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Launch Rules for Small Businesses

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Abstract
The entrepreneurial desire is alive and well in the U.S., and universities have developed various programs targeted at helping those embarking on this adventure. From their work with hundreds of start-up businesses, Extension economists at two such centers have defined a set of "launch rules" to help new businesses avoid common pitfalls. These "rules" are highly recommended actions to be taken by entrepreneurs as they stake their time and resources to a new venture. They will also provide direction for Extension faculty engaged in helping these entrepreneurs.

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Introduction

The entrepreneurial desire in the U.S. is alive and well. Over 99% of employers in the U.S. are small businesses, and there are more than 15.6 million self employed (U.S. Small Business Administration, 2005). Universities have developed numerous programs to assist entrepreneurs (Burney, 2001; Holcomb & Muske, 2000; Muske & Stanforth, 2000). Two examples are the Food & Agricultural Products Center at Oklahoma State University and the Food Innovation Center of Oregon State University.

From their work with hundreds of start-up businesses, the Extension economists at these centers have defined a set of "launch rules" to help new businesses avoid common pitfalls. These "rules" are highly recommended actions to be taken by entrepreneurs as they stake their time and resources to a new venture.

These rules will benefit Extension faculty whose responsibilities include helping entrepreneurs. In addition, this information will positively affect the stakeholder clients of these programs as the Extension faculty become better equipped to provide the assistance they need.

Rules for Launch Preparation

Considerable work is required before a business launch should be considered (Johnson & Holcomb, 2006). Once these pre-launch activities have been performed, an entrepreneur must focus on the planning functions associated with a business launch.

- Develop, test, and implement a production plan.
- Form a distribution plan, including steps to take in the event of unforeseen marketing occurrences.
- Establish a working capital plan to carry the business through the launch phase.

Production Plan

A production plan goes far beyond the process of manufacturing a product. The production plan includes all aspects of input procurement, processing, and inventory management.

It is recommended that more than one supplier for each ingredient and packaging/labeling input be identified, even if contractual arrangements are only made with one supplier. In the event of an immediate need, these back-up suppliers can be contacted. Manufacturing is notorious for employee turnover, so considerations must be made to have enough trained employees present to maintain production levels as well.

Inventory management is crucial for maintaining a flow of products to buyers. Finding the right balance for inventories is best determined on a case-by-case basis. Experience will help small business owners identify seasonal swings and adjust inventory levels. Accountants and business specialists may be useful in evaluating the logistics and costs associated with storage time and space.

Distribution Plan

The distribution plan details how merchandise will get from its production point to the selling venue. There are two types of distribution: direct store delivery and indirect distribution.

Direct store delivery means that the manufacturer directly delivers the products to the individual retail establishments. For small start-up businesses, direct distribution is a means of getting product to the buyer/retailer while avoiding fees and handling costs associated with the use of wholesale warehouses or chain-specific distribution centers. Other times, it is a necessity as the startup doesn't have the volume of sales to warrant other distribution methods.

Direct distribution does, however, create management challenges. It may be difficult for a small business owner to fulfill all the responsibilities associated with production and distribution. Too often the owner will gravitate towards one, resulting in problems with the other. Additionally, managing promotion materials and displays is a vital part of direct distribution, but the time and expenses associated with such activities are often overlooked in the development of a distribution plan.

Indirect distribution means using brokers, wholesalers and/or distributors to manage distribution and promotions. These players come at a cost: commissions for brokers or slotting fees to get into a warehouse. One must carefully select the brokers she or he uses to launch a new product and the commissions required for their services. A good, motivated broker may collect purchase orders for several truckloads of the new product, while a broker with too many clients may neglect the newly launched product in favor of consistent business from his/her other clients (Brooks, 2004).

Warehouses provide the means for reaching several retail outlets while maintaining a single drop-off point. Because warehouses service retail outlets with truckloads of multiple products, the distribution costs per unit are lower for all items, thus products can be distributed over a larger geographic region at less expense.

Warehouses typically operate at or near full capacity with low per-unit margins on the products they carry. Slotting fees--i.e., the initial cost of "buying" space for a new product in a warehouse--can occur in some industries and are prominent in the food industry. Several factors figure into the level of slotting fees (e.g., sales potential, storage requirements, and the product's perishability).

In addition to slotting fees, a warehouse may request, on behalf of the retail outlets it represents, that the manufacturer pay for and participate in specific promotional efforts to bolster retail sales of the product and increase turnover in the warehouse.

If product turnover declines or quality problems are experienced, the warehouse may require the manufacturer to "buy-back" the products at a higher-than-wholesale price (even up to retail price) to recapture costs associated with warehouse storage expenses.

Working Capital Plan

The amount of money needed to successfully launch a new enterprise is commonly underestimated, largely because a business and/or product launch takes longer and cost more than anticipated. One should estimate how much capital will be needed for the start-up effort, and then have a larger amount on hand.

At or after the launch, one of the most common cash management mistakes results from the incorrect notion that products manufactured are immediately sold and the revenue collected. In the early stages of a new business, a considerable amount of money may be used manufacturing products to meet initial orders and build inventory. Further, retailers or warehouses may wait a month to pay the invoice amount for a shipment. Thus, the level of accounts receivable grows while available cash quickly declines. A wise entrepreneur will plan ahead for such activities and be prepared with factoring agents and an accounts receivable loan at his/her bank.

A working capital plan also needs to include contingencies in the event a large customer is lost.

Balancing the number and size of one's clients is a difficult task, and the upside of having a few large, consistent clients overshadows the potential drawbacks.

Conclusions

Developing and launching a small, new business requires considerable research and meticulous planning to improve the odds of success. These "rules" are highly recommended actions to be taken by entrepreneurs as they stake their time and resources to a new venture. It is hoped that new entrants into any industry and the Extension specialists assisting them will carefully consider the suggestions and examples that have been incorporated into this article before starting new ventures.

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