: [www.asaenet.org/gateway/GatewayHP.html](http://www.asaenet.org/gateway/GatewayHP.html) and [www.trainingforum.com/assoc.html](http://www.trainingforum.com/assoc.html)

Chambers of Commerce

Competitors' Web sites, brochures, ads, etc.

### Statistics/Demographics

Overview of U.S. Bureau of Labor Statistics by industry: <http://www.bls.gov/bls/industry.htm>

American Factfinder: <http://factfinder.census.gov/>

State & County Quick Facts: <http://quickfacts.census.gov>

*The Sourcebook of Zip Code Demographics*

*Generation X: Americans Born 1965 to 1976* (Ithaca, New York: The New Strategist Editors, 2004)

Entrepreneurship organizations, such as the National Organization for Women Business Owners, National Federation of Independent Businesses, and others  
Conduct surveys of potential customers and employees, or see if such surveys already exist in any of the above sources

### Business Plans

U.S. Small Business Administration Business Plan Basics, [http://www.sba.gov/starting\\_business/planning/basic.html](http://www.sba.gov/starting_business/planning/basic.html)

## Company and Industry Resources—Financial Information

### Databases (in addition to the ones previously described)

**Bloomberg Terminal:** The Bloomberg Terminal provides minute-by-minute financial, economic, and government information covering all market sectors. Data available from Bloomberg includes stock prices and financial summaries for every public company traded anywhere in the world; currency exchange rates; economic statistics such as GDP, GNP, CPI, and much more. The Bloomberg Terminal is stand-alone terminal and is available in the library only.

### Print Sources

**Annual Statement Studies:** comparative historical data and other sources of composite financial data by industry.

**Industry Norms and Key Business Ratios:** provides statistics on more than 800 lines of business.

*Entrepreneur*

*Fast Company*

*Forbes*

*Fortune*

*INC.*

*Wall Street Journal*

### Web Sites

**Company Web sites:** Company Web sites are a good source of financial information. Annual reports can be found on company Web sites, usually located under the investor relations section. Company Web sites also contain press releases that provide financial information. Example: <http://investor.colgate.com/>

**EDGAR SEC Filings:** The SEC Electronic Data Gathering, Analysis, and Retrieval system contains forms filed by companies and others that are required by law. In this database, you can search for company filings such as the Form 10-K. <http://www.sec.gov/edgar.shtml>

**Forbes.com:** The Forbes.com Web site provides access to business and financial news as well as company information and rankings. <http://www.forbes.com/>

**Fortune.com:** The Fortune.com Web site provides access to business and financial news as well as company information and rankings. <http://www.fortune.com/fortune/>

**Yahoo! Finance:** This Web site provides company stock information as well as company profiles, company news, key statistics, listings of competitors and industry information. <http://finance.yahoo.com/>

## Appendix 3.2

# Estimating Start-Up Expenses

### Start-Up Expenses

Enter your company name here

#### Notes on Preparation

**EXPENSES**—Begin by estimating expenses. What will it cost you to get your business up and running? The key to accuracy here is attention to detail. For each category of expense, draw up a list of everything you will need to purchase. This will include both tangible assets (for example, equipment, inventory) and services (for example, remodeling, insurance). Then determine where you might purchase these goods or services. Research more than one vendor, that is, comparison shop. Do not look at price alone; terms of payment, delivery, reliability, and service are also important.

**CONTINGENCIES**—Add a reserve for contingencies. Be sure to explain in your narrative how you decided on the amount you are putting into this reserve.

**WORKING CAPITAL**—You cannot open with an empty bank account. You need a cash cushion to meet expenses while the business gets going. Eventually you should do a 12-month cash flow projection. This is where you will work out your estimate of working capital needs. For now, either leave this line blank or put in your best rough guess. After you have done your cash flow, you can come back and enter the carefully researched figure.

**SOURCES**—Now that you have estimated how much capital will be needed to start, you should turn your attention to the top part of this worksheet. Enter the amounts you will put in yourself, how much will be injected by partners or investors, and how much will be supplied by borrowing.

**COLLATERAL**—If you will be using this plan to support a bank loan request, use the section near the bottom to show what assets are offered as collateral to secure the loan, and give your estimate of the value of these items. Be prepared to offer some proof of your estimates of collateral values.

