NEW VENTURE EVALUATION WORKBOOK

DEFINITION SECTION

MANAGEMENT GUIDE

VERSION 1.2

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PREFACE

This workbook is a part of a larger new venture planning tools development program. Its primary objective is to assist in the development of new business without large development staffs.

The tools consist of a series of workbooks designed to provide a check list of key issues that need to be addressed during the development of most business concepts. We believe that the process of venture development is an active one. While much of the workbooks focus on data collection, analysis and planning, we believe, that most activities should be dedicated to "hands on work" with the product, the process, and the potential customers. We hope that these tools will act to focus activities on "what must be done". The philosophy expressed in this workbook reflects that of the authors and not of the organizations or corporations involved.

We intend that this workbook and all others in the series will be "evergreen". New versions of the workbooks are expected to be published periodically, reflecting constructive comments by users. This workbook reflects the efforts of many individuals who have provided ideas and comments.

INTRODUCTION

This is a *New Venture Evaluation Workbook*. It is designed as a tool for evaluating New Venture Ideas as viable Business Concepts. It is designed to work with the *New Venture Workbook*. That document is designed for developing an operational plan for the new business concept. This document combines information gathered in that workbook with other subjective information to produce an evaluation summary.

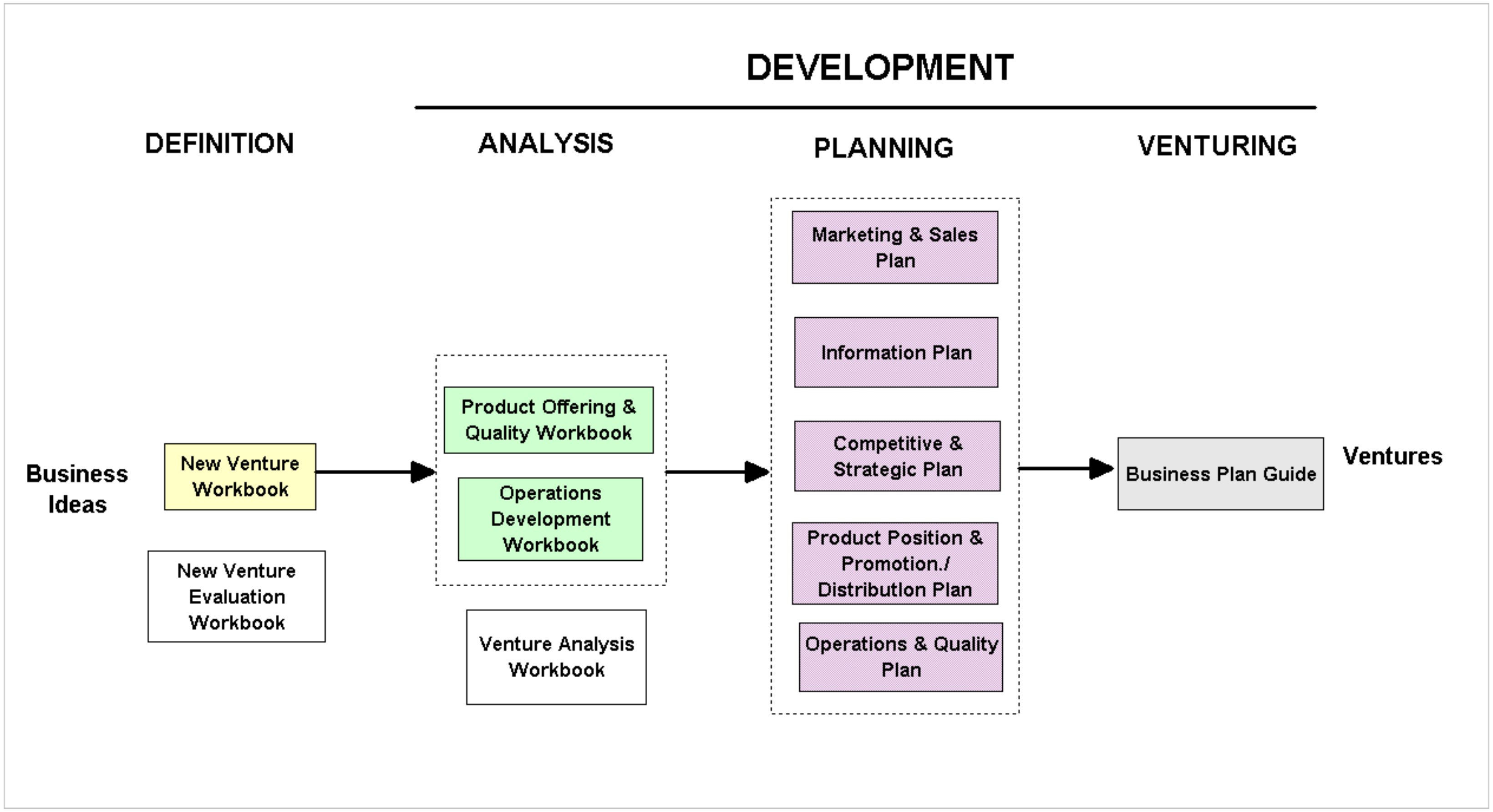
It is the intent of this evaluation workbook to assist management in determining which programs should be supported fully. Your judgement is crucial in accomplishing that goal.

