Join or take over a family business – More than 50 percent of the U.S. gross domestic product comes from family owned businesses. An advantage of joining or taking over the family business includes the ease of entry into the business world where one can work with people who can be trusted and already understand a lot about the business. However, the flip side is that entry into the business world may be too easy and the business members know each other too well. Another disadvantage is the lack of objectivity to the business operation.

Start-up businesses can increase their chances of success by doing the following:

- Understand their strengths and weaknesses
- Develop and follow a business plan with realistic goals
- Know who their competitors are and understand their target market
- Create customer loyalty and build strong customer relationships
- Develop a product or service that appeals to a large market share
- Understand and closely monitor financial matters
- Maintain flexibility

3. Existing business

Existing businesses are already in the middle of reality. They have different issues generally, than start-up businesses. They may be experiencing rapid growth, changing markets, personnel issues, funding needs for expansion, etc. A successful existing business has the advantage of experience and a history of income and expenses, customer base, and an established image.

What is the market? This question is an on-going question because the market is not static. A business or enterprise is not a museum to store products and services. Business survival depends on creative, flexible, dynamic marketing strategies. Markets are continually changing and competitors are always entering the business arena. Marketing is everything a business does to get the products and services to the end user. Marketing is ongoing, dynamic, and requires an understanding of the operating environment in which the business exists.

Marketing strategies

- *Customer orientation* – Successful marketing involves designing market strategies that focus on satisfying customer needs.
- *Niche marketing* – Identifying and targeting marketing efforts to the needs of a few customers who have specific characteristics and similar needs.
- *Customer profiling* – Maintaining an accurate, current customer profile that keeps the business focused on the needs of the customer.
- *Detecting trends* – Identifying trends within the business community and taking advantages of marketing opportunities.
- *Studying the competition* – Competitive analysis allows a business to remain astute to the changes in the competitive environment.

Management strategies

- *Communication* – A successful business or enterprise needs to focus internally on the communication within the organization so that employees are motivated. The responsibilities of each person within the business should be clear and matched with appropriate level of authority. Externally, the business should communicate effectively so that customers and suppliers remain loyal and supportive. Replacing customers and suppliers due to mismanagement can be very costly to a business.
- *Controls* – Accurate controls need to be established. Certain controls need to be monitored daily, weekly or monthly, depending on the type and scope of the business. These controls include sales, cash flows, and account receivables. Other controls such as expenses, profit margins, and inventories can be monitored monthly or every few months or so, again depending on the business.

Perhaps the two most serious questions an existing business must ask itself are:

1. how will it manage growth, and
2. how will it manage crises?

4. Managing growth

"Growth for growth's sake is the ideology of a cancer cell." P. Chebard, CEO, Patagonia

Does a business have to grow? No. Growth has a price! Norm Brodksy, entrepreneur and business consultant, warns that to be in control of one's business, the owner has to know how much cash is needed for every additional dollar in sales. The decision to grow a business, not just start it, is an active decision that requires planning. Growth should not be uncontrolled or unplanned. Intelligent and

deliberately controlled growth, including understanding the forces that impact a business such as the market, customers, and the financial and cost issues associated with growth, are essential for business survival. (Brodsky, Norm. "Paying for Growth," Inc. Magazine. October 1996, 29-30.)

As a professional, you are in a good position to explain the reality of what business growth means to a business. Ask the question: Why do you want to grow? Reasons why people want to "grow" their business might include the following:

- Achieve economics of scale
- Acquire volume discounts
- Protect market share
- Increase profits
- Improve image
- Increase customer base
- Improve ability to compete
- Improve customer service

Does the reason for wanting to grow the business still fit with personal and family goals? It often happens that the businessperson overlooks his or her personal goals for being in business. Encourage the businessperson to take some time to review personal and family goals and make sure that the goals for growth are aligned with personal and family goals.

Once the goals have been reviewed, the business owner must be able to answer several questions if he or she is considering business growth:

- How much growth and for how long?
- What is the gross margin?
- Is there additional overhead?
- How long until payback?

