

GLOBAL
EDITION



Essentials of Entrepreneurship and Small Business Management

NINTH EDITION

Norman M. Scarborough
Jeffrey R. Cornwall



Engage, Assess, Apply and Develop Employability Skills with MyLab Entrepreneurship

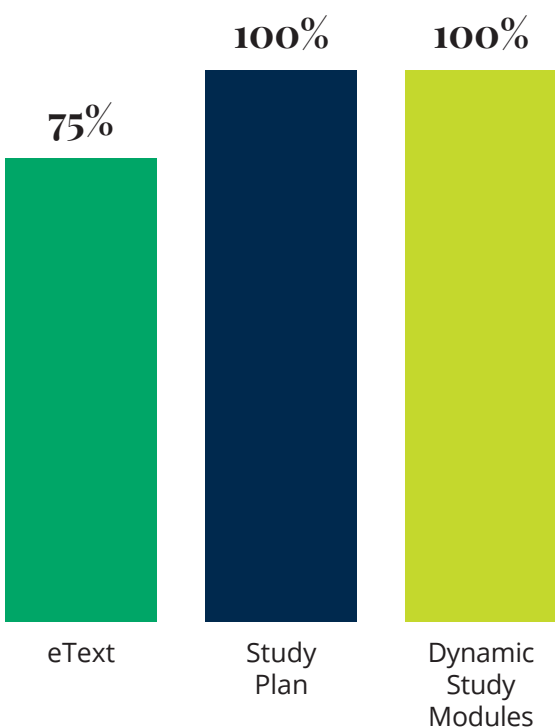
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XIII. Loan or Investment Proposal

- A. Amount requested
- B. Purpose and uses of funds
- C. Repayment or “cash out” schedule (exit strategy)
- D. Timetable for implementing plan and launching the business

XIV. Appendices (Supporting documentation, including market research, financial statements, organization charts, résumés, and other items)**MyLab Entrepreneurship**

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Chapter Summary by Learning Objective

1. Explain the benefits of an effective business plan.

- A business plan, which builds on information from the feasibility analysis and business model, serves two essential functions. First and more importantly, it guides the company’s operations by charting its future course and devising a strategy for following it. The second function of the business plan is to attract lenders and investors. Applying for loans or attempting to attract investors without a solid business plan rarely attracts needed capital. Rather, the best way to secure the necessary capital is to prepare a sound business plan.
- An effective business plan should pass these three tests:
 - **Reality test.** The external component of the reality test involves proving that a market for the product or service really exists. The internal component of the reality test focuses on the product or service itself.
 - **Competitive test.** The external part of the competitive test evaluates the company’s relative position to its key competitors. The internal competitive test focuses on the management team’s ability to create a company that will gain an edge over existing rivals.
 - **Value test.** To convince lenders and investors to put their money into the venture, a business plan must prove to them that it offers a high probability of repayment or an attractive rate of return.

2. Describe the elements of a solid business plan.

- Although a business plan should be unique and tailored to suit the particular needs of a small company, it should include these basic elements: executive summary, mission statement, company history, business and industry profile, description of the

company’s business strategy, profile of its products or services, statement explaining its marketing strategy, competitor analysis, owners’ and officers’ résumés, plan of operation, financial data, and loan or investment proposal.

3. Explain the “five Cs of credit” and why they are important to potential lenders and investors reviewing business plans.

- Small business owners need to be aware of the criteria bankers use in evaluating the creditworthiness of loan applicants, known as the *five Cs of credit*:
 - **Capital.** Lenders expect small businesses to have an equity base of investment by the owner(s) that will help support the venture during times of financial strain.
 - **Capacity.** Capacity is a synonym for cash flow. The bank must be convinced of the firm’s ability to meet its regular financial obligations and to repay the bank loan—and that takes cash.
 - **Collateral.** Collateral includes any assets the owner pledges to the bank as security for repayment of the loan.
 - **Character.** Before approving a loan to a small business, the banker must be satisfied with the owner’s character.
 - **Conditions.** The conditions—interest rates, the health of the nation’s economy, industry growth rates, and so on—surrounding a loan request affect the owner’s chance of receiving funds.

4. Understand the keys to making an effective business plan presentation.

- Entrepreneurs who are informed and prepared when requesting a loan or investment favorably impress lenders and investors.