The Evaluation Workbook is mainly a screening and management device. Not all good ideas should be continued and not all good ideas by those that originated the concept. The Workbook is designed to be used by an individual or a small team, who have other responsibilities. It represents a framework for evaluation.

We have come to recognize that many good Ideas, which might have become successful ventures, have gone undefined and undeveloped. These workbooks are a part of the effort to change that.

This *New Venture Workbook* and its management companion, the *New Venture Evaluation Workbook*, represent step one of a four-step process for taking an Idea to a Venture.

Good Luck. It is not supposed to be easy.


DEVELOPMENT
DEFINITION
ANALYSIS
PLANNING
VENTURING
Business Ideas
New Venture Workbook
New Venture Evaluation Workbook
Product Offering & Quality Workbook
Operations Development Workbook
Venture Analysis Workbook
Marketing & Sales Plan
Information Plan
Competitive & Strategic Plan
Product Position & Promotion./ Distribution Plan
Operations & Quality Plan
Business Plan Guide
Ventures

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I. BUSINESS DEFINITION

A. PRODUCTS

What products and services do you intend to sell[1]?
This description can be as specific or as general as the present stage of development will permit. Try to be as specific as possible. The product definition limits the range of the business that will be considered. However, the more specific the product is, the easier it is to define the means of production. At a minimum, specify the use of the product and service to the customer and user.

ABSTRACT

1 Included in the *New Venture Workbook*

B. APPLICATIONS

What are the specific applications for the products and services?[2]
The evaluation of market potential focuses on specific applications into which the product or service will be sold. These "applications" should represent separate opportunities, or markets, for the business. In some cases, the applications can be different major customers or separate industries.
Since the total opportunity will be assessed based on the sum of the opportunities of the applications, they should be selected to be as independent as possible.
For each application the customer should be identified with a description of his use.

APPLICATION 1. -

Customer:

Use:

APPLICATION 2. -

Customer:

Use:

ABSTRACT

Application 1
Application 2

[2] Included in the *New Venture Workbook*

C. MANUFACTURING

How will you make the products and services that you intend to sell?[3]

The means of producing the products and services should be described in as much detail as possible. At least the general process of manufacture should be described.

If new facilities are needed, a general description should be included. If toll production or a manufacturing partnership is contemplated, the arrangement should be described.

ABSTRACT

[3] Included in the *New Venture Workbook*

D. MARKETING AND DISTRIBUTION

How will you deliver the products and services to your customers[4]?

The means of distribution and marketing must be described. Identify the proposed distribution channel including possible distributors or marketing partners.