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*Sources of Capital*


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**Owners' Investment (name and percent ownership)**

Your name and percent ownership	\$
Other investor	
Other investor	
Other investor	
<b>Total Investment</b>	<b>\$</b>

**Bank Loans**

Bank 1	\$
Bank 2	
Bank 3	
Bank 4	
<b>Total Bank Loans</b>	<b>\$</b>

**Other Loans**

Source 1	\$
Source 2	
<b>Total Other Loans</b>	<b>\$</b>

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*Start-Up Expenses*


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**Buildings/Real Estate**

Purchase	\$
Construction	
Remodeling	
Other	
<b>Total Buildings/Real Estate</b>	<b>\$</b>

**Leasehold Improvements**

Item 1	\$
Item 2	
Item 3	
Item 4	
<b>Total Leasehold Improvements</b>	<b>\$</b>

**Capital Equipment List**

Furniture	\$
Equipment	
Fixtures	
Machinery	
Other	
<b>Total Capital Equipment</b>	<b>\$</b>



## 92 ENTREPRENEURSHIP STRATEGY

**Location and Administrative Expenses**

Rental	\$
Utility deposits	
Legal and accounting fees	
Prepaid insurance	
Preopening salaries	
Other	

**Total Location and Administrative Expenses** **\$**

**Opening Inventory**

Category 1	\$
Category 2	
Category 3	
Category 4	
Category 5	

**Total Inventory** **\$**

**Advertising and Promotional Expenses**

Advertising	\$
Signage	
Printing	
Travel/entertainment	
Other/additional categories	

**Total Advertising/Promotional Expenses** **\$**

**Other Expenses**

Other expense 1	\$
Other expense 2	

**Total Other Expenses** **\$**

**Reserve for Contingencies** **\$**

**Working Capital** **\$**

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*Summary Statement*

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**Sources of Capital**

Owners' and other investments	\$
Bank loans	
Other loans	

**Total Source of Funds** **\$**

**Start-Up Expenses**

Buildings/real estate	\$
Leasehold improvements	
Capital equipment	
Location/administration expenses	

Opening inventory	
Advertising/promotional expenses	
Other expenses	
Contingency fund	
Working capital	
<b>Total Start-Up Expenses</b>	<b>\$</b>

### Security and Collateral for Loan Proposal

<i>Collateral for Loans</i>	<i>Value</i>	<i>Description</i>
Real estate		
Other collateral		
Other collateral		
Other collateral		
<hr/>		
<i>Owners</i>		
<hr/>		
Your name here		
Other owner		
Other owner		
<hr/>		
<i>Loan Guarantors (other than owners)</i>		
<hr/>		
Loan guarantor 1		
Loan guarantor 2		
Loan guarantor 3		
<hr/>		

## Glossary of Terms Used in Determining Start-Up Expenses

The following terms are explained; some may apply to particular businesses and not to others.

**Legal, accounting, and professional services:** Professional fees are associated with registering your legal form of business, reviewing contracts and agreements, and preparing financial information for your business plan. This area also includes consultants and other professionals.

**Advertising and promotions:** This includes all promotional costs associated with opening your business.

**Deposits for utilities:** Advance payments required to obtain electric, gas, telephone, water, and sewer.

**Licenses and permits:** Fees for licenses, permits, and other requirements related to starting your business and making its operations legal.

**Prepaid insurance:** Advance payments required to obtain business insurance that protects the contents of your business against fire, theft, and other losses.

**Salary and wages:** Base pay plus overtime and bonuses, includes owner's draw on this line item. For purposes of estimating net profit, it is important that all costs, including owner's draw, be part of the projection.

**Payroll taxes:** Includes paid vacations, sick leave, health insurance, unemployment insurance, Medicare, and social security taxes. (Note: Usually 10 to 15 percent of gross payroll)

**Taxes, licenses, and permits:** Excise tax, inventory tax, real estate tax, sales tax, other nonpayroll taxes, and license or permit fees as applicable.

**Truck and vehicle:** Includes mileage, parking, tolls, and so on prior to opening the business.

**Travel:** Includes conference, hotel, meal, and transportation charges related to securing prospective distributors, suppliers, and customers.