- Tips include: Demonstrate enthusiasm about the venture but don't be overly emotional; "hook" investors quickly with an up-front explanation of the new venture, its opportunities, and the anticipated benefits to them; use visual aids; hit the highlights of your venture; don't get caught up in too much detail in early meetings with lenders and investors; avoid the use of technological terms that will likely be above the heads of most of the audience; rehearse your presentation before giving it; close by reinforcing the nature of the opportunity; and be prepared for questions.

5. Understand the importance of strategic management to a small business.

- Companies without clear strategies may achieve some success in the short run, but as soon as a competitive threat arises, they often fail.

6. Explain why and how a small business must create a competitive advantage in the market.

- The goal of developing a strategic plan is to create for the small company a competitive advantage—the combination of factors that sets the small business apart from its competitors and gives it a unique position in the market.
- Every small firm must establish a plan for creating a unique image in the minds of its potential customers.
- A company builds a competitive edge on its core competencies, which are a unique set of capabilities that a company develops in key operational areas—such as quality, service, innovation, team building, flexibility, and responsiveness—that allow it to vault past competitors. They are what the company does best and help focus the strategy. This step involves identifying target market segments and determining how to position the firm in those markets.
- Entrepreneurs must identify some way to differentiate their companies from competitors.

7. Develop a strategic plan for a business by using the nine steps in the strategic management process.

- Small businesses need a strategic planning process designed to suit their particular needs. It should be relatively short, it should be informal and not structured, it should encourage the participation of employees, and it should not begin with extensive objective setting.
- Linking the purposeful action of strategic planning to an entrepreneur's ideas can produce results that shape the future.

Step 1. Develop a clear vision and translate it into a meaningful mission statement. Highly successful entrepreneurs communicate their vision to those around them. The firm's mission statement answers the first question of any venture: What business am I in? It sets the tone for the entire company.

Step 2. Assess the company's strengths and weaknesses. Strengths are positive internal factors; weaknesses are negative internal factors.

Step 3. Scan the environment for significant opportunities and threats facing the business. Opportunities are positive external options; threats are negative external forces.

Step 4. Identify the key factors for success in the business. In every business, key factors determine the success of the firms in it, so they must be an integral part of a company's strategy. KSFs are relationships between a controllable variable and a critical factor influencing the firm's ability to compete in the market.

Step 5. Analyze the competition. Business owners should know their competitors almost as well as they know their own companies. A competitive profile matrix is a helpful tool for analyzing competitors' strengths and weaknesses.

Step 6. Create company goals and objectives. Goals are the broad, long-range attributes that the firm seeks to accomplish. Objectives are quantifiable and more precise; they should be specific, measurable, assignable, realistic, timely, and written down. The process works best when managers and employees are actively involved.

Step 7. Formulate strategic options and select the appropriate strategies. A strategy is the game plan the firm plans to use to achieve its objectives and mission. It must focus on establishing for the firm the KSFs identified earlier.

Step 8. Translate strategic plans into action plans. No strategic plan is complete until the owner puts it into action.

Step 9. Establish accurate controls. Actual performance rarely, if ever, matches plans exactly. Operating data from the business assembled into a comprehensive scorecard serves as an important guidepost for determining the effectiveness of a company's strategy. This information is especially helpful when plotting future strategies.

- The strategic planning process does not end with these nine steps; rather, it is an ongoing process that an entrepreneur repeats.

- The three basic strategies a business can pursue are low cost, differentiation, and focus.
- Controls are essential for the effective implementation of a strategic plan. A dashboard is a set of

measurements unique to a company that includes both financial and operational measures and gives managers a quick and comprehensive picture of the company's total performance.