The way by which the product will be marketed to the customer needs to be described. For example, if the product is to be sold to an automotive company, direct selling is usually the method of choice.

ABSTRACT

[4] Included in the *New Venture Workbook*

E. COMPETITIVE PRODUCTS

What are the existing competitive products and services which our product offering (products and services) will replace[5]?

There is almost always some type of competition, either potential or existing, for the product offering. Both in-kind and functional competition should be considered. In particular, functional competition should be examined closely.

APPLICATION 1. -

APPLICATION 2. -

ABSTRACT

Application 1
Application 2

[5] Included in the *New Venture Workbook*

II. BUSINESS STAKE

This sub-section covers Business Stake. A clear definition of Business Stake can determine if a candidate Business Concept is worthwhile.

At the top of this Business Stake definitional effort is the question:

"Can this product offering be sold at a reasonable profit and in reasonable volumes"?

Because Allocated Overheads are both difficult to predict and difficult to control, it is better to do initial calculations without them. By convention, during the Definition Step, we use Contribution Margin to produce a reasonably clear picture of potential profitability.

Also, by convention, we use Analogs or Models to help us predict the size and shape of the market. If our product is new, we can look at similar products and use them to help project Functional Opportunity.

The objective of going through this sub-section is to screen the candidate Business Concept for potential market viability, profitability, and worth. Detailed financial analysis comes at a later point in the process.

In general, Contribution Margins below 30% are not desirable and Contribution Margins above 50% are desirable. Candidate opportunities should fall in the $5MM to $20MM range to be considered viable.

Projected Timing and Development Costs are balanced against Opportunity and Contribution. These are handled separately.

A. CONTRIBUTION MARGIN, TARGETED VARIABLE COST & PRICE

What must be the maximum cost for the product to make the venture profitable[1]?

What should be the gross earnings (contribution) of the product offering (products and services)? The test of potential financial worth of the venture is "acceptable" earnings. The minimum measure of earnings is the Contribution Margin, which is the difference between the target sales price and the variable cost. Contribution Margin does not consider allocated fixed costs or overhead.

Contribution Margins of greater than 50% are desirable.

Contribution Margins of less than 30% are not desirable.

The highest target variable costs are calculated based on the targeted price and the minimum contribution margin.

Contribution Margin = (Targeted Price - Variable Cost)/Targeted Price

Variable Cost = (1 - Contribution Margin) X (Targeted Price)

APPLICATION 1. -

APPLICATION 2. -

ABSTRACT

Application 1	**Application 2**
%	%

Confidence:
Certain 3 2 1 0 Not at all

[1] This section is included in the New Venture Workbook. Use only the main feasible applications.

B. MEASURE OF STAKE

What is the measure of worth to the firm for this business concept[2]?

Various measures of business stake can be used to estimate the worth of a successful venture. However, at the early phase of a venture, sufficient information for such a credible assessment is usually not available.

At a minimum, the feasible sales potential in units sold either in total or annually should be estimated. The Functional Potential is the total market where the product has both fitness for use and a price range that could be acceptable. The Opportunity is defined as the probable market after adjustment for share and penetration.

ABSTRACT

[2] While this topic is discussed in the *New Venture Workbook*, the choice of an appropriate measure for management review is beyond the planning function. This section should have an evaluational focus.

C. STAKE

What is the stake to the firm for this business[3]?
Either a measure of potential or opportunity should be used. The choice depends on the accuracy of the estimates at this point in time. The appropriate measure should be identified in the previous section.

ABSTRACT

Application 1	Application 2	Confidence:
Yrs.	Yrs.	Certain 3 2 1 0 Not at all

[3] Measures of functional potential and opportunity are included in the *New Venture Workbook*.

D. SCALE

How can this business concept be viewed as the nucleus of a large business venture?

How likely is it that this larger business venture will materialize from the success of this venture?

While a profitable business of any size is always of interest, profitable, large, businesses are of greater interest. Identify possible routes of viewing this business concept as a part of a larger undertaking. Indicate the mission of this larger business, its products and customers along with the likelihood of expansion.

