Business Life Cycles and Business Planning

What are business life cycles, and what is their relationship to business planning?

Generally, businesses pass through three stages before reaching the final stage of decline. The time it takes to reach or to pass through each stage varies by business. It is important that you properly identify the life cycle stage of your business so that you can plan appropriately and establish realistic goals for the future. The four life cycle stages for a business are start-up, growth, maturity, and decline.

What are the traits associated with each life cycle stage?

Each stage has unique characteristics.

Start-up

Start-ups are businesses that have yet to come into existence or have yet to turn a complete revenue cycle. At this stage, the owner (or owners) needs to invest a great deal of time, effort, energy, and money into the business to create a stable customer base, to buy inventory, and to engage in other business activities before revenues are generated. The start-up stage is generally characterized by innovation, high risk, and low profit margins.

Growth

When businesses leave the start-up stage, they typically start to grow. Although a company can always use more cash, most growing firms can get by on their own limited resources. The business owner understands his or her business at this point, as well as the key competitors. Major customers have been identified. Often, additional help is needed in production, manufacturing, operations, or sales. Ideally, during this stage, consumer demand is established and increases, the company experiences increasing sales, profit margins increase, and a market is established.

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Maturity

When businesses crack the local market and manage their affairs efficiently, they become mature. Mature firms have achieved a certain amount of name recognition. Contacts are well-established, sales require less effort, the business produces a reliable stream of cash, and borrowing becomes easier. At this point, intensive marketing may be needed to increase or maintain market position, and there is little product innovation. Profit margins tend to stabilize.

Decline

During this final stage, the market begins to shrink. There is usually no product innovation, businesses cut costs to maintain profits, and profit margins are thin.

Which goals and planning tips are most appropriate for each stage?

By knowing which life cycle stage your business is in, you can plan effectively.

Start-up

The challenges facing a start-up are very clear. You must learn your business, establish and expand your customer base, and begin to grow. During this initial stage, you should prepare a business plan, determine the structure of your business, and begin to think about investment management and tax management. Planning is essential, but you must also call on customers and do everything that you can to generate cash.

Growth

At this stage, your goal is to become an established firm in the market. Indeed, you may want to become the preferred company. Other goals may include expanding your business through capital reinvestment or outside financing, attracting and retaining key employees, providing insurance and employee benefit plans, and reviewing retirement plans. It is still important to maintain a cash reserve and to watch expenses, however, to guard against unforeseen problems.

Maturity

The main risk at this stage is complacency and failure to adapt to a changing environment. You need to stay competitive and become innovative. Budgets, moreover, become very important. Move your investments into productive areas of your business and withdraw them from areas of low return. Expenses should be scrutinized. Also during this stage, you should focus on enhancing and managing employee benefit programs, setting up nonqualified plans for key employees, developing a business protection strategy, and updating your business's valuation.

Decline

At this stage, you should be concerned with ensuring the proper succession of your business or considering the possible sale or merger of your business. You may also be concerned with stock incentive programs for you and your employees to spur profits. In addition, you may wish to explore ways to minimize estate and gift taxes.

Clearly, the particular stage of growth of your business dictates planning for it. Firms may stall, regress, or fail at any point. Before creating any plan for your firm, therefore, you must determine which stage it is in and become familiar with the issues that come into play at that particular stage.

What is business planning?

Business planning involves making decisions about the future of your business. Plans force owners to consider the long term as well as the short term. Many businesses construct five-year plans, and nearly all create annual budgets. Plans help to improve business control, to allocate resources most effectively, and to communicate the potential of your business to lenders and customers.

What is the business-planning cycle?

If you're starting up a small business, there are a number of plans you can draw up. In particular, however, there are four annual plans that deserve particular note. The first is a personal plan, the second is a strategic plan, the third is an annual operating plan, and the fourth is a forecast. Of course, you'll probably also want to create a formal business plan, which is a fairly standard document used to apply for venture capital or to attract other sources of capital, such as a Small Business Administration loan. Although similar to strategic plans, formal business plans are more detailed.

Personal plan

This is not really a formal document. It's just a thought process that enables you to determine why you are in business and what you want from your firm. What are your goals and expectations? In addition, of course, you'll want to develop a personal cash-spending plan at this point, which should correspond to the cash you'll withdraw from the business for personal use. To do so, you'll need to analyze your personal spending, income, and savings reserves.

Strategic plan

The strategic plan maps out where the firm should be several years from now. Financial projections are general and usually cover five years. You need to develop specific strategies today to meet your long-term goals. Annual budgets must conform to long-term goals. Strategic plans usually start with a mission statement and then analyze both the external business environment and the inner workings of the company itself. You recognize your company's strengths and weaknesses and map out a course to take the company from its current position to its desired position.

Annual operating plan

This is really the budget. You use detailed financial projections to show why the firm is ahead of or behind planned performance. You'll need to include sales, cost of sales, labor expense, and other expenses.

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