COMMERCE
ASSESSMENT
GROUP

So, You Want to Start A Small Business?

At some point, the idea of starting a small business crosses the minds of most people. This thought however remains a dream that few ever act on - and for good reason. Statistics show that for every 100 small businesses started, 80 fail within the first two years and 90 fail within the first five years.

While much is made of these statistics, little is written about the causes of new business failure or the steps one can take to avoid becoming a statistic.

In our view, four defining factors lead to new business failure. Taking the time now to understand and adequately address these can mean the difference between success and failure.

1. Validated Product or Service

Starting a business begins with a product or service idea. Undoubtedly this is shared with family and friends to solicit feedback. Typically one receives initial support and encouragement for their idea, which is what you would expect. Individuals will often then invest considerable money and time developing their idea and continue to share their work with family and friends. Many will then start their business, unaware of a crucial step they have bypassed: validating their offering with potential customers.

The real test of your business idea begins when you actually talk to prospective customers and strangers. This can take the form of presenting your product or discussing your service offering with those who will use and purchase what you have to sell.

No one likes to experience rejection and it is natural to only focus one's thoughts on future success. However, by not talking and fully vetting your product or service with potential customers before beginning your business, you risk spending valuable funds prematurely. Skipping this step means you may find yourself investing further time and money into your offering, changing the concept of your idea or worse, learning there is no market for your product.

Stepping outside of your comfort zone and talking to potential customers is an important exercise to test how you handle questions, feedback and rejection. Planning a series of questions will help you through this step. The exercise will allow you to uncover if and how your product or service meets a basic need of potential customers. It will also help you understand the strengths and weaknesses of your offering and to determine how to position your offering for success.

The information gathered will likely save you from making costly mistakes or missing important opportunities that you may not have thought about.

2. Customers Ready to Buy?

Speaking to potential customers about your product or service is critical to ensuring there is a market and desire for your product. However merely talking about your offering is not enough. You also need to determine if customers are prepared to purchase your offering once you start your company.

As a business owner, you must be prepared to ask prospective customers:

"If I come back in 3 months, will you purchase my product (or service)?"

This is by far the single most important indicator of success that you can establish prior to your upstart. Asking this question of potential customers will provide you with a good sense of the demand for your product or service. Launching your business without asking this question will most likely result in a waste of time and expenditure of limited capital.

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3. Business Financing

A credible business plan forms the foundation for future success. The business planning process forces the entrepreneur to think through all of the financial requirements of their business. Ultimately this helps to accurately predict revenue.

When building your business plan, it is important to develop realistic, pessimistic and optimistic sales forecasts based on feedback from prospective customers. It is also important to get actual quotations for capital (assets such as equipment) and develop the most accurate cost picture possible. This should also include some cost contingency to deal with unforeseen expenses.

By taking this approach to developing your business plan you will be in a much better position to determine your cash needs and if you have sufficient resources to start and operate your business until you surpass the break even point. It is crucial to track all cash outlays on a regular basis and compare these to your original budget or plan. This will provide you with a clear view of costs and revenue and ensure that you have sufficient funding to meet your startup and operating needs. By following this approach, you will be in a position to ensure you have adequate funding for your business.

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4. Personal Finances

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The impact of personal finances is too often overlooked in relation to entrepreneurial success. One needs to consider their personal financial obligations and take these into consideration as they contemplate developing a business. Given the impatient nature of many entrepreneurs to get started with their idea, it is easy to gloss over this point. Anecdotal evidence and experience speaking with dozens of successful small business owners suggests doing the following:

Do not plan on withdrawing any salary or cash from your business for the first 12 months. If you are intending to draw money out of your business during this period, then you need to reevaluate your personal finances and get them in order prior to starting your business.

Ensure that your personal financial needs are addressed through savings, or through support from family members. Take the time to ensure your own financial house is in order.

If you do not have your personal finances in order, delay starting your business until this is rectified.

No amount of advice can guarantee success when starting a new business. Unforeseen circumstances and luck also play a role in one's success. However, ensuring that you adequately address the four factors of business failure prior to the launch of your new business will likely increase your odds of being in business five years from now.