ABSTRACT

Application 1	
	Size:
Application 2	
	Size:

Confidence:
Certain 3 2 1 0 Not at all

E. TIME FRAME

When will the business be commercialized[4]?
Timing of commercialization is extremely difficult for new concepts. Timing of commercialization is critical for both developing a realistic estimate of stake and for developing a plan. During the concept identification phase of venture analysis, the earliest feasible commercialization date is usually used. It should be recognized that this time frame is almost always optimistic. More conservative dates are developed later as more information becomes available. If the timing of the venture is tied to outside issues, such as a specific automotive model year or a government contract date, that date should be given with appropriate citation indicating that the date is relatively fixed.

APPLICATION 1. -

APPLICATION 2. -

ABSTRACT

Application 1	Application 2	Confidence:
Yrs.	Yrs.	Certain 3 2 1 0 Not at all

[4] Included in the *New Venture Workbook*

F. RISK ASSESSMENT

What is the likelihood of success for the main application?[5]

The commercialization of new ventures is not without risk. Estimate the likelihood that each application can be commercialized at or within the time frame and at or above the estimated opportunity. Use only the main feasible applications.

Generally, the estimation is done in parts: (1) the likelihood of developing the product; (2) the likelihood of market acceptance if it is developed; (3) the likelihood of obtaining adequate management support; (4) the likelihood of meeting customers expectations within cost; and (5) the likelihood of the market responding as expected given that the product meets targeted specifications.

These probability estimates are usually considered to be independent. The collective probability is the product of these probabilities. While each of these factors may be likely to take place, the collective probability for new ventures is rarely higher than 50%.[6]

$$P_c = P_1 \times P_2 \times P_3 \times P_4 \times P_5$$

APPLICATION 1. -

APPLICATION 2. -

ABSTRACT

Probability of:	**Application 1**	**Application 2**
Developing Product	**%**	**%**
Market Acceptance	**%**	**%**
Management Support	**%**	**%**
Quality Requirements	**%**	**%**
Sales Target	**%**	**%**

[5] Included in the *New Venture Workbook*

[6] If all the factors have a 85% change of success the collective likelihood of success is only 44%.

III. RESOURCES & EXPOSURE

A. MARKET DEVELOPMENT COSTS

How much will it cost to develop these markets? How long will it take to establish the product in this market[1]?

Indicate relative time frame in years.

ABSTRACT

Application 1	**Application 2**
$	**$**

Confidence:

Certain 3 2 1 0 Not at all

[1] Included in the *New Venture Workbook*

B. R&D COSTS

How much will it cost to develop the product and processes to a level sufficient for testing feasibility?

ABSTRACT

Application 1	Application 2	Confidence:
$	$	Certain 3 2 1 0 Not at all

C. DEVELOPMENT INVESTMENT

What resources are necessary to continue the program through the next phase (obtaining necessary information)?[2]

Only include investment for the development, not for commercialization.

ABSTRACT

Application 1	Application 2	Confidence:
$	$	Certain 3 2 1 0 Not at all

[2] Covered under Development Costs in the *New Venture Workbook*

D. FRONT END EXPOSURE

What would be the loss to the firm if the concept were developed, but not commercialized?

Include all sources of loss: financial, business arrangements, commitments, and lost opportunities.

ABSTRACT

$

IV. CRITICAL ISSUES

This sub-section covers Critical Issues. In general, these are found in the areas of Product Feasibility, Market Acceptance, Production, Partnership, and/or Business Fit.

An adequate definition of Critical Issues determines the key elements of a Development Program.

Critical Issues do not have to be "bad". They are merely critical to the candidate Venture. Their proper identifications are the main determinants of a useful Action Plan.

A. CRITICAL QUESTIONS

What are the critical questions for continuing the analysis of the project?

The development program for new ventures must focus on the critical questions and issues. These questions should be listed first and revised as issues are identified.