MyLab Entrepreneurship

If your instructor is using MyLab Entrepreneurship, go to www.pearson.com/mylab/entrepreneurship for the following Assisted-graded writing questions:

1. What are the five Cs of credit?
2. Why is it important for a small business to establish a competitive advantage?

Discussion Questions

- ★ 5-1. Why should an entrepreneur develop a business plan?
- 5-2. Describe the three tests that an entrepreneur needs to pass to obtain external financing from potential lenders and investors.
- 5-3. Describe the major components of a business plan.
- 5-4. How are the three components of intellectual capital likely to become the source of a company's competitive advantage in the marketplace?
- 5-5. How do lenders and investors use the five Cs of credit when evaluating a request for financing?
- 5-6. How would you prepare to make a formal presentation of your business plan to a venture capital forum?
- 5-7. Why is strategic planning important to a small company?
- 5-8. What is a competitive advantage?
- 5-9. Strategic management is a continuous process that consists of nine steps. Identify these steps.
- 5-10. How do entrepreneurs examine their companies' competitive advantage?
- 5-11. What features of an entrepreneur's character does an investor or lender evaluate before placing their money in the small business?
- 5-12. What are strengths, weaknesses, opportunities, and threats?
- 5-13. How does a company gain a sustainable competitive advantage?
- 5-14. Core competencies are central to a company's ability to compete successfully and are usually the result of important skills and lessons that a business has learned over time. Define core competency.
- 5-15. Why is setting objectives important?
- 5-16. What are business strategies?
- ★ 5-17. Describe the three basic strategies available to small companies.
- 5-18. Under what conditions is each of the three basic strategies most successful?
- 5-19. Explain how a company can gain a competitive advantage using each of the three strategies described in this chapter: cost leadership, differentiation, and focus.
- 5-20. Give an example of a company that is using each of the three strategies.
- 5-21. How is the controlling process related to the planning process?
- 5-22. What is a dashboard?
- 5-23. What value does a dashboard offer entrepreneurs who are evaluating the success of their current strategies?

Beyond the Classroom . . .

- 5-24. Contact the owner of a small business that competes directly with an industry giant, such as Home Depot, Wal-Mart, or Target.
- 5-25. What does the owner see as his or her competitive advantage?
- 5-26. How does the business communicate this competitive advantage to its customers?
- 5-27. What competitive strategy is the owner using?
- 5-28. How successful is the competitive strategy?
- 5-29. What changes would you suggest that the owner make?
- 5-30. In his book *The HP Way*, Dave Packard, cofounder of Hewlett-Packard, describes the seven commitments of the HP Way:
 - Profit—the ultimate source of corporate strength
 - Customers—constant improvement in the value of the products and services the company offers them
 - Field of interest—seeking new opportunities but limiting them to complementary products and services based on company core competencies
 - Growth—a measure of strength and a requirement for survival

- Employees—provide opportunities for advancement, share in their success, and offer job security based on performance
- Organization—foster individual motivation, initiative, and creativity by giving employees the freedom to work toward established goals and objectives
- Citizenship—contribute in a positive way toward the community and society at large

In what ways do these values help HP define its vision?

- 5-31. In what ways do these values help HP define its competitive edge?
- 5-32. How important is it for entrepreneurs to define a system of values to guide their companies?
- 5-33. Contact a local entrepreneur and help him or her devise a dashboard for his or her company.
- 5-34. What goals did you and the owner establish in each of the four perspectives?
- 5-35. What measures did you use to judge the company's progress toward those goals?
- 5-36. Use the strategic tools provided in this chapter to help a local small business owner discover his or her firm's strengths, weaknesses, opportunities, and threats.
- 5-37. Use the strategic tools provided in this chapter to help identify the relevant KSFs.
- 5-38. Use the strategic tools provided in this chapter to help analyze its competitors.
- 5-39. Help the owner devise a strategy for success for his or her business.
- 5-40. Choose an entrepreneur in your community and interview him or her.
- 5-41. Does the company have a strategic plan?
- 5-42. Does the company have a mission statement?
- 5-43. Explain why the company does or does not have a mission statement.
- 5-44. What does the owner consider the company's strengths and weaknesses to be?
- 5-45. What opportunities and threats does the owner perceive?
- 5-46. What image is the owner trying to create for the business?
- 5-47. Has the effort been successful?
- 5-48. Do you agree with the owner's assessment of its effectiveness?
- 5-49. Which of the generic competitive strategies is the company following?
- 5-50. Who are the company's primary competitors?
- 5-51. How does the owner rate his or her chances for success in the future, using a scale of 1 (low) to 10 (high)?
- 5-52. Compare your evaluation with those of your classmates.
- 5-53. What, if any, generalizations can you draw from the interview?

Endnotes

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