**Tools and supplies:** Services, supplies, and tools purchased prior to opening, for use in the business.

**Machines and equipment:** Acquisition cost plus installation expense. If you plan to pay by installments, enter your down payment.

**Building improvements:** Includes costs of structural changes, repairs, painting, and decorating.

**Land and buildings:** Includes the down payment for lease, rent, or purchase and deposits required.

**Depreciation:** If property you acquire to use in your business has a useful life of more than one year, you generally cannot deduct the entire cost as a business expense in the year you acquire it. You must spread the cost over more than one tax year and deduct part of it each year.

**Starting inventory:** Includes acquisition cost plus transportation.

**Cash (working capital):** Amount of money you will need to maintain your business until the business generates enough sales to cover normal operating expenses.

**Other costs (specify):** Includes those start-up costs that may be unique to your business and do not have an account listed on the worksheet.

## The Expected Annual Revenue (Sales) Forecast for the First Year

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To help determine this, estimate:

- a. How many different customers do you anticipate serving in a 12-month period?
- b. How many times in a 12-month period will the average customer return to purchase something?

- c. How much will the average customer spend on each visit to your business?
- d. Multiply  $(a) \times (b) \times (c) =$  Estimated annual revenue (sales)
  1. Estimating your annual revenue (sales) will help you set a sales goal for your business and provide you with tools to manage your day-to-day operations.

By monitoring each of these factors on a daily, weekly, and monthly basis, you will know if your business is on target to meet its sales goal or if adjustments must be made to increase sales or decrease expenses.

#### Estimated Sales and Earnings (First and Second Year)

Forecasting sales and earnings is important for your financial success. It may take several years before your business begins to generate satisfactory profits, but your sales goal should be to break even (match sales with expenses) by the end of the first year and show modest profits. Do not include start-up expenses.

How many products and services do you expect to sell? What will your gross revenues be? What percentage of market share do you think you will reach in one year?

#### Cost of Goods Sold

Estimate the cost of sales for the sales found under revenue (sales). Include the cost of the labor used to produce the product or service (direct labor), materials used in the final product or service (direct material), and their transportation and handling costs. If you plan to manufacture goods, consider the cost of raw materials, labor, and delivery of goods. If you plan to sell retail or wholesale goods and services, consider markup, inventory costs, and freight. Refer to the Risk Management Association's studies for more information to help you compute these costs. See [www.rmahq.org](http://www.rmahq.org).

Total Revenue (Sales) minus Total Cost of Goods Sold = Gross Profit

**GROSS PROFIT – TOTAL EXPENSES = NET PROFIT**

- Pricing Your Product or Service

Calculate your sales breakeven point: \$\_\_\_\_\_

Sales Breakeven Point = Total Fixed Expenses / Gross Profit

Gross Profit = Difference between the selling price of a product or service and its variable cost/unit.

Example: Total fixed expenses of \$35,000 divided by gross profit of \$15 (assume that the selling price is \$100 and variable cost/unit is \$85). Your sales breakeven point would then be \$233,333 (the sale of 2,333 units).

The *Sales Breakeven Point* tells you the amount of sales that must be made to cover all the expenses identified. Once you've figured your breakeven point, you can begin making plans to achieve your sales goal. The "Total Revenue" that you will

need to breakeven at the end of the year is equal to your “Total Fixed Expenses” divided by your “Gross Profit”

- *An alternative way to determine if you can meet your business’s financial obligations:*
  - a. Project your average total monthly revenue (sales): \$ \_\_\_\_\_
  - b. Project your average total monthly expenses: \$ \_\_\_\_\_

Divide total revenue and total expenses by 12 to obtain a monthly average for each. Subtract the monthly expenses from the monthly revenue (sales) figure to obtain the monthly net profit or loss. This number will help you determine if your monthly revenue (sales) forecast is realistic in relationship to your monthly expenses.

- *Where will you find money to start your business?*

There are many sources of debt and equity available to entrepreneurs for start-up capital. Some of the most commonly used ones are listed below. There are many other sources you can research that may apply to your state, the ownership status (minority, women-owned, etc.), or the industry in which your business is classified.

Personal savings	\$ _____
Family and friends	\$ _____
Bank loan	\$ _____
Retirement account	\$ _____
Investor(s)	\$ _____
Partners	\$ _____
Credit cards	\$ _____
Other	\$ _____

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