It should be realized that the process of exploring for this information will likely change the focus of the business concept. During the early phase of business development such changes should be expected and encouraged. Few successful businesses were originally focused on products and markets that eventually were responsible for their success.

B. PATENT SITUATION

How extensive is the product patent position?
Will it give competitive advantage[1]?

The potential for basic, composition of matter, and application patents must be discussed. The relative strengths of patents are not easily assessed without court action, but estimates can be generated. The potential importance of adequate product patent protection should be covered.

How extensive is the process patent position?
Will it give competitive advantage?

The potential for patent protection for the process must be discussed. The relative strengths of patents are not easily assessed without court action, but estimates can be generated. The potential importance of adequate process patent protection should be covered.

ABSTRACT

Extremely Important	**5**	**4**	**3**	**2**	**1**	**0**	**Unimportant**
Extremely Strong	**5**	**4**	**3**	**2**	**1**	**0**	**Undefendible**

[1] Product patents have been handled separately from process patents on the *New Venture Workbook*. For evaluational purposes they should be combined as two parts of the same issue.

C. CUSTOMER COMMITMENT

Will the customer commit to purchasing the product if his expectations are met[2]?
Some "objective" means of obtaining a measure of customer commitment should be derived.

ABSTRACT

Binding Agreement 5 4 3 2 1 0 Maybe

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[2] Included in the *New Venture Workbook*

D. PARTNERSHIP

What is the potential for obtaining a development partner[3]?

A development partner is a producer or processor who will manufacture the products or services in total or in part. The intent is to use outside resources for manufacture to reduce investment and costs and to secure specific manufacturing expertise. The types of arrangements may be as simple as toll production, where the firm uses a contractor to process materials. Or it may consist of a joint venture to produce the product.

A key condition of the development partnership is that the firm maintains ownership of the product , either in part or totally, during the processing.

What is the potential for developing customer partners?

A customer partner is a user of the products or services who is willing to work with us in its development. The intent is to work with him to test the product and verify its effectiveness and quality. The customer partner is intended to act as a source of market expertise and to help promote the product

ABSTRACT

Potential Key Partner:

Formally Committed 5 4 3 2 1 0 No Response

[3] The sections on partnership in the *New Venture Workbook* explores the opportunities and requirements for such arrangements. For evaluational purposes, focus on the likelihood of such arrangements.

E. ACQUISITION POTENTIAL

Is the acquisition of one or more companies necessary for this business to be successful?
Some "objective" means of obtaining a measure of customer commitment should be derived.

F. BUSINESS FIT

1. Business Organization

What strengths and unique competitive advantages does your specific business organization provide that will assist in making you successful[4]?

Not all potentially profitable businesses should be of interest to your business group. There should be some synergy between your present business and the new venture concept to assure some competitive advantage. These need to be identified. Include: the ability to run the business, common markets, processes & facilities, technologies, and relations.

ABSTRACT

	All in Common					None-in-common
Customers:	**5**	**4**	**3**	**2**	**1**	**0**
Products:	**5**	**4**	**3**	**2**	**1**	**0**
Technologies:	**5**	**4**	**3**	**2**	**1**	**0**
Skills:	**5**	**4**	**3**	**2**	**1**	**0**
Facilities:	**5**	**4**	**3**	**2**	**1**	**0**
Structure:	**5**	**4**	**3**	**2**	**1**	**0**

[4] The *New Venture Workbook* covers competitive advantages from a corporate perspective. This section focuses on those synergies within the business group.

2. The Firm as a Whole

What strengths and unique competitive advantages does the firm have to allow you to be successful?[5]

Not all potentially profitable businesses should be of interest to the firm. There should be some synergy between the firm's existing operations and the new venture concept to assure some competitive advantage to the firm. These need to be identified. Include: the ability to run the business, common markets, processes & facilities, technologies, and relations.