Warning signs of uncontrolled growth
When a business is experiencing uncontrolled growth, it usually is in a state of disaster and chaos. There are signs to warn an owner before the final pitfall of unmanaged growth occurs, which could be loss of the business and/or bankruptcy.

- Daily business details overlooked or ignored
- Customer complaints and loss of customer loyalty
- Low employee morale and high employee turnover
- Cash flow problems and loss of profitability
- Mismanaged resources
- Inconsistent performance standards and diminished quality of products

5. Exiting a business

Nothing lasts forever. A business has a life cycle and at some point, decisions will have to be made regarding exiting the business. Many business owners tend to wait too long before planning how they will exit their business. By creating an exit strategy, a person will have a benchmark against which to judge the business' progress and the owner's personal involvement and/or commitment. An exit strategy also compels a person to think about when and why he or she might decide to exit the business before he or she is forced to make an untimely, unwanted, or uncalculated exit.

The percentage of ownership to be liquidated, the exit deadline, and the amount of on-going participation in the business have an influence on the type of exit strategy. There are eight basic strategies for ending a business:

- Selling to one's heirs or employees
- Selling to a supplier, customer, or competitor
- Selling to a financial buyer
- Liquidating assets
- Enforced liquidation

- Going public
- Managing for life
- Passing the business on to one's heirs

Each of these strategies are described further below:

Selling to one's heirs or employee – since the buyers in this category are closely associated with the business, they should have a good understanding of the real value of the business but may not have the money to purchase it. The seller would benefit by adequately training the future owner so that he or she protects the owner's investment. A long-term payout from the business profits may cover many years.

Selling to a supplier, customer, or competitor – the buyer may have some knowledge of the value of the business and will benefit by acquiring the business, either to reduce competition, control distribution, or increase vertical growth.

Selling to a financial buyer – the buyer may not have a particular interest in the specific business but has money and management skills and is interested in acquiring a profitable business.

Liquidating assets – this strategy involves selling the assets and goodwill separately because they are worth more sold separately than if they were sold together.

Enforced liquidation – a business owner has little or no control with this type of business exit, other than trying to salvage as much as possible from the remains. Enforced liquidation occurs because of bankruptcy or a loan default.

Going public – the owner of a financially sound, growth-oriented business has the option of remaining in the business for a while after selling his or her stock to the public. Eventually, the owner can sell his or her stock and cash out.

Managing for life – this approach is frequently used because it is simple and ambiguous – the owner runs the business until he or she dies with no clear plan for succession or continuation. If the owner has not made plans for what happens to the business upon his or her death, there may be serious complications, and possible loss of the business, for the family members, business partners, or employees left behind.

Passing the business on to one's heirs – this strategy is unique to each family-business. It depends on many variables including the age of the owner and other family members, the size and value of the business, the communication process, the flexibility of the owner and family members, the family culture, the likelihood of an adequate successor, and the level of debt. A well-managed transfer from one generation to another involves treating family members as equally as possible, while recognizing their skills and interests.

C. Enterprise changes

1. Business valuation

Determining the market value of a business is one of the first steps to preparing an exit plan. However, there may be other reasons that one wants to determine the market value of his or her business. The process of determining the market value of a business can be quite complex. There are many hard-to-measure variables including intangibles that make the valuation process very challenging. The key to a successful transaction is knowledge and information on the part of the buyer to overcome the seller's claims of unreported cash income or the seller's real reason for selling the business – the hidden problems that the seller does not want to reveal.

The difference between value and cost of a business is that ultimately the worth of a business for a buyer seeking an investment is only as much as its ability to produce profits. For the buyer looking for a livelihood, the worth of a business is only as much as its ability to produce profits, cash flow, and a fair wage. For the seller, the worth of the business is only as much as the buyer is willing to pay.

People can become so excited with the idea of buying a business, they overlook other opportunities. What is the actual cost of purchasing a business? The cost to the buyer is the opportunity cost – the alternative investment opportunities versus of purchasing the business.