ABSTRACT

Fit to Overall Business Plan:

Integral 5 4 3 2 1 0 Not a Factor

5 Included in the *New Venture Workbook*

V. MANAGEMENT

A. DECISION ELEMENTS

What are the key decisions that have to be made to continue this business concept? Are these decisions achievable in a reasonable time frame?

B. ACTION ITEMS

What information is necessary to make these decisions? **Can this information be gained at a reasonable expense and within a reasonable time frame?**

C. TIMING

When must that information be available?

By convention, we use 24 timing checkpoints per year where great precision is not available or required. This convention uses numerical split months, either A or B. For example, early September is 9A, late September is 9B, etc.

Moving from split month Action Plan Timing to split month or weekly Gantt Chart Timing is generally easy. Some imposed timing may be very precise and this should be noted.

ABSTRACT

Date for Development Decision:

D. PERSONNEL

1. Responsibility

Who is responsible?[1]

For each project element, someone should be assigned responsibility. The person assigned must be held responsible for obtaining the desired information within the time frame and resource constraints. Where possible, link authority for the execution of the project element with the responsibility of reporting results.

ABSTRACT

Project Leader:

[1] Preliminary assignments of responsibility are included in the *New Venture Workbook*. However, back-up and support people should be noted for management purposes.

2. Enthusiasm

How enthusiastic are the people involved?

Enthusiasm reflects both the confidence of the project leaders on the outcome of the project and their motivation. High confidence and motivation are critical for the success of new venture. Assess the enthusiasm of both leaders and support staff.

ABSTRACT

Technical Staff:

Highly Enthusiastic 5 4 3 2 1 0 No Energy

Management

Highly Enthusiastic 5 4 3 2 1 0 No Energy

3. Skill Sets

Do the personnel have the skills to development this business?

ABSTRACT

Technical Staff:							
Existing Skills	**5**	**4**	**3**	**2**	**1**	**0**	**All New Skills**
Management							
Existing Skills	**5**	**4**	**3**	**2**	**1**	**0**	**All New Skills**

E. AVAILABLE RESOURCES

Are the resources to develop this business likely to be available?

For each project element, someone should be assigned responsibility. The person assigned must be held responsible for obtaining the desired information within the time frame and resource constraints. Where possible, link authority for the execution of the project element with the responsibility of reporting results.

F. INTERNAL PARTNERS

What is the potential for developing internal partners?

An internal partner consists of any group of an operating division that will cooperate in the development of this business.

G. HOMES FOR THE CONCEPT

Are there other potential homes within the firm for this business concept?

Assess the advantages for the concept in each potential home and that home's impact on the likelihood of success. Note any advantages to your organization in transferring the project to the potential new home.

VI. SUMMARY SHEETS

A. DESCRIPTION AND STAKE

Products

Applications

Application 1

Application 2

Manufacturing

Marketing and Distribution

Competitive Products

Application 1

Application 2

Contribution Margin

Application 1	Application 2
%	%

Confidence:

Certain 3 2 1 0 Not at all

Measure of Stake

B. COSTS AND TIMING

Stake

Application 1	Application 2
Yrs.	Yrs.

Confidence:
Certain 3 2 1 0 Not at all

Scale

Application 1
Size:
Application 2
Size:

Confidence:
Certain 3 2 1 0 Not at all

Time Frame

Application 1	Application 2
Yrs.	Yrs.

Confidence:
Certain 3 2 1 0 Not at all

Risk Assessment

Probability of:	Application 1	Application 2
Developing Product	%	%
Market Acceptance	%	%
Management Support	%	%
Quality Requirements	%	%
Sales Target	%	%

Market Development Costs

Application 1	Application 2
$	$

Confidence:
Certain 3 2 1 0 Not at all

R&D Costs

Application 1	Application 2
$	$

Confidence:
Certain 3 2 1 0 Not at all

C. FIT AND COMMITMENT

Development Investment

Application 1 $	Application 2 $	Confidence: Certain 3 2 1 0 Not at all

Front End Exposure

$

Patent Situation

Extremely Importance 5 4 3 2 1 0 Unimportant

Extremely Strong 5 4 3 2 1 0 Undefendible

Customer Commitment

Binding Agreement 5 4 3 2 1 0 Maybe

Partnership

Potential Key Partner:

Formally Committed 5 4 3 2 1 0 No Response

Business Fit

	All in Common					None-in-common
Customers:	5	4	3	2	1	0
Products:	5	4	3	2	1	0
Technologies:	5	4	3	2	1	0
Skills:	5	4	3	2	1	0
Facilities:	5	4	3	2	1	0
Structure:	5	4	3	2	1	0

Fit to Overall Business Plan:

Integral 5 4 3 2 1 0 Not a Factor

Timing

Date for Development Decision:

D. PERSONNEL

Responsibility

Project Leader:

Enthusiasm

Technical Staff:

Highly Enthusiastic 5 4 3 2 1 0 No Energy

Management

Highly Enthusiastic 5 4 3 2 1 0 No Energy

Skill Sets

Technical Staff:

Existing Skills 5 4 3 2 1 0 All New Skills

Management

Existing Skills 5 4 3 2 1 0 All New Skills

GLOSSARY

Many of the terms used in this workbook have broader definitions than are intended here. The following definitions refer to this New Venture Workbook.

Acquisition An existing independent business purchased out-right by the firm. Joint ventures are considered here to be a type of partnership. The nature of the joint venture agreement may extend beyond a development agreement to that of an acquisition. In any case, joint ventures and acquisitions require Departmental and Corporate approval.

Applications An application is defined as a group of uses which have separate and identifiable customer benefits. It is synonymous with a market segment as used in this workbook.

Business Fit Business fit refers to the potential synergy between the business concept and other businesses. Fit focuses on mutually supporting strengths.

Business Opportunity The business opportunity is the total opportunities for all applications.

Contribution Margin The contribution margin is the proportion of the price that exceeds the variable costs. It is a measure of the inherent profitability of the product and services. It should be noted, however, that there are additional costs that will be set against the contribution. Contribution margins of over 50% are generally expected for a concept to be considered viable.

Customer Commitment For new venture analysis, customer commitment focuses on his intention to buy the product. It is recognized that that intention may not become reality.

Distribution Distribution refers to all means of getting the product to the ultimate user. This may include several levels of customers.

Marketing Marketing is the function of encouraging the customer to use the product. This function includes sales and promotion.

Markets The collection of all potential customers for the product and services is referred to as the product markets. As used in this workbook, markets consist of applications.

Opportunity It is unlikely that any business will capture 100% of a market. Opportunity reflects the likely fraction of the price-adjusted functional potential that is realistically capturable by this business.

Partnership

Any agreement with an outsider organization or other internal organization involving working together in the development of this business is a partnership. This may be either formal or informal in nature.

Potential

In general the potential refers to the largest possible annual sales of the product. Potential as used in this workbook refers to <u>the functional potential</u>.

Functional potential includes all feasible markets for which the product is fit for use and is within the acceptable price range.

Product

Product, as used in this workbook, is synonymous with the product offering. It includes all physical products, services, and attributes as delivered to the customers.

Resource

A resource consists of manpower, funds and special facilities needed to continue the development of a business concept.

Risk

Risk reflects all the possibilities of things that can go wrong in the development of the business. For this workbook, risk refers to the collective probability of success.

Stake

The stack reflects the economic value of the business to the firm. There are a number of measures of stake that can be used. In the New Venture Workbook, stake is synonymous with market potential and opportunity. Other measures can be used, if appropriate.

Target Price

Target price is the proposed price for the products. It is understood that this is only an estimated price. It must be consistent with the estimate of the functional potential. A high target price should restrict the product's uses. A low target price would provide a larger market but at a restricted contribution margin.

Variable Costs

Variable or marginal costs refer to those unit costs directly attributed to making an additional unit (of product and service). All overhead, burden, and investment charges are excluded from variable costs.