Methods of valuation – There are several methods of valuation that are commonly used. In fact, it is not uncommon for people to compute several methods and use a weighted average to determine the actual valuation. The following methods are some of the most common valuation methods used:

- Adjusted book value
- Asset valuation
- Capitalization of income valuation

- Capitalized earning approach
- Cash flow method
- Cost to create approach
- Debt assumption method
- Discounted cash flow
- Excess earning method
- Multiplier of earnings
- Multiplier or market valuation
- Owner benefit valuation
- Rule of thumb method
- Tangible assets method
- Value of specific intangible assets

There are pros and cons for each method. The method selected should be relevant to the type of business being valued. See the Appendix Section (VII) for a description of each of the methods listed above. Regardless of what method is used, the business owner needs to understand the valuation method used and the reason for using the method so that he or she can defend the price of the business. The buyer needs to understand the reasoning behind the price so that he or she can evaluate the level of personal and financial risk required to make the purchase and own the business.

2. Reasons why businesses fail

There are many reasons why businesses fail. As a professional, you are in a good position to provide a person who wants to start a new enterprise or a person who is already in business with information so the following problems can be avoided.

a. <u>Management:</u>

- *Failure to commit* – A business owner must be willing from the very beginning to commit money, time, and other resources. He or she must be willing to come in first, leave last, get paid last, and in many cases, get paid less.

- *Failure to seek help when in trouble* – It is not uncommon for business owners to wait until it is too late to get some help. A new businessperson should put together an advisory team of people who are indirectly affiliated with the company such as a banker, accountant, lawyer, mentors, suppliers, family or close friends with experience in a similar business, and other business resources groups.

b. <u>Marketing:</u>

- *Failure to promote* – Adequately promoting one's product/services is essential. Ranchers and business owners who don't market because sales are so good that they think they don't need to promote, or sales are so bad they think they can't afford to promote, are headed for failure.

- *Failure to introduce new products/services* – Every product goes through a life cycle of introduction, growth, maturity, and decline. Businesses will not survive without new products or services. Although sales can be made on products/services in the decline stage, sales become increasingly unprofitable.

- *Failure to pay attention to the outside world* – Market and global factors will impact an enterprise. Business owners have a difficult time paying attention to market and economic conditions, competitors, environmental changes, trends, and other external factors that affect an enterprise because they are so busy with the day-to-day operations.

c. Financial:

- *Failure to manage cash flow* – Cash flow is the heartbeat of any enterprise or business. It is essential that a new business owner knows the source and use of every dollar in the business. The loss of one customer or one sale should not cause irreparable damage; however, a mismanaged cash flow that results in nonpayment of workers compensation taxes or a missed payroll can put a person out of business.

- *Failure to manage accounts receivables and customers' accounts* – It is not uncommon for new business owners to fail to collect from customers. A sale is not a sale until money is collected from the customer. Customers won't pay if the business doesn't take time to invoice them. A good set of credit and collection policies can be a major factor in the business's profitability and survivability.

- *Failure to show earnings* – If a new business or enterprise doesn't show that the business owner will be able to draw an income within three years, it is a hobby, not a business.

- *Failure to cover overhead* – A person must know exactly what it costs to produce the product/service and allocate a portion of the overhead cost to each until sold. Volume will not correct the problem if the product/service is incorrectly priced.

- *Failure to understand cost versus price* – It is the market, not the business's costs, that ultimately determines the price at which one can sell one's product or service. While the cost establishes the level below which one cannot sell one's unit and make money, the maximum price for which one can sell a product or service is determined to be somewhere between the price floor and the price ceiling, depending on the market.

- *Failure to understand financial reports* – "My accountant handles my financials," is a common statement made by business owners. However, the accountant is not going to pay the loan when the company fails. It is essential that the business owner know his or her financial records. To understand one's business, the owner must understand the statement of cash flows, the balance sheet, and the income statement, and how they connect with each other.

- *Failure to use money wisely* – Cash shouldn't buy buildings and equipment, and long-term loans shouldn't pay for inventory. A business owner needs to know how to apply for loans with terms that match the uses of funds.

3. Crises management

A crisis is anything that has the potential to negatively affect the stability, reputation, or creditability of a business. A small business or a start-up business must be prepared, even more so than a large business, to handle a crisis, even a small crisis, because the margin of error is so much smaller. Crises management should be a top priority because disruption or loss of business happens – and when it does, it can be very serious. Because so many businesses operate with limited resources, including time, business owners often fail to plan for crises management. Good business management includes developing plans to cope with unforeseen events that can seriously disrupt operation.

a. There are five core types of business crises:

Organizational crises – Organizational crises are events that disrupt the operation of the business. For example, the loss of a supplier of pesticide at the beginning of the summer can seriously disrupt crop production. A threatened lawsuit by a disgruntled neighbor over a dispute over water rights can suddenly take precedent over the daily operations. Management succession can create a crisis within a family business.

Employee-related crises –The people within a business can disrupt operations in many ways, intentionally or unintentionally. For example, violence or drugs in the workplace, or an accident can create an emergency situation. The loss of a key employee can seriously disrupt management indefinitely.

Customer-related crises – Although the business owner has little control over customer-related crises, it is extremely vulnerable to predicaments such as product-liability problems,

loss of a major customer, customer payment delays or bankruptcy.

External crises – External crises are devastating to a business. A business has very little, if any, control over natural catastrophes such as weather, fire, or earthquakes or man-made disasters such as power outages, gas leaks, or industrial accidents. Even changes in zoning and local political issues can create chaos in a business.

Personal crises – Usually the last in priority, but often the most serious, personal crises can be devastating to a business. Personal crises include the death or loss of spouse or family member, a serious illness or accident, or personal, marital, or family problems. Family businesses face personal crises when business succession is not handled properly within the family.

b. <u>Proactive crises management</u>

The most important thing a person can do is to plan ahead for the inevitable — do not wait until a disaster happens to start planning. The following steps, recommended by business crises management counselors, can help a businessperson prepare for and manage a crisis, no matter how small the business.
Get the facts – The first step is to get accurate information about the crisis and its potential damage. By knowing the facts and understanding the elements of the crisis, the owner can challenge rumors, exaggerations, and negative perceptions.

Form a crisis team – Define roles and responsibilities as well as how to reach one another day and night. Develop different scenarios and even simulate mock emergencies to practice responsiveness to the five core types of crises (above).

Identify weaknesses in the business – Forecast potential crises by preparing a list of crises that might be more likely to occur and another list of crises that might not be as likely to occur but would be more devastating to the business. Compare both lists for similar weaknesses in the business that occur on both lists and develop a plan to respond to those vulnerabilities before they turn into a crisis, either by eliminating them or lessening their risk to the business in the event a crisis occurs.

Develop an action plan – For each potential crisis, develop an action plan that includes a simple checklist of steps that will be followed. The plan should include the team members assigned to certain responsibilities and important phone numbers.

People who have weathered a business disaster say that the worst part of the experience is the element of surprise. A well-thought-out plan will remove some of the damage out of the crisis should it occur.

c. **Recovering from a crisis**

If a crisis does occur, the best thing a business owner can do is to avoid taking a defensive role or acting as if nothing has happened. The crisis will not disappear by ignoring it. Negative information (whether correct or incorrect) about a business can spread very quickly. The business owner should communicate with family, business team, customers, suppliers, and community that the crisis is being managed effectively. Quick, practical communication is important to reassure everyone who is directly involved in the business as well as the public. If the media becomes involved, proactive communication includes providing a brief statement about the crisis and clarification of corrective steps that will be taken to overcome the crisis.

d. **Plan ahead for the next crisis**

Surviving a crisis offers the management an opportunity to review how the crisis occurred, analyze how the crisis was handled, evaluate the performance of each member of the crisis team, and prepare a plan for how to handle a similar crisis in the future.

In summary, although crises are inevitable, the majority of them can be managed. Good business management includes developing a plan to handle unforeseen events that can seriously disrupt business operation. No one should just sit and wait for a crisis to hit. With pre-planning, good communication, and effective follow-through, a business can be managed to survive a crisis.

D. Resources

- An excellent resource for business planning assistance are the Small Business Development Centers, located throughout the state. For a list of Wyoming offices, see the Resources Section (6) of this guide.
- Gail Gordon, Business Development and Family Economics Specialist, University of Wyoming Cooperative Extension Service, College of Agriculture, P.O. Box 3354, Laramie, WY 829071, (307) 766